

REVENUE DEPARTMENT[701]

Regulatory Analysis

Notice of Intended Action to be published: Iowa Administrative Code 701—Chapter 206
“Bundled Transactions”

Iowa Code section(s) or chapter(s) authorizing rulemaking: 421.14, 422.68, and 423.42
State or federal law(s) implemented by the rulemaking: Iowa Code section 423.2

Public Hearing

A public hearing at which persons may present their views orally or in writing will be held as follows:

October 25, 2023
9 a.m. to 12 noon

Via video/conference call:
meet.google.com/cox-brcn-tok?hs=122&authuser=0

Public Comment

Any interested person may submit written or oral comments concerning this Regulatory Analysis. Written or oral comments in response to this Regulatory Analysis must be received by the Department of Revenue no later than 4:30 p.m. on the date of the public hearing. Comments should be directed to:

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P.O. Box 10457
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Purpose and Summary

The purpose of this proposed rulemaking is to readopt Chapter 206. This chapter was recently updated, and the Department has determined that it does not contain language that is obsolete, unnecessary, or duplicative of statutory language. The chapter describes the Department’s interpretation of the underlying statute to help the public understand the taxability of bundled transactions. The rules reduce uncertainty about how tax applies when items are sold together.

Analysis of Impact

1. Persons affected by the proposed rulemaking:
 - Classes of persons that will bear the costs of the proposed rulemaking:
The proposed rules do not create costs for any class of persons.
 - Classes of persons that will benefit from the proposed rulemaking:
The public, including retailers and purchasers, will benefit from clarification about the taxability of bundled transactions.

2. Impact of the proposed rulemaking, economic or otherwise, including the nature and amount of all the different kinds of costs that would be incurred:
 - Quantitative description of impact:
There is no economic impact of the proposed rules.
 - Qualitative description of impact:
These rules reduce uncertainty about the taxability of bundled transactions. Failing to adopt them would lead to confusion, questions to the Department, and potential errors in calculating taxation of bundled transactions.

3. Costs to the State:
 - Implementation and enforcement costs borne by the agency or any other agency:
There are no costs to the agency of implementing the rules beyond those that would otherwise be required to administer the statute.

- Anticipated effect on state revenues:

There is no anticipated effect on state revenues. However, the rules clarify the taxability of bundled transactions, making it more likely that the correct amount of tax will be remitted.

4. Comparison of the costs and benefits of the proposed rulemaking to the costs and benefits of inaction:

There are no costs of the rules themselves. The cost of inaction would be confusion about the taxability of bundled transactions.

5. Determination whether less costly methods or less intrusive methods exist for achieving the purpose of the proposed rulemaking:

The proposed rulemaking is not costly or intrusive. The purpose of the rules is to provide guidance on the taxability of bundled transactions. The Department considered the option of not having rules explaining the taxability of bundled transactions but determined that the rules provide useful clarification to the public.

6. Alternative methods considered by the agency:

- Description of any alternative methods that were seriously considered by the agency:

The Department considered the possibility of not providing rules on this topic but determined that it provides useful guidance to the public beyond what is provided by statute.

- Reasons why alternative methods were rejected in favor of the proposed rulemaking:

Proceeding without these rules would lead to confusion about how to tax bundled transactions.

Small Business Impact

If the rulemaking will have a substantial impact on small business, include a discussion of whether it would be feasible and practicable to do any of the following to reduce the impact of the rulemaking on small business:

- Establish less stringent compliance or reporting requirements in the rulemaking for small business.
- Establish less stringent schedules or deadlines in the rulemaking for compliance or reporting requirements for small business.
- Consolidate or simplify the rulemaking's compliance or reporting requirements for small business.
- Establish performance standards to replace design or operational standards in the rulemaking for small business.
- Exempt small business from any or all requirements of the rulemaking.

If legal and feasible, how does the rulemaking use a method discussed above to reduce the substantial impact on small business?

The rulemaking does not have a substantial impact on small business. The rules do not make any special distinctions for small businesses. The rules do not impose any requirements on businesses, other than taxation requirements imposed by the underlying statutes.

Text of Proposed Rulemaking

ITEM 1. Rescind 701—Chapter 206 and adopt the following **new** chapter in lieu thereof:

CHAPTER 206 BUNDLED TRANSACTIONS

701—206.1(423) Taxability of bundled transactions. The sales price of a bundled transaction is subject to tax if any product included in the bundled transaction would be taxable if sold separately. For purposes of this rule, products include tangible personal property, services, and specified digital products and exclude real property and services to real property.

701—206.2(423) Bundled transaction. A “bundled transaction” is the retail sale of two or more products where the products are otherwise distinct and identifiable and the products are sold for one nonitemized price.

206.2(1) Distinct and identifiable product. “Distinct and identifiable product” does not include any of the following:

a. Packaging or other materials that accompany the retail sale of the products and are incidental or immaterial to the retail sales of the products. Packaging or other materials include but are not limited to containers, boxes, sacks, bags, bottles, envelopes, wrapping, labels, tags, twine, garment hangers, and instruction guides.

EXAMPLE 1: Seller Z provides paper and plastic bags for purchasers to use to carry away their purchased items. The bags are incidental or immaterial to the retail sales of the products and are not distinct and identifiable products. Seller Z's retail sale of purchased items in the provided bags does not constitute a bundled transaction.

EXAMPLE 2: Seller X sells brownies and offers purchasers the option of adding a premium box for an increased price. The sales price of the brownies is the same whether they are sold on their own or with a standard box, but the total sales price increases if the purchasers select a premium box. The premium box is distinct and identifiable from the food product because it requires separate shopping preferences and product selection by the purchaser and is not standard with every order of food product. The retail sale of the brownies and the premium box may constitute a bundled transaction if the other requirements pursuant to Iowa Code section 423.2(8) are satisfied.

EXAMPLE 3: Seller A offers purchasers the option to buy reusable, long-lasting grocery bags to use to carry away purchased grocery items. If the reusable grocery bags are purchased with other items and separately itemized, they are taxable and the sale does not constitute a bundled transaction.

b. A product that is provided free of charge to the consumer in conjunction with the required purchase of another product, if the sales price of the other product does not vary depending on whether the product provided free of charge is included in the transaction. Examples include a free car wash with the purchase of gasoline or free dinnerware with the purchase of groceries.

c. Items specified in the definition of "sales price" in Iowa Code section 423.1.

206.2(2) One nonitemized price. "One nonitemized price" does not include the following:

a. A price that is separately identified by product on a binding sales document, or other sales-related documentation, that is made available to the customer in paper or electronic form, including but not limited to an invoice, a bill of sale, a receipt, a contract, a service agreement, a lease agreement, a periodic notice of rates and services, a rate card or a price list.

b. A price for which the sales price varies or is negotiable based on the purchaser's selection of the products included in the transaction even if the seller only provides one price on its invoice to the purchaser.

EXAMPLE 1: Seller A sells a bakery item as part of a meal which consists of taxable prepared food. The purchaser selects items from a list of options of prepared food to be included in the meal. The individual items of the meal are not itemized on the receipt and the meal is always the same price, notwithstanding the items selected by the purchaser. The meal is sold for one nonitemized price, and the sales price of the meal is subject to tax as a bundled transaction.

EXAMPLE 2: Seller B enters into a contract with buyer D to provide various information technology services. Buyer D selects the information technology services it wants from seller B. Through negotiation, buyer D and seller B agree on a price based on the services selected and seller B bills buyer D one price for all of the services, some of which are taxable and some of which are not taxable. Although the invoice from seller B to buyer D only contains one price for all of the services, since the price was based on the products selected by buyer D, the price is not one nonitemized price and the sale does not constitute a bundled transaction.

701—206.3(423) Transactions not taxable as bundled transactions. Generally, the entire sales price from a bundled transaction is subject to sales tax. However, the transactions described in this rule are not taxable as bundled transactions.

206.3(1) Sales involving mixed tangible personal property and services. The retail sale of tangible personal property or specified digital product and a service, if the tangible personal property or specified digital product is essential to the use of the service, and provided exclusively in connection with the service, and if the true object of the transaction is the service.

EXAMPLE: Seller A charges customer B for computer programming services where customer B is also given a backup disk and instruction manual. The true object of the transaction is the provision of the programming services. Seller A is selling nontaxable services and is not making a sale of a bundled transaction. Iowa sales tax is not due on the programmer's charge for services; sales tax is due on seller A's purchases of tangible personal property used to fulfill the service.

206.3(2) Sales involving services. The retail sale of services, if one of the services is essential to the use or receipt of a second service, and provided exclusively in connection with the second service, and if the true object of the transaction is the second service. If the transaction is not a bundled transaction as a result of this exclusion, then the true object of the transaction will be the retail sale of the second service and should be taxed accordingly.

206.3(3) True object test. The true object of a transaction is the main product that is the subject of the transaction. Determining the true object of a transaction is a fact-based inquiry and shall be made on a case-by-case basis. Factors that may be considered in determining the true object of a transaction include but are not limited to the nature of the seller's business and purchaser's reason for making the purchase.

206.3(4) Sales involving de minimis taxable products. A transaction that includes taxable and nontaxable products and the seller's purchase price or sales price of the taxable products is de minimis. "De minimis" means the seller's purchase price or sales price of the taxable products is 10 percent or less of the total purchase price or sales price of the bundled products. A seller shall use either the seller's purchase price or seller's sales price of the products to determine whether the taxable products are de minimis. A seller may not use a combination of the seller's purchase price and seller's sales price of the products to determine whether the taxable products are de minimis.

EXAMPLE 1: Seller H sells a coupon book that includes a packet of stickers for one nonitemized price of \$75. The packet of stickers is not provided free of charge. Seller H purchased the stickers, a taxable product, for \$2 per packet, which does not exceed 10 percent of the total purchase price of the coupon book and stickers. Seller H's sale of the coupon book and stickers is not a bundled transaction, and the sales price of \$75 is not subject to tax.

EXAMPLE 2: Technology Company F (company F) sells access to a day-long live webinar about the latest trends occurring in the technology industry for one nonitemized price of \$200. The webinar, which does not allow people viewing the presentation to submit questions, is not subject to Iowa sales tax. The customer also receives a smartwatch that is included in the payment of the webinar but is not provided free of charge. Company F's sales price of the smartwatch is \$50, which exceeds 10 percent of the total sales price of the fee. The watch is subject to sales tax by the customer. Because company F's purchase price of the watch is not de minimis, the \$200 transaction is a bundled transaction and is subject to tax.

206.3(5) Sales involving taxable and exempt food or medical products. The retail sale of exempt tangible personal property and taxable tangible personal property where all of the following apply:

a. The transaction includes food and food ingredients, drugs, durable medical equipment, mobility enhancing equipment, prosthetic devices, or medical supplies; and

b. The seller's purchase price or sales price of the taxable tangible personal property is 50 percent or less of the total purchase price or sales price of the bundled tangible personal property. Sellers may not use a combination of the purchase price and sales price of the tangible personal property when making the 50 percent determination for a transaction.

EXAMPLE: Seller F offers its customers a package containing two prepared hot dogs and five frozen hot dogs. The sales price for the two prepared hot dogs is \$5, and the sales price of the five frozen hot dogs is \$10. The package is sold for one nonitemized price of \$15. The sales price of the package is not taxable because the sales price of the taxable items (the two prepared hot dogs) is 50 percent or less of the total sales price of the package.

These rules are intended to implement Iowa Code section 423.2(8).