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**STATE BOARD OF EQUALIZATION**

October 4, 1994

In the Matter of the Petition	)	
for Redetermination Under the	)	DECISION AND RECOMMENDATION
Sales and Use Tax Law Of:	)	
	)	No.
<u>Petitioner</u>	)	

The Appeals conference in the above-referenced matter was held by Senior Staff Counsel Stephen A. Ryan on August 15, 1994 in Torrance, California.

Appearing for Petitioner:

Appearing for the  
Sales and Use Tax Department:

Mr. Herb Nemec  
Tax Auditor

Mr. Pete Elash  
Supervising Tax Auditor

Protested Item

The protested tax liability for the period July 1, 1988 through December 31, 1990 is measured by:

	<u>Item</u>	<u>State, Local and county</u>
A.	Gross receipts from retail sales- disallowed deductions	\$569,848

Petitioner's Contentions

1. Sales of ice cubes are exempt as bottled water pursuant to Revenue and Taxation Code section 6359.6.
2. Sales of dry ice are exempt pursuant to Revenue and Taxation Code section 6359.7.

Summary

Petitioner is identified by the Board's Sales and Use Tax Department ("Department") as a caterer of meals and sodas to foreign airlines. This was the first audit.

Petitioner had claimed deductions on its sales tax returns for all its reported gross receipts on grounds of Revenue and Taxation Code section 6385. The Department allowed exemption for the sales of food (pursuant to Revenue and Taxation Code section 6359.1), but not for the gross receipts

derived from the sales of sodas, dry ice, or ice cubes. Petitioner disputes the tax determined on the receipts from its sales of ice cubes (\$307,205), and dry ice (\$58,922). Petitioner did not obtain any resale certificates, exemption certificates, bills of lading, airway bills, or other similar records regarding the dry ice or ice cubes sold.

The ice cubes consisted of 50-pound bags of small ice cubes for use in cold drinks served by the foreign airlines to their passengers during the next flight which was always to leave California on a trip to an out-of-state location.

The dry ice was packaged together by petitioner with the containers of food prior to delivery to the foreign airline purchasers. This dry ice helped keep the food from spoiling prior to service by the airline to the passengers during the next flight which was always to an out-of-state destination.

### Analysis and Conclusions

Petitioner was required to keep records showing all deductions claimed on its sales tax returns (Regulation 1698 (a) (2)). The taxpayer also has the burden to prove the applicability of any sales tax exemption (Standard Oil Co. v. State Board of Equalization (1974) 39 Cal.App.3d 765, 769).

Petitioner claimed exemption on its sales tax returns for the \$366,127 in dispute on the basis of Revenue and Taxation Code section 6385. That exemption was limited to situations in which: (1) the property sold was transported by the foreign carrier "to a foreign destination"; (2) a writing, such as a bill of lading, evidenced that transportation of cargo to a foreign destination; and (3) the carrier timely delivered an exemption certificate to the seller. None of those three requirements was met in petitioner's situation, and thus no such exemption.

Receipts from the sale of food products for human consumption, including bottled water, are exempt from sales tax pursuant to Revenue and Taxation Code section 6359 (b) (3). Bottled water sales have also been treated by the Legislature in Revenue and Taxation Code section 6359.6 which provides for a sales tax exemption for the receipts from sales of non-carbonated and non-effervescent bottled water in containers of at least one-half gallon.

Petitioner's sales of the frozen ice cubes do not qualify for exemption as bottled water pursuant to Revenue and Taxation Code section 6359.6 as alleged by petitioner. That exemption expressly is limited to bottled water in containers of at least one-half gallon. Small frozen water ice cubes in 50-pound bags do not constitute bottled water. Similarly, the frozen ice cubes are not food products of the "bottled water" type under section 6359 (b) (3). Further, as discussed below, since the Legislature has also provided for certain exemptions for ice, there is strong evidence of Legislative intent that the bottled water exemptions are inapplicable to ice cubes.

Petitioner is however relieved of sales tax liability for a portion of its receipts from sales of the ice cubes which were resold by the airlines to passengers who paid for drinks containing those ice cubes (see attached exhibit 1 of Annotation 325.0670 [2/8/71] which was effective during this

audit period; and exhibit 2 of the opinion letter upon which Annotation 280.0260 [11/19/63] is based). This nontaxable portion needs to be established and deleted from the deficiency. The Department also needs to establish (probably by reasonable estimate) and delete from this deficiency the portion of the undisputed \$203,721 measure which represent the income from petitioner's sales of soda which was also similarly resold by the airlines. The other ice cubes provided by the airlines to passengers with complimentary drinks were not sold by the airlines, but rather consumed by the airlines (Annots. 280.0260 and 325.0670). Petitioner is thus liable for sales tax on the retail sale of the ice cubes consumed by the airlines by way of complimentary drinks for passengers.

Petitioner claims exemption pursuant to Revenue and Taxation Code section 6359.7 which reads as follows:

"As incidental to the exemption provided for in Section 6359, there are exempted from the taxes imposed by this part the gross receipts from the sale of and the storage, use, or other consumption in this state of ice or dry ice used or employed in packing and shipping or transporting food products for human consumption when the food products are shipped or transported in intrastate, interstate, or foreign commerce by common carriers, contract carriers, or proprietary carriers."

This statute was effective January 1, 1986. Revenue and Taxation Code section 6359.5, which was effective from 1945 for ice and from 1954 for dry ice, through a 1979 repeal, read as follows:

"As incidental to the exemption provided for in Section 6359, there are exempted from the taxes imposed by this part, the gross receipts from the sale of and the storage, use, or other consumption in this State of ice or dry ice used or employed in packing and shipping or transporting food products for human consumption between a point or points within and a point or points without this State."

That old version for exemption of ice and dry ice sales for use in transporting food was thus for food which was being shipped from California to an out-of-state "point". Whether "point" was a point in the air or a place on land was not expressly indicated, but the Board has interpreted "point" to mean a place on land with that exemption limited to situations when the food was cargo being shipped along the entire route from California to the out-of-state destination city (see Annot. 400.0240 [4-18-55] which reads as follows: "Dry ice sold and used in refrigerating food served as meals on aircraft is not within the exemption of Section 6359.5. The statutory exemption only applies in cases where food products are shipped as cargo in the usual sense to an out-of-state destination." [Emphasis added.] ).

The language in the old and new versions of section 6359.7 does not list an out-of-state "point", land, destination, or city. It merely identifies the shipment/transportation in commerce by a

carrier. It is still, however, the interpretation of the Board's Legal Section that this current exemption is similar to the Board's interpretation of the prior exemption in that the food must be cargo shipped along the entire route from California to the first out-of-state destination-city, rather than merely carried only part way for consumption by passengers during that first outbound flight (see attached exhibit 3, which is an opinion memorandum of the Board's Legal Section on this issue). Therefore, it is the opinion of this Appeals Review Section that the dry ice sold by petitioner for the treatment of food to be consumed onboard the outbound flights does not qualify petitioner for exemption pursuant to section 6359.7.

Since the foreign air carriers used and consumed the dry ice without reselling it, petitioner made the retail sales and incurred sales tax on its gross receipts (Good Humor Co. v. State Board of Equalization (1957) 152 Cal.App.2d 873).

#### Recommendation

Grant in part to delete the to-be-estimated portion of receipts derived from sales of ice cubes resold as described herein. No other adjustments are recommended.

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Stephen A. Ryan, Senior Staff Counsel

10-4-1994  
Date

(w/ Exhibits 1, 2 and 3)

Annotation 325.0670

Liquor Served to Purchasers Aboard Aircraft. Liquor sold or served free of charge aboard aircraft in airspace within the boundaries of California is subject to sales or use tax. The airspace within these boundaries in "within the state" for purposes of the Sales and Use Tax Law. 2/8/71

Elizabeth Abreu  
Tax Counsel

May 15, 1992

Request for Legal Opinion

This is in response to your memorandum dated February 5, 1992. You state that the above-referenced taxpayer sells meals, soft drinks, ice, and dry ice exclusively to foreign airlines. Dry ice is used to preserve the meals until served to passengers. The taxpayer's representative asserts that the exemption in Revenue and Taxation Code Section 6359.7 applies to the sales of dry ice.

Section 6359.7 reads:

“As incidental to the exemption provided for in Section 6359, there are exempted from the taxes imposed by this part the gross receipts from the sale of and the storage, use, or other consumption in this state of ice or dry ice used or employed in packing and shipping or transporting food products for human consumption when the food products are shipped or transported in intrastate, interstate, or foreign commerce by common carriers, contract carriers, or proprietary carriers.”

Annotation 400.0240, which was issued \_\_\_\_\_ provides that dry ice used in refrigerating meals on aircraft is not within in section 6359.5 exemption. (Section 6359.5 was identical to section 6359.7 except that the last clause of 6359.7, beginning with “when the food products are shipped...” read “between a point or points within and a point or points without this State.”) The letter underlying this annotation concluded that food served as meals on the aircraft was not being “shipped” or “transported” in the sense intended by the statute since the food was not being shipped or transported as cargo in the usual sense. We believe that the conclusion in this annotation is correct and that dry ice used to refrigerate meals served on the airlines is not exempt under section 6359.7.