

Cite as Det. No. 15-0249, 35 WTD 225 (2016)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Correction of)	<u>D E T E R M I N A T I O N</u>
Assessment of)	
)	No. 15-0249
)	
...)	Registration No. . . .
)	

WAC 458-20-183; RCW 82.04.4282: B&O TAX – DEDUCTION – MEMBERSHIP FEES AND DUES – MARTIAL ARTS TRAINING CENTER. A martial arts training center that provides its members the benefits of martial arts training and use of its facilities in exchange for membership dues may deduct the portion of its dues income representing dues solely for the privilege of membership, and not for any significant goods or services. RCW 82.04.4282. If the taxpayer is unable to submit evidence of dues solely for the privilege of membership, the Department may presume that the entire amount of dues income is taxable. WAC 458-20-183(4).

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

Eckholm, A.L.J. – A non-profit organization that operates a martial arts training center appeals the denial of the RCW 82.04.4282 deduction it claimed for its membership dues income, asserting that the dues are deductible donations. The taxpayer’s petition is denied.¹

ISSUE

Whether income from membership dues paid in exchange for martial arts training qualifies for deduction under RCW 82.04.4282.

FINDINGS OF FACT

[The taxpayer] is a nonprofit corporation that operates a martial arts school on a membership basis. The taxpayer’s home page describes itself as [a unique and intense approach to external martial arts, offers classes five days a week, and offers a two-week membership trial period where a prospective member can attend classes for free.]

(Emphasis in original.)

¹ Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

The taxpayer's "about us" page describes the types of classes it offers and its unique martial arts training. The "about us" page also refers to the availability of the first two weeks free, but contains no mention of a voluntary donation based membership, or any mention of volunteer or community services. The taxpayer's membership sign-up application requires an applicant to choose a membership package with an associated monthly fee. The application also includes the choice of "sliding scale" payment with specific instructions [that only those who have communicated with an officer of the organization in advance may make that selection.]

The application also provides a separate instruction [that] a tax deductible donation [is made "in addition to your monthly dues."]

(Underline emphasis added.)

The Department of Revenue (Department) Audit Division reviewed the taxpayer's records for excise tax purposes for the period January 1, 2010 through December 31, 2013. The taxpayer's records evidenced income from yearly membership fees, monthly dues, outreach program fees, retreat advance payments, sign-up specials, testing fees, and floor rental storage. During the audit period, the taxpayer had reported income from the described income sources and then deducted all of its income as bona fide fees and dues, and donations, pursuant to RCW 82.04.4282. The auditor noted that the taxpayer's webpage regarding membership during the audit indicated as follows:

Initiation Fees	Membership Fees	Monthly Dues
Adults \$. . .	Kids and students: \$. . . /yr	Adults: \$. . . /month
Juniors \$. . .	Adults: \$. . . /yr	Junior (13-17) \$. . . /month
Kids \$. . .	Family: \$. . . /yr	Kids (under 13) \$. . . /month
	Benefactor: \$. . . /yr	

After reviewing the taxpayer's records, its website, and other information collected during the audit, the auditor concluded that the taxpayer offered martial arts training services in exchange for dues and fees; therefore, the taxpayer was denied the deduction under RCW 82.04.4282 because the dues were in exchange for goods and services, and were not solely paid for the privilege of membership. As a result, the Department assessed unpaid taxes, interest, and an assessment penalty, in the total amount of \$² In calculating the assessment, the auditor excluded lump sum monthly donations from taxable income where the taxpayer could show that the amounts were not in exchange for goods or services.

The taxpayer appealed the assessment, and asserted that its organization operates on a donation basis, all classes are offered for free to the community, the instructors and all employees are

² Document No. . . . , issued August 19, 2014, for the period January 1, 2010 through December 31, 2013, included assessments of retail sales tax of \$. . . , service and other activities business & occupation (B&O) tax of \$. . . , a small business credit of \$. . . , and interest of \$. . . , for a total amount assessed of \$ A balance due notice that overlapped the 2013 period had previously been issued to the taxpayer, in the amount of \$. . . , and was not included in the assessment issued August 19, 2014. The total amount at issue in this appeal is \$ For the audit period, the taxpayer's dues income was classified under the service and other activities B&O tax classification. Effective January 1, 2016, the sale of martial arts training at an "athletic or fitness facility" constitutes a retail sale under RCW 82.04.050(3)(g), taxable as a retailing activity. Laws of 2015, ch. 169, § 1.

volunteers, and all funds collected are utilized for outreach programs in the community. The taxpayer asserted that its membership dues are deductible as donations under RCW 82.04.4282 and are paid in exchange solely for the privilege of membership. In support of the taxpayer's contention that the classes are offered for free, the taxpayer provided two affidavits with its appeal petition indicating that the affiants were allowed to take classes without paying membership dues.

Following the audit, the taxpayer changed its membership webpage to [include a "pay what you choose" option for membership that suggested payment of the quoted monthly membership fee amounts because those amounts are reasonable and cover the organization's monthly operating expenses.]

At the hearing the taxpayer indicated that the Audit Division had approved the taxpayer's change in phrasing on its membership webpage as supporting a donation-based organization. The Audit Division indicated it did not provide such approval and that it specifically informed the taxpayer it would not offer such approval.

ANALYSIS

The business and occupation tax is imposed for the privilege of engaging in business in Washington. RCW 82.04.220. The term "business" includes "all activities engaged in with the object of gain, benefit, or advantage to the taxpayer or another person or class, directly or indirectly." RCW 82.04.140. The measure of the tax is the gross proceeds of sales, value proceeding or accruing, or gross income of the business. RCW 82.04.220. Washington's Revenue Act contains no general exemption from taxation for non-profit organizations. *See* WAC 458-20-169 (Rule 169). Unless a specific deduction or exemption applies, B&O tax is imposed on the business income of nonprofit organizations. Exemptions and deductions from tax are narrowly construed, and the party claiming the deduction has the burden of showing that it qualifies for the deduction. *See, e.g., Budget Rent-A-Car, Inc. v. Dep't of Revenue*, 81 Wn.2d 171, 174-175, 500 P.2d 764 (1972).

The taxpayer asserts that its dues income is nontaxable under the statutory deduction for certain initiation fees, dues, contributions and donations, RCW 82.04.4282, because the dues are donations paid solely for the privilege of membership. However, RCW 82.04.4282 specifically provides that the deduction does not apply "[i]f dues are in exchange for any significant amount of goods or services rendered by the recipient thereof" The purpose of the dues deduction is to exempt from taxation only revenue exacted for the privilege of membership. *Automobile Club v. Dep't of Revenue*, 27 Wn. App. 781, 786-87, 621 P.2d 760 (1980). A taxpayer may deduct those portions of its dues income [representing dues solely for the privilege] of membership, [and not for any significant goods or services]. *Id.* If the taxpayer is unable to submit evidence of [dues solely for the privilege of membership], the Department may presume that the entire amount of dues income is taxable. *Id.*; *see* WAC 458-20-183(4) (Rule 183(4)).

Here, the taxpayer provides its members with the benefits of martial arts training and use of its facilities in exchange for dues. The members do not pay any additional charges for these benefits; therefore, any amounts of dues paid in exchange for these goods and services are not

deductible from taxable income under RCW 82.04.4282. The taxpayer has not asserted any other privileges of membership provided in exchange for the dues. The taxpayer's expenses from operating its training facility are supported by the dues paid by its members. The taxpayer has not established that any portion of its dues is used solely for the privilege of membership; therefore, its income from dues is not deductible under RCW 82.04.4282. *Automobile Club*, 27 Wn. App. at 786-87; Rule 183(4).

The taxpayer also asserts that the membership dues are deductible under RCW 82.04.4282 as donations. Funds do not qualify as "contributions" or "donations" if the funds are not provided for a gratuitous purpose. Det. No. 13-0156R, 33 WTD 199, 202 (2014) citing *Analytical Methods v. Dep't of Revenue*, 84 Wn. App. 236, 243, 928 P.2d 1123 (1996). The court in *Analytical Methods* noted that RCW 82.04.4282 does not define "contributions" and "donations," and looked to dictionary definitions to define the terms:

"Contribution" means "a sum or thing voluntarily contributed." WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 496 (1966). "Contribute" means "to give or grant in common with others (as to a common fund or for a common purpose)." WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 496 (1966). . . . "Donation" means "the action of making a gratuitous gift or free contribution." WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 672 (1966). These definitions require a gratuitous purpose

Analytical Methods, 84 Wn. App. at 243.

Here, the taxpayer provides martial arts training in exchange for membership dues; therefore, the dues are not given gratuitously.

To assist in interpreting the use of the term "donation" in RCW 82.04.4282, the Department has also looked to the definition of donation in WAC 458-20-169(5)(g)(iii), the rule that defines what constitutes a contribution or donation for purposes of exempt fund raising activity by a non-profit organization under RCW 82.04.3651. 33 WTD at 202. Rule 169(5)(g)(iii) provides:

(iii) Contributions of money or other property. The term contributions includes grants, donations, endowments, scholarships, gifts, awards, and any other transfer of money or other property by a donor, provided the donor receives no significant goods, services, or benefits in return for making the gift. For example, an amount received by a nonprofit educational broadcaster from a group that conditions receipt upon the nonprofit broadcaster airing its seminars is not a contribution regardless of how the amount paid was titled by the two organizations.

(Emphasis added.)

The membership dues paid by the taxpayer's members are not paid to the taxpayer as gifts, but are paid in exchange for martial arts training services and the use of the taxpayer's martial arts training facility; therefore, the membership dues would not qualify as donations or contributions under Rule 169(5)(g)(iii).

The taxpayer asserts that because it does not require that members actually pay membership dues to receive the martial arts training that the membership dues that are collected should be considered donations. Based on the available information regarding the taxpayer's organization, as described above, the Department finds that the membership dues are not gratuitous donations and the taxpayer does not operate its business on a donation basis. The taxpayer's membership application lists different membership packages, the associated monetary dues level, and requests a donation from a member "in addition to your monthly dues."³ The taxpayer actually distinguishes between donations and dues. Though the application references a "sliding scale" selection, the selection of such reduced pricing is subject to communication with officers of the taxpayer's organization and the webpage indicates that the member must enter "the immediate amount you've agreed to pay," and instructs the member to "please enter the amount of the first installment here."⁴ Similarly, the taxpayer's revised membership page provides that unlimited classes are provided in exchange for membership dues.⁵

In addition, the taxpayer offers two weeks of unlimited free classes to individuals interested in trying out the taxpayer's classes when considering whether to become a member. If membership and attending the classes is free, as asserted by the taxpayer, then it would be unnecessary to grant two weeks of free classes to prospective members to assist them in determining whether to become members. Though the taxpayer's new membership webpage refers to "suggested donations" to support membership, and contains an asterisk footnote at the bottom of the page that provides "a donation in any amount, including nothing," may be made, these indicators do not support the conclusion that membership is not a paid membership.⁶ The taxpayer is clearly communicating that membership to its organization is a paid membership and that membership dues are provided in exchange for martial arts instruction.

Even if the Department were to accept the taxpayer's assertion that the dues are provided as donations only, the fact remains that individuals are accorded membership in exchange for the asserted donations and membership accords the benefit of martial arts training. The membership dues are paid in exchange for the benefit of martial arts training; therefore, the taxpayer's income from membership dues is not deductible under RCW 82.04.4282. The taxpayer's petition is denied.

DECISION AND DISPOSITION

The taxpayer's petition is denied.

Dated this 9th day of September, 2015.

³ . . .

⁴ *Id.*

⁵ . . .

⁶ *Id.*