

Cite as Det. No. 94-219, 15 WTD 55 (1995).

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

In the Matter of the Petition	)	<u>D E T E R M I N A T I O N</u>
for Interpretation of	)	
	)	No. 94-219
	)	
. . .	)	Unregistered
	)	

RULE 179; RCW 82.16.010, RCW 82.16.020; ETB 176:  
PUBLIC UTILITY TAX -- EXEMPTIONS -- DEDUCTIONS -- WATER  
DISTRIBUTION BUSINESS --HOMEOWNERS' ASSOCIATION. Fees  
received by homeowners' association for the operation  
and improvement of a water delivery system are subject  
to public utility tax.

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.

NATURE OF ACTION:

Homeowners' association appeals ruling that quarterly assessments for the operation and improvement of a common well and water delivery system are subject to public utility tax.<sup>1</sup>

FACTS:

Mahan, A.L.J. -- In accordance with the a declaration of protective covenants for the plats of a common property, the association was established in 1982. The association is responsible for maintaining and administering the property and facilities owned in common by the homeowners.

Common property operated by the association includes a community well and water delivery system. Each member who owns improved real property is assessed each quarter for the operation of the

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

water system as well as for capital improvements. The charge is assessed whether or not the member uses water from the system. The usage is unlimited and there are no meters on the system for individual users. If a member fails to pay the assessment, liens are placed against the member's property. The association also has the authority to discontinue service.

The association was instructed by the Department of Revenue ("Department") that it must register to do business and pay public utility tax on revenue from the distribution of water to its members. This appeal followed.

The association contends that it is not in the business of distributing water for sale. Rather, it contends in its petition that:

In support of our position that the required elements of a sale (i.e. water for a fee) do not exist, we made reference to Internal revenue code (IRC) Section 528. . . . In order for the water fee assessment to be "exempt function income" (i.e. nontaxable) for Federal income tax purposes, it must be required of members solely in their capacity as home owners/members. In contrast, if the water fee was in the nature of providing water services for a fee (i.e. a sale), then it must be classified as "gross income" (i.e. taxable) for federal tax purposes.

In this manner, the association contends that the Department should distinguish between nonprofit cooperatives making sales of water and homeowners' associations assessing fees for the upkeep of common property. According to the association, it interprets federal law as exempting the fees assessed for water by an association of homeowners and believes it should receive the same treatment under state law.

#### ISSUE:

Whether the quarterly fees assessed by a homeowners' association for the operation and improvement of a common water distribution system are subject to public utility tax.

#### DISCUSSION:

[1] An "association" such as the one here is included within the definition of "persons" subject to tax under this state's tax structure. RCW 82.04.030. RCW 82.16.020 imposes the public utility tax on, inter alia, water distribution businesses. RCW 82.16.040(4) defines a "water distribution business" to mean "the business of operating a plant or system for the distribution of water for hire or sale." See also WAC 458-20-179 (Rule 179).

Here there is no question that the association is a taxable entity and it is in the business of operating a plant or system for the distribution of water. The payment of a quarterly fee for the right to the water would also constitute a sale. In general, RCW 82.04.040 defines a "sale" to mean "any transfer of the ownership of, title to, or possession of property for a valuable consideration." The payment of an assessment for the right to take possession of water for personal use comes within the scope of this broad definition of a sale.

Further, an association's nonprofit status, the lack of eminent domain authority, or the lack of regulation by this state's utility commission does not affect the imposition of the tax. In this regard, the Department has previously stated that nonprofit cooperatives that are in the water distribution business are subject to public utility tax, to wit:

RCW 82.16.010(11) designates the water distribution business, defined in RCW 82.16.010(4), as a public service business. The Commission held that the lack of eminent domain power and absence of state regulation were immaterial because the taxpayer's business was among those specifically listed as subject to Public Utility Tax in the Statute. Since the taxpayer was operating a system for the distribution of water for hire or sale, it was subject to the Public Utility Tax.

Excise Tax Bulletin 176.16.176 (ETB 176).

Even if, as the association suggests, federal law can be read to allow the deduction of income from the operation of an association's water system, it does not necessarily follow that this state's tax structure allows a similar deduction from the public utility tax.

This state's tax structure provides that the measure of the business and occupation (B&O) and the public utility taxes is on the "gross income" of a business. RCW 82.04.220; 82.16.020.<sup>2</sup> Various deductions from the measure of the tax may be available. For example, similar to the federal scheme, homeowners' associations are allowed a B&O tax deduction for "amounts used solely for repair, maintenance, replacement, management, or improvement of the residential structures and commonly held property". RCW 82.04.4298. No similar deduction from the public

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<sup>2</sup>With respect to the public utility tax, an exemption is available to a water distribution business only if the gross income for a monthly period is less than five hundred dollars. RCW 82.16.040. We do not have adequate information to know if this exemption applies to this association.

utility tax is available for homeowners' associations. However, a deduction is available to a nonprofit water association for capital improvement costs. RCW 82.16.050(10).<sup>3</sup>

Accordingly, the income from the operation of the association's water system is subject to the public utility tax. However, the exemption allowed under RCW 82.16.040 and the deduction allowed under RCW 82.16.050 may offset some or all of the tax burden.

DECISION AND DISPOSITION:

The taxpayer's petition is denied. As previously instructed by the Department, the taxpayer should register and file returns accordingly.

DATED this 25th day of October, 1994.

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<sup>3</sup>Indeed, if Chapter 82.16 RCW does not apply to a nonprofit water association as the association here suggests, there would have been no need for this deduction.