

Cite as Det. No. 13-0156R, 33 WTD 199 (2014)

BEFORE THE APPEALS DIVISION  
DEPARTMENT OF REVENUE  
STATE OF WASHINGTON

In the Matter of the Petition for	)	<u>D E T E R M I N A T I O N</u>
Reconsideration of Assessment of	)	
	)	No. 13-0156R
...	)	
	)	Registration No. . . .
	)	

1] RCW 82.04.080: GROSS INCOME OF BUSINESS – PAYMENTS TO A NON-PROFIT ORGANIZATION. There is no specific deduction or exemption for income received by a non-profit organization. B&O tax is imposed on the business income of non-profit organizations, unless a specific deduction or exemption applies.

[2] RCW 82.04.4282: DEDUCTION FOR CONTRIBUTIONS AND DONATIONS. Payments do not qualify as “contributions” or “donations” if the funds are not provided for a gratuitous purpose and the party providing retains control over the funds.

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] seeks reconsideration of a determination that denied Taxpayer’s request for refund of service and other activities business and occupation (“B&O”) tax paid on payments received from a foundation. Taxpayer’s petition for reconsideration is denied, based on a conclusion that the payments received were to further a business purpose and not gratuitous.<sup>1</sup>

ISSUES:

1. Are the payments Taxpayer receives from [a foundation] “gross income of the business” as defined in RCW 82.04.080?
2. Are the payments Taxpayer receives from [a foundation] exempt from B&O tax under the provisions of RCW 82.04.4282?

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

## FINDINGS OF FACT:

Taxpayer is a medical clinic located [in Washington] that provides primary medical care to residents and visitors. The Department of Revenue (“Department”) audited Taxpayer’s books and records for the period January 1, 2007 through December 31, 2010. On March 30, 2012, the Department issued a \$. . . assessment.<sup>2</sup> Taxpayer paid the assessment and now requests a refund. The refund request is for B&O tax assessed on payments received from [the Foundation].<sup>3</sup>

[The Foundation] is a non-profit charitable foundation qualified under Section 501(c)(3) of the Internal Revenue Code. [The Foundation] was established . . . with a mission to “promote and support quality medical care for [area] residents and visitors.” It is registered with the Washington State’s Secretary of State as a charitable organization with the same stated purpose.

Taxpayer’s application for refund explained the relationship between Taxpayer and [the Foundation]:

[Taxpayer] has made a modest profit every year it has been in existence, but only because of the financial support that [the Foundation] gives it. It is a practical impossibility for a physician, with the supporting staff, medical equipment and office and operating space that is now required to provide quality primary medical care, to earn a living [in the area] without substantial taxpayer or charitable support. [The area] is not unique in this respect. Medical practices receive such support in every rural area in Washington State and in nearly every rural area in the United States.

[The Foundation], in turn, obtains the cash it needs from donations from the public, virtually all of whom are residents of [the area]. Since [the Foundation] owns the building in which [Taxpayer] is the tenant and the furnishings and equipment in it, a sizeable portion of its financial support also consists of the use of this property.

The audit narrative explained:

[The Foundation] reimburses [Taxpayer] for medical practitioner salaries, malpractice insurance premiums, business manager salaries, and employee benefits for providing medical services to residents and visitors [in the area]. The contract also stipulates that [Taxpayer] will consult with [the Foundation] prior to committing to any unplanned expenditures that may reasonably be expected to be paid by [the Foundation].

The relationship between Taxpayer and [the Foundation] is spelled out more specifically in a building lease and clinic service agreement (“Agreement”). The Agreement specifically addresses Taxpayer’s operation of the medical center in the building that is owned by the Foundation:

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<sup>2</sup> The assessment consisted of \$. . . tax, \$. . . interest, and \$. . . assessment penalty.

<sup>3</sup> The current name of the entity is . . . . During the audit period the name of the entity was . . . [the Foundation].

[The Foundation] hereby contracts with [Taxpayer] to operate and manage a primary care medical facility at the Center (the “Medical Clinic”) pursuant to all applicable statutory and/or regulatory requirements, as well as all other requirements of this Agreement. [Taxpayer] shall be responsible for the operation and management of the Medical Clinic consistent with such standards and requirements, and for establishing and implementing all policies and procedures necessary to operate the Medical Clinic, Including, without limitation, policies related to personnel, services, and pricing.

The Agreement also stated that the relationship of Taxpayer and the Foundation was that of independent contractors.

Other aspects addressed in the Agreement were:

- All management and medical decisions are Taxpayer’s;
- It spells out the division of administrative and financial responsibilities between Taxpayer and [the Foundation];
- It states the amount of the grant that will be allocated to Taxpayer’s use of Foundation property;
- Taxpayer must consult with Foundation before committing itself to any expenditures it expects [the Foundation] to pay; and,
- It sets the salaries of the physicians and certain high-ranking personnel.

On May 29, 2013, the Department issued Determination No. 13-0156. Determination No. 13-0156 denied Taxpayer’s request for refund reasoning that the payments received from [the Foundation] constituted gross income of the business and that the payments did not qualify for the tax exemption allowed for “contributions” or “donations” (RCW 82.04.4282). On July 1, 2013, Taxpayer filed a petition for reconsideration.

Taxpayer disagreed with the decision. On July 1, 2013, Taxpayer filed a petition for reconsideration. Taxpayer argued that the decision contained in Det. No. 87-110, 3 WTD 021 (1987) should be controlling.

Taxpayer maintained that neither [the Foundation] nor its members or directors were entitled to receive any significant goods or services from Taxpayer because of the payments. The only thing the contract between [the Foundation] and Taxpayer required Taxpayer to do was to provide primary care [in the area].

#### ANALYSIS:

The B&O 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.

As we discussed in Determination No. 13-156, “gross income of the business” is defined in RCW 82.04.080 as any “value proceeding or accruing by reason of the transaction of the business engaged in and includes . . . compensation for the rendition of services . . . and other emoluments however designated,” without deduction of the costs of doing business. In exchange for providing medical services, Taxpayer receives payments from the Foundation. Accordingly, the payments Taxpayer receives are taxable as “gross income of the business” unless some deduction or exemption applies.

Exemptions and deductions from tax are narrowly construed. *Budget Rent-A- Car, Inc. v. Department of Rev.*, 81 Wn.2d 171, 500 P.2d 764 (1972). Taxation is the rule; exemption is the exception. *Spokane County v. City of Spokane*, 169 Wash. 355, 13 P.2d 1084 (1932). A person claiming a tax exemption or exception has the burden of proving he or she qualifies for the exemption or exception. *Group Health Cooperative of Puget Sound, Inc. v. State Tax Commission*, 72 Wn.2d 422, 433 P.2d 201 (1967); Det. No. 89- 268, 7 WTD 359 (1989). Thus, the burden is on the taxpayer to show it qualifies for a tax exemption.

RCW 82.04.4282 provides a deduction for donations:

In computing tax there may be deducted from the measure of tax amounts derived from bona fide (1) initiation fees, (2) dues, (3) contributions, (4) donations, . . . .

Funds do not qualify as “contributions” or “donations” if the funds are not provided for a gratuitous purpose and the party providing the funds retains control over the funds. *Analytical Methods v. Dep’t of Revenue*, 84 Wn. App. 236, 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.<sup>4</sup> It concluded:

“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 NEW THIRD INTERNATIONAL DICTIONARY 496 (1966). “Donation” means “the action of making a gratuitous gift or free contribution.” WEBSTER’S NEW THIRD INTERNATIONAL DICTIONARY 672 (1966). These definitions require a gratuitous purpose.

*Id.* at 243.

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<sup>4</sup> As stated in *John H. Sellen Constr. Co. v. Dep’t of Revenue*, 87 Wn.2d 878, 882, 558 P.2d 1342 (1976), “Words in a statute are given their ordinary and common meaning absent a contrary statutory definition.” Washington courts use WEBSTER’S NEW THIRD INTERNATIONAL DICTIONARY in the absence of other authority. *State v. Glas*, 106 Wn. App. 895, 27 P.3d 216 (2001), citing, *In re Personal Restraint of Well*, 133 Wn.2d 433, 438, 946 P.2d 750 (1997). Respect for the legislature’s intent in using a specific word is not compromised by using the dictionary to define the common meaning of words.

Here, the Taxpayer contracted with [the Foundation] “to operate and manage a primary care medical facility.” Because Taxpayer is contractually obligated to provide the services in exchange for the funds, it cannot be reasonably said that the funds are a contribution or donation to the taxpayer.

A similar conclusion would be reached under WAC 458-20-169(5)(f)(iii) as to what constitutes a contribution for purposes of exempt fund raising activity by a non-profit organization:

(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.

Here, similar to the example in the rule, the amounts received by the taxpayer conditioned upon the taxpayer providing services to the community. i.e. “[the Foundation] hereby contracts with [Taxpayer] to operate and manage a primary care facility.”

On reconsideration, Taxpayer argued that the original determination was in error because: 1) the donations did not result in either [the Foundation] or its members or directors receiving any significant goods or services. Taxpayer argued that the decision contained in Det. No. 87-110, 3 WTD 021 (1987), should be controlling.

In 3 WTD 021, the Department held that donations by home bound persons who received a meal that the taxpayer provided were not subject to B&O tax, because they received the meals whether or not they made the donations. Det. No. 87-110 stated, “outright gifts, donations, . . . which do not entitle the payor to receive any significant goods or services in return for the payment are not subject to... [the B&O Tax].”

The facts of 3 WTD 021 are distinguishable from Taxpayer’s. In Taxpayer’s case, the payments Taxpayer receives are not an outright gift or donation but are in return for medical services. The contract between Taxpayer and [the Foundation] is not as simple as [the Foundation] paying funds over to Taxpayer with the intent that the funds would be used to provide medical care. Rather, [the Foundation] is paying Taxpayer to operate a clinic. The funds it passes onto Taxpayer are not gratuitous, rather they are payments made in exchange for services – the continued operation of a medical practice. Having found the payments did not have a gratuitous purpose we sustain the assessment.

#### DECISION AND DISPOSITION:

Taxpayer’s petition for refund is denied.

Dated this 31st day of December 2013.