Cite as Det. No. 13-0270, 33 WTD 18 (2014)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

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| In the Matter of the Petition for Correction of Assessment of<br><br>. . . | ) | D E T E R M I N A T I O N<br><br>No. 13-0270<br><br>Registration No. . . .<br><br>Docket No. . . . |

[1] RCW 82.04.050(3); WAC 458-20-183: RETAILING B&O TAX AND RETAIL SALES TAX – PHYSICAL FITNESS SERVICES. Taxpayer's "crossfit" classes focus primarily on exercise and are therefore are retail fitness services

[2] RCW 82.32A.020; RCW 82.32A.030: TAXPAYER RIGHTS AND RESPONSIBILITIES. Taxpayer has the right to rely on specific written tax reporting instructions from the Department. Taxpayer has the responsibility to seek instructions from the Department when uncertain about its tax reporting obligations. Taxpayer was neither given specific written instruction nor did it seek specific written tax reporting instructions from the Department.

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.

Lewis, A.L.J. – Taxpayer, a business that provides "crossfit" training, disputes re-classification of its income from the service and other activities business and occupation ("B&O') tax classification to the retailing B&O and retail sales tax classifications. Taxpayer maintains the services it offers are primarily instructional in nature and distinguishable from retail physical fitness services offered by regular "gyms". We conclude that improving and maintaining physical conditioning was the primary focus of the classes at issue and sustain the assessment of tax on this income as retail physical fitness services. Taxpayer's petition is denied.[1]

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

ISSUES:

1. Whether the income Taxpayer receives from providing "crossfit" instruction and training to its customers constitutes physical fitness services subject to payment of retailing B&O tax and collection of retail sales tax under RCW 82.04.050(3) and WAC 458-20-183(3)?

2. Even if the income was correctly reclassified, is the Department prevented from making the tax adjustment based on alleged tax reporting confusion within the industry and Department?

FINDINGS OF FACT:

Taxpayer derives income from offering fitness training. Taxpayer's customers are initially taught and trained how to exercise in a safe manner that emphasizes form, which maximizes the benefits of the exercise. As Taxpayer's customers become more knowledgeable and skilled they are instructed in using components of Olympic weight training, gymnastics, Pilates, and martial arts. Taxpayer made clear that customers do nothing in her facility without trainer supervision.

Taxpayer registered with the Department on . . . 2006. Taxpayer began reporting income under the service and other activities B&O tax classification. Subsequently, the Department's Audit Division audited Taxpayer's business records for the period January 1, 2008 through December 31, 2011. On July 26, 2012 the Department issued two assessments. One assessment for $. . . represented tax, interest and penalty assessed on the purchase of assets and supplies used in the business.[2] The Department also issued a second assessment for $. . . arising from the reclassification of Taxpayer's income from the service and other activities B&O tax classification to the retailing B&O and retail sales tax classifications. The Audit Division made the reclassification of income, concluding that the income was derived from providing "physical fitness services", which is a retail activity.

Taxpayer disagreed with the assessment. On August 28, 2012, Taxpayer filed a petition requesting Correction of the Assessment. Taxpayer's petition contained two (2) reasons for cancellation of the assessment:

- The income Taxpayer receives is derived from providing instructional lessons, which is subject to the service and other activities B&O tax classification; and

- The guidelines for determining the distinction between providing lessons and physical fitness services is and has been unclear to the point that mis-information about which leads to inconsistent reporting and enforcement. . . .

[2] The $. . . consisted of $. . . tax, $. . . interest, and $. . . assessment penalty.

ANALYSIS:

[1] Washington's excise tax law requires persons who charge for services defined as retail sales to collect retail sales tax on the charges to their customers and remit the tax to the state. RCW 82.08.020; RCW 82.08.050; *see* Det. No. 02-0039, 21 WTD 318 (2002).

RCW 82.04.050 states that the term retail sale includes the following services:

> (3) The term "sale at retail" or "retail sale" shall include the sale of or charge made for personal . . . services including amounts designated as . . . fees . . . and other service emoluments however designated, received by persons engaging in the following business activities: …
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> (g) The following personal services: Physical fitness services . . . .

WAC 458-20-183(2) (Rule 183) defines physical fitness services and provides, in part:

> (l) "Physical fitness services" include, but are not limited to: All exercise classes, whether aerobic, dance, water, jazzercise, etc., providing running tracks, weight lifting, weight training, use of exercise equipment, such as treadmills, bicycles, stair-masters and rowing machines, and providing personal trainers (i.e., a person who assesses an individual's workout needs and tailors a physical fitness workout program to meet those individual needs). "Physical fitness services" do not include instructional lessons such as those for self-defense, martial arts, yoga, and stress-management. Nor do these services include instructional lessons for activities such as tennis, golf, swimming, etc. "Instructional lessons" can be distinguished from "exercise classes" in that instruction in the activity is the primary focus in the former and exercise is the primary focus in the latter.

Sales of services falling within the definition of "sale at retail" or "retail sale" are subject to the retailing business and occupation (B&O) tax classification, and the seller is required to collect retail sales tax from the buyer. RCW 82.04.250, RCW 82.08.020, and RCW 82.08.050

If a service does not fall within the definition of "retail sale" and is not explicitly taxed under another section of Chapter 82.04 RCW, then the gross proceeds derived from rendering the service are subject to tax under the service & other activities B&O tax imposed in RCW 82.04.290(2), and not subject to retail sales tax. . . .

At issue here is whether the Taxpayer's "crossfit" training services are primarily "instructional lessons" or "physical fitness services." In February of 2009, the Department issued Excise Tax Advisory 3104.2009 (ETA 3104) which clarifies this distinction.

ETA 3104 includes the following characteristics as indicative of instructional lessons: "teaching the participant how to perform certain activities, generally following a specific curriculum that includes the study of the underlying philosophy of the activity . . . the participant obtaining certification as a physical fitness trainer or group fitness instructor, or mastery of the techniques

and philosophy with possible advancement in levels of achievement." In contrast the primary purpose of physical fitness services is characterized as: "primarily to improve flexibility, strength, or general fitness for the participant."

Another ETA that applies the primary purpose test to distinguish between "physical fitness services" from personal services or activities not subject to retail sale tax is ETA 3003.2009 Taxability of Yoga, Tai Chi, and Qi Gong, issued February 2, 2009 (ETA 3003). ETA 3003 provides that a person providing Yoga, Tai Chi, or Qi Gong classes in a "fitness facility" is generally presumed to be providing a "physical fitness service," but may overcome that presumption with the following evidence:

> Such evidence may include, but is not limited to, lesson plans or other similar materials that identify the specific curriculum followed in the class indicating that physical fitness related activities are not the primary focus of the class. For example, in the case of a Yoga class this would include a class curriculum that places significant emphasis on breath regulation, meditation, and/or discussion of the historical and philosophical origins of Yoga with the incidental physical fitness related activities

In addition, in 2005, the Department published a determination stating that Pilates was a "physical fitness service" subject to payment of retailing B&O tax and collection of retail sales tax. Det No. 04-0239E, 24 WTD 265 (2005) stated:

> WAC 458-20-183(2) (Rule 183) defines physical fitness services and provides, in part:"Physical fitness services" include, but are not limited to: All exercise classes, whether aerobic, dance, water, jazzercise, etc., providing running tracks, weight lifting, weight training, use of exercise equipment, such as treadmills, bicycles, stair-masters and rowing machines, and providing personal trainers (i.e., a person who assesses an individual's workout needs and tailors a physical fitness workout program to meet those individual needs). In the present case, the taxpayer leads and instructs clients in Pilates exercises. We found above that Pilates is a type of physical exercise engaged in to build strength and flexibility, and to improve the conditioning and functionality of the body. Pilates classes are therefore exercise classes, and physical fitness services under Rule 183. To the extent the taxpayer assesses its clients' workout needs and tailors the Pilates routine to meet those needs, the taxpayer is providing personal training, which is also included in the definition of physical fitness services under Rule 183. Det. No. 99-174, 19 WTD 172 (2000). . . .
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> In conclusion, RCW 82.04.050 provides that physical fitness services are classified as retail services and that retail sales tax must be collected. Pilates is a physical fitness activity. . . . We find no legal support for concluding that the taxpayer does not provide a physical fitness service.

Similarly, the Taxpayer's available class descriptions involve both instructional elements and physical fitness activities. As an example the class schedule for August . . . 2013 included

[several] one hour classes entitled "All levels – Strength and Conditioning"; one class entitled "Basic . . . Strength Training" and one class entitled . . . . The emphasis in describing the classes is on exercise, physical fitness, and improved strength and conditioning. Based on the information available we conclude the Taxpayer's classes are primarily focused on exercise and therefore are retail physical fitness services under the authority detailed above. Accordingly, we affirm the reclassification of Taxpayer's income derived from offering these classes to the public from the service and other actives B&O tax classification to the retailing B&O and retail sales tax classification.

[2] Taxpayer's request for relief was also based on what it described as confusion within the Department and industry.[3] 24 WTD 265 also addressed a taxpayer's concern about consistent reporting within the industry stating:

> The taxpayer states that it knows of several Pilates businesses that have received instructions from the Department to report under service rather than retail. Consistent treatment of taxpayers is a legitimate concern, and we will briefly address it. However, we cannot discuss other taxpayers by name because of confidentiality requirements. See RCW 82.32 330; Det. No. 00-206E, 21 WTD 66 (2002).
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> Statutes and rules require interpretation and application to specific facts. If the taxpayer believes the Department may have given advice to some of the taxpayer's competitors inconsistent with TI&E's current instructions to the taxpayer, it may inform the Department of the names of the competitors so that consistent instructions can be provided. Even if the taxpayer's concern should prove to be correct, however, that does not mean the Department must perpetuate past errors by repeating them with respect to other taxpayers. See, e.g., Det. No. 00-206E.

Moreover, RCW 82.32A contains the Taxpayer Bill of Rights. Both Taxpayers and the Department have certain rights and responsibilities. RCW 82.32A.020 invests the taxpayers of Washington with certain rights, included are:

> (2) The right to rely on specific, official written advice and written tax reporting instructions from the department of revenue to that taxpayer, and to have interest, penalties, and in some instances, tax deficiency assessments waived where the taxpayer has so relied to their proven detriment; . . .
>
> (5) The right to receive, upon request, clear and current tax instructions, rules, procedures, forms, and other tax information; and

[3] Taxpayer's reliance on the treatment of Yoga due to unclear advice from the Department in Rule 183 is not comparable. Taxpayer does not cite to any unclear advice given to "crossfit" or "crossfit" like businesses in Rule 183 or elsewhere.

Similarly, RCW 82.32A.030 imposes certain responsibilities on Taxpayers, which include:

> (2) Know their tax reporting obligations, and when they are uncertain about their obligations, seek instructions from the department of revenue;

Neither Taxpayer's petition nor in-person testimony stated that Taxpayer ever consulted the Department for clarification as to how to correctly report income. If there was confusion in the industry as Taxpayer claims, it could have asked the Department for a written ruling. If requested, the Department would have provided Taxpayer with a written decision that would have provided Taxpayer with reporting instructions that the Department would accept for the audit period.

## DECISION AND DISPOSITION:

Taxpayer's petition is denied.

Dated this 27th day of August 2013.