Cite as Det. No. 89-009A, 12 WTD 1 (1993).

BEFORE THE INTERPRETATION AND APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In The Matter of the Petition For Correction of Assessment of	)	F I N A L D E T E R M I N A T I O N
	)	No. 89-009A
. . .	)	Registration No. . . .
) . . .	/Audit	No. . . .
)		

[1] RCW 82.04.290: B&O TAX -- RETAIL SALES TAX -- SERVICE AND OTHER CLASSIFICATION -- SALES OF "COUPON BOOKS" AND ENTERTAINMENT "MEMBERSHIPS." Where a transaction consists of elements of both a service and a retail sale, the taxability is determined by the "true object" of the transaction, i.e., what the buyer was objectively seeking in exchange for the amount paid to the seller. When the activity does not fall under any specific tax classification, it falls under the catch-all "service and other" classification of the B&O tax.

TAXPAYER REPRESENTED BY: . . .

DATE OF CONFERENCE: . . .

DEPARTMENTAL REPRESENTATIVE: . . .

FACTS AND ISSUES:

Hesselholt, Chief A.L.J. -- The taxpayer's books and records were audited for the period . . . through . . . . The taxpayer petitioned the Director for direct review. The Audit Division assessed tax, asserting that the taxpayer was selling tangible personal property. Because the taxpayer did not obtain resale certificates from the organizations to which it sold memberships for resale, the Audit Division asserted retailing B&O tax and retail sales tax under RCW 82.04.050. Later file audits were done for the period . . . through . . . and . . . through . . . . The Department upheld the assessment . . . . By letter

dated January 17, 1989 taxpayer petitioned for reconsideration . . . .

Taxpayer contracts with various vendors to advertise their goods and services. The taxpayer provides this advertising service by selling "memberships" for various geographic areas. The contract between the taxpayer and the vendors provides that the vendor "wishes to attract additional customers and advertise his goods or services" and that taxpayer agrees "to provide advertising for [vendor] in the form of discount offers. . . . " The advertising services can be provided in various ways, but the items involved in this appeal consist of what the taxpayer refers to as "memberships." These memberships consist of a plastic membership card and a book. The books contain listings of restaurants, hotels, and other vendors that will grant a discount to the member when the card is presented, and coupons that entitle the bearer to free or discounted goods or services. The vendors are located both inside and outside of Washington. The taxpayer provides the membership book and cards to various clubs, usually nonprofit service clubs, which in turn sell the memberships to the public. The benefit to the vendor is the advertisement of its goods or services. The benefit to the taxpayer is the revenue it receives for the "memberships" it provides. The benefit to the consumers is the reduced price of the goods or services purchased. The book provided to the "members" explains how the membership is to be used and the rules of use. The Department assessed retail sales tax and retailing B&O tax on the sales of the books by the taxpayer.

The taxpayer raised a variety of issues. More generally, the taxpayer argues in its memoranda as follows:

> . . . the analysis that we urge starts with the recognition that the property does indeed contain both tangible and intangible components. The question is which of these components should dominate for purposes of tax characterization. We contend that the analysis in this case should be exactly like that in all cases where a tangible piece of paper represents an intangible promise to give a performance in the future. Promissory notes and tickets are examples of situations calling for the same analysis. The focus by the Connecticut court in Dine Out Tonight on relative "value" of the intangible component as compared to the tangible, is the right one in our opinion. In determining which characteristic deserves to dominate for tax purposes one should look for the value or "true object" sought by the parties.
>
> . . .

> The issue we raise is whether a "property" which admittedly has "value" should be characterized as "tangible" or "intangible" for tax purposes.

DISCUSSION:

Taxpayer believes that the issue is whether the tangible or intangible component of a property should dominate its tax characterization when the property consists of a tangible paper evidencing an intangible promise to give a performance in the future, and it requests that the intangible component of the property also be taken into account in determining its tax status.
Taxpayer provided a copy of a Connecticut case, Dine Out Tonight Club, Inc. v. Department of Revenue Services, 210 Conn. 567 (1989), arguing that the analysis used in that case should be applicable here.

In Dine Out, the taxpayer sold memberships in its club to Connecticut residents. Members received a membership card that entitled them to a free meal with the purchase of a second meal at restaurants participating in taxpayer's program. They also received a directory of participating restaurants. Members present the card when dining. The card is punched at each restaurant once it has been used there. The memberships are not transferable. The Connecticut Department of Revenue determined, in 1985, that the sale of the membership card was a "sale of tangible personal property" and therefore subject to the sales tax. The Connecticut Supreme Court found that "[t]he membership card and directory are merely indicia of that intangible right [to receive free meals and access to the knowledge of an expanding list of restaurants that provide them] and incidental aids to its exercise." [Citations omitted; brackets supplied.] The court held that because the transaction was "essentially the conveyance of an intangible right to free meals" the taxpayer's membership fees were intangible and not subject to Connecticut's sales tax.

Administratively, the states of California, Colorado, New York, Illinois, Texas, Minnesota and New Jersey have also ruled that the sale of similar memberships is not a retail transaction, although these rulings do not contain any explanation for the ruling.

A somewhat similar business to that involved here was discussed in State ex rel. Fishback v. Universal Serv. Agency, 87 Wash. 413 (1915). The issue in Universal was whether the corporation was doing an insurance business without complying with the statutes

regulating insurance. Therefore, the nature of the corporation's business was explored at some length in the court's opinion.

Universal had contracts with various vendors, including a physician, pharmacist, and dealers in shoes, clothing, groceries, and harness. The contracts with the vendors recited that Universal "proposes to act as agent of various persons in securing for them certain privileges and benefits." 87 Wash. at 415-416. After procuring the contracts under which the vendors agreed to provide goods and services at stated discounts from their regular rates to any consumer contracting with Universal, Universal sold, for a fixed consideration, the privileges specified in the vendor contracts to various consumers. The application signed by the consumers stated that they applied "for the service furnished by the Universal Service Agency" for one year and agreed to abide by the rules and regulations in the contracts issued to them. The contracts subsequently issued to the consumers stated that Universal Service Agency "is acting as the agent of the holder in securing the propositions" contained in contracts with various vendors, that these "propositions are contingent offers which become contracts upon their acceptance by the holder," and that "acceptance thereof shall at all times be evidenced by the payment to the agency of the compensation hereinafter provided." Universal issued each consumer/holder a card showing the vendors offering the discounts and the time period for which the holder had paid the compensation due the agency. The consumer contracts with Universal stated that "[i]n presenting the various offers herein contained the agency acts only as the agent of the parties and assumes no liability for the breach of any one of all of said contracts."

The court in Universal held that Universal was not an insurance company, but was instead acting as an agent of the vendors.

In this case, while none of the contracts identify the taxpayer as an agent, the book provided to the "members" contains a disclosure specifically stating that

> [Taxpayer] and/or its subsidiaries, will not be responsible if any establishment breaches its contract or refuses to accept cards/coupons; however, we will attempt to secure compliance. [Taxpayer] and/or its subsidiaries, will not be responsible in the event of Acts of God, fire, casualties, strike or other events beyond its control.

The membership book also specifically states that the membership is nontransferable.

RCW 82.04.050 defines a retail sale, in part, as:

> every sale of tangible personal property (including articles produced, fabricated, or imprinted) to all persons irrespective of the nature of their business . . . .

It was under the authority of this section that the Audit Division asserted the retailing B&O tax and retail sales tax. But we believe that taxpayer's activities are more properly classified under the service and other classification of the B&O tax:

> any business activity other than or in addition to those enumerated in RCW 82.04.230, 82.04.240, 82.04.250, 82.04.255, 82.04.260, 82.04.270, and 82.04.280 . . . This section includes, among others, and without limiting the scope hereof (whether or not title to materials used in the performance of such business passes to another by accession, confusion or other than by outright sale), persons engaged in the business of rendering any type of service which does not constitute a "sale at retail" or a "sale at wholesale."

RCW 82.04.290.

The application of the retail sales tax and retailing B&O tax to these facts depends on the "true object" of the transactions. The true object test is the prevailing test applied by the courts for distinguishing between nontaxable sales of services versus taxable sales of tangible property. See, e.g., Culligan Water Conditioning v. State Board of Equalization, 17 Cal. 3d 86, 550 P.2d 593, 130 Cal. Rptr. 321 (1976); Hartford Parkview Assocs. Ltd. Partnership v. Groppo, 211 Conn. 246, 558 A.2d 993 (1989); Commissioner of Revenue v. Houghton Mifflin Co., 396 Mass. 666, 487 N.E.2d 1388 (1986); Emery Indus., Inc. v. Limbach, 43 Ohio St. 3d 134, 539 n.E. 2d 608 (1989); WTAR Radio-TV Corp. v. Commonwealth, 217 Va. 877, 234 S.E.2d 245 (1977).

The true object test, however, is a subjective test and is more a conclusion than a true test. The inquiry as to the true object of the transactions involved in this matter should focus on the issue of what the buyer is seeking in exchange for the amount paid to the seller. See Emery Indus., Inc. v. Limbach, 539 N.E.2d at 613; Commissioner of Revenue v. Houghton Mifflin Co., 487 N.E. 2d at 1391, Hellerstein, Significant Sales and Use Tax Developments During the Past Half Century, 39 Vand. L. Rev. 961, 970 (1986), Det. No. 90-128, 9 WTD 280.1 (1990). In this case, the purchaser of the taxpayer's memberships is buying the service

that the taxpayer has provided by arranging for all of the discounts available to the purchaser of the membership.

We believe that taxpayer's activity is not covered under any specific tax classification and, therefore, falls under the service and other classification of the B&O tax. RCW 82.04.290. Persons taxable under this classification are defined as consumers (RCW 82.04.190) and subject to the retail sales tax on all purchases of tangible property used in the performance of their business activities.

DECISION AND DISPOSITION:

Taxpayer's petition is granted.

DATED this 31st day of December 1992.