Cite as Det. No. 01-015, 23 WTD 121 (2004)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition	)	D E T E R M I N A T I O N
For Correction of Assessment/Refund of	)	
	)	No. 01-015
. . .	)	
	)	Registration No. . . .
	)	Docket No. . . .
	)	FY . . . /Audit No. . . .

[1] RULE 118: B&O TAX – EXEMPTION – RENTAL OF REAL ESTATE. A lessor's limited access to a rented space for specific purposes pursuant to the lease agreement does not destroy the character of the contractual arrangement as a lease.

[2] RULE 118: B&O TAX – EXEMPTION – RENTAL OF REAL ESTATE. When a lessee is contractually authorized to occupy the premises, and its interest is not terminable or revocable at the will of the party who gave it, and the agreement unequivocally provides for notice to the other party before termination of the agreement, the agreement is found to be a lease and not a license.

[3] RULE 168; RCW 82.04.260(12): B&O TAX – SPECIAL RATE -- PUBLIC AND NONPROFIT HOSPITALS – "SERVICES TO PATIENTS" – DEPARTMENTS AND SERVICES. As demonstrated by the phrase "services to patients" in Rule 168(3)(a), the Department has determined that the legislative intent of RCW 82.04.260(12), as discussed above, was to extend the special rate to hospitalization services rendered by nonprofit hospitals to inpatients. Additionally, for departments and services available to both inpatients and outpatients -- e.g., emergency rooms, radiology services, and laboratories -- the RCW 82.04.260(12) rate will be applicable to those that are an "integral, interrelated and essential part" of the hospital using the Group Health analysis.

[4] RULE 168; RCW 82.04.260(12): B&O TAX – SPECIAL RATE -- PUBLIC AND NONPROFIT HOSPITALS – "SERVICES TO PATIENTS" – INTEREST ON OVERDUE ACCOUNTS RECEIVABLE. The extension of credit, no matter how generous the terms might be, is not a hospitalization service.

[5] RULE 168; RCW 82.04.260(12): B&O TAX – SPECIAL RATE -- PUBLIC AND NONPROFIT HOSPITALS – "SERVICES TO PATIENTS" – PHYSICIAN TRANSCRIBING FEES. Transcribing service is provided by Taxpayer to physicians, who pay for it. It is a cost of doing business of physicians with hospital privileges. The transcribing service is not a hospitalization service rendered to patients, and the fact that the doctors may be required to provide the transcriptions for the hospital's records does not change this analysis.

[6] RULE 168; RCW 82.04.260(12): B&O TAX – SPECIAL RATE -- PUBLIC AND NONPROFIT HOSPITALS – "SERVICES TO PATIENTS" – EDUCATIONAL OFFERINGS. Under the rationale of Group Health, educational offerings open to, or provided to, the general public at the hospital will properly qualify as being an "integral, interrelated, and essential part" of the hospital operation if they are unique and incidental to the provision of hospitalization services (i.e., services which will be, have been, or are currently being provided to the students or participants).

[7] RULE 167; RCW 82.04.170, RCW 82.04.4282: B&O TAX – DEDUCTION – "TUITION FEES"/"BONA FIDE TUITION FEES" -- RADIOLOGY SCHOOL TUITION. When a hospital's radiology school is not accredited, does not offer a program of a general academic nature, or otherwise qualify under RCW 82.04.170 or RCW 82.04.4282, it will be considered to be a trade or specialty school for which no deduction is permitted. Lacey Nursing v. Dept. of Revenue, 128 Wn.2d 40, 49-50 (1995).

[8] RULE 111: B&O TAX – EXEMPTION – ADVANCES AND REIMBURSEMENTS – EMERGENCY ROOM PHYSICIANS. Hospital's contract with emergency room physicians held not to support a Rule 111 exemption when the hospital was liable for the emergency room doctors' payments whether or not patients paid their bills, and when the contract clearly provided that patients coming to the emergency room for treatment were the hospital's patients.

[9] RCW 82.04.4297: B&O TAX – DEDUCTION – HEALTH OR SOCIAL WELFARE ORGANIZATION – EMPLOYEE BENEFIT PLAN – CHAMPUS PAYMENTS. CHAMPUS held to be an employee health benefit plan for the military, and its payments to hospitals are ineligible for the RCW 82.04.4297 deduction.

[10] RULE 178: USE TAX – COMPUTER TRAINING – SEPARATELY NEGOTIATED AND SEVERABLE. Training costs, of payments to a vendor of canned computer programs for the training of employees to use those programs, are not subject to sales or use tax when separately negotiated and severable from purchase of the canned program.

[11] RULE 18801; RCW 82.04.0281, RCW 82.12.0275: RETAIL SALES AND USE TAX – EXEMPTION – PRESCRIPTION DRUGS – "LABORATORY REAGENTS" AND "OTHER DIAGNOSTIC SUBSTANCES." Stains, dyes, and decolorizers used by pathologists in the diagnosis of disease, which react with and cause a change in cellular tissue, are exempt from retail sales/use tax. Fixatives, decalcifying solution, dehydrating solution, and clearing reagents are exempt reagents. Paraffin and gelatin are not reagents. Substances with multiple uses are exempt only when used to react with cells.

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:

Petition by a nonprofit hospital concerning the appropriate business and occupation (B&O) tax classifications of its income.[1]

FACTS:

Bauer, A.L.J. – Taxpayer's business records were reviewed by the Audit Division (Audit) of the Department of Revenue (Department) for the period January 1, 1992 through December 31, 1995. As a result, the above-referenced tax assessment was issued on October 25, 1996 in the total amount of $ . . . , which amount included interest calculated to that date.

Taxpayer is a nonprofit corporation which, during the audit period, operated as a hospital.

ISSUES:

1. Morgue . . . . Whether space allocated to the county for use as a morgue is the nontaxable rental of real property, or a taxable license to use real estate.

2. Applicability of RCW 82.04.4289 and RCW 82.04.260(12):[2] Whether, after June 30, 1993, certain educational programs . . . were properly deductible under RCW 82.04.4289 prior to July 1, 1993, and taxable under the RCW 82.04.260(12) B&O tax classification, and whether the following were, after June 30, 1993, taxable under the RCW 82.04.260(12) B&O tax classification:

a. Interest earned on overdue patient accounts receivable . . . .
b. Education programs . . . : Diet consulting and the . . . Health Conference
c. Transcription of Medical Records . . . : Taxpayer disagrees with the auditor's characterization of this revenue as the "making of copies of medical records . . . " the revenue on this schedule, according to Taxpayer, is from transcribing services rendered to physicians.

[1] Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.
[2] Originally codified as RCW 82.04.260(15).

3. Radiology Program Tuition . . . . Whether tuition income for the radiology program is taxable or exempt, similar to the nursing education tuition which was deemed not taxable in Deaconess Hospital v. Department of Rev., BTA Docket No. 79-26 (1980) (Deaconess).

4. Emergency Room Physicians . . . . Whether Taxpayer is taxable on amount received and paid to its emergency room physicians

5. CHAMPUS[3] . . . . Whether Taxpayer is eligible for a deduction for its CHAMPUS revenues

6. "Installation Expense" . . . . Whether use tax was properly assessed on certain amounts characterized in Taxpayer's books as "Installation Expense" from . . . .

7. Pathology substances. Whether use tax was properly assessed on pathology substances such as items used "to fix samples, stains, and decolorizers."

DISCUSSION:

1. Morgue. Amounts received from the local county coroner's office were taxed under the service and other activities classification of the B&O tax as a license to use real estate. Taxpayer disagrees, contending the contract between the county and itself is an exempt rental of real estate. RCW 82.04.390; WAC 458-20-118 [Rule 118].

The county's coroner's office, through its agent, performs all county autopsies in the morgue. The coroner's office has contracted with physicians to perform the actual autopsies, and they perform these autopsies only at the direction of the Coroner. These physicians have complete dominion and control of the space (except for housekeeping services, which Taxpayer provides).

Taxpayer believes that the auditor was influenced by newspaper articles where it was reported that the coroner himself, an elected official, had complained that he, personally, could not obtain a key to the morgue. Taxpayer did not give the coroner a key because of reasons allegedly related to some of his actions, and not related to the use of the space. Taxpayer argues that this was of little import in the case, because the coroner's agents, the only users, did have keys and exercised dominion and control over the space. In support of its argument, Taxpayer has provided a copy of the rental agreement.

WAC 458-20-200 (Rule 200) is titled "Leased Departments." It reads, in part:

> (a) Where the lessor receives a flat monthly rental . . . as rental for a leased department, such income is presumed to be from the rental of real estate and is not taxable. In a determination of whether an occupancy is a rental of real estate, all the facts and circumstances, including the actual relationship of the parties, are to be considered (see: WAC 458-20-118). Written

[3] Civilian Health and Medical Program for the Uniformed Services

agreements, while not required, are preferred and are given considerable weight in deciding the nature of the occupancy. While the fact that the written agreement may identify the occupancy as a "lease" is not controlling, agreements which contain the following provisions support the presumption that the occupancy is a rental of real estate:

i. The occupant is granted exclusive possession and control of the space.

ii. The occupancy is for a time certain which is more than 30 days, i.e. month to month, yearly, etc.

iii. The parties are required to notify each other in the event of termination of the occupancy.

In this case, Taxpayer receives a flat monthly rental fee. The written agreement is, without question, in the form of a lease.

Under the terms of the agreement, the county coroner's office is granted possession and control, on a 24 hour basis, of the space, for the purposes of performing autopsies, office space, and evidence and body storage. As to other provisions which support the agreement as a rental arrangement according to Rule 200, the contract being construed is for a time certain, ten years, and the parties must notify each other in the event of termination of the contract. The space is physically enclosed by walls and lockable doors. Although the language of the agreement in force during the audit period does not expressly state that the lessee has "exclusive dominion and control" of the space, it is apparent that that is what the parties essentially intended, evidenced by the necessity of the lessee to approve, by agreement, that Taxpayer could use the premises without charge for certain purposes (i.e., the temporary storage of bodies).

[1] We do not view Taxpayer's having limited access the morgue for specific purposes pursuant to the lease agreement as interrupting possession and control by the lessee. Indeed, Washington courts have held that reservations by a lessor, wherein the lessor has some limited use of the leased premises, do not destroy the character of the contractual arrangement as a lease. See Tacoma v. Smith, 50 Wash.App. 717, 750 P.2d 647 (1988); and Barnett v. Lincoln, 162 Wash. 613, 299 P. 392 (1931).

Further, in Regan v. City of Seattle, 76 Wn.2d 501, 504, 458 P.2d 12 (1969), the Supreme Court held that a one day rental agreement for the Seattle Center Coliseum (to be used for go-cart racing), which agreement contained a provision that the building would at all times remain under the charge and control of the Superintendent of Buildings of the City, who had a right to enter the building at any time, and any matter not provided for in the lease would be left to the sole discretion of the Superintendent, did not divest the tenant of possession and control thereby converting a lease into something else.

The characterization of the arrangement at issue as a rental of real estate is also consistent with Rule 118, which reads, in part:

(2) LEASE OR RENTAL OF REAL ESTATE. A lease or rental of real property conveys an estate or interest in a certain designated area of real property with an exclusive right in the lessee

> of continuous possession against the world, including the owner, and grants to the lessee the absolute right of control and occupancy during the term of the lease or rental agreement.

In assessing the contested taxes, Audit was concerned that the county coroner did not have his own key. That is clearly a matter controlled by the county, which pays the rent. The county, as paying tenant, has the clear authority under the lease agreement to intervene and provide the coroner with access.

The Washington Supreme Court in Barnett v. Lincoln, supra, states, quoting Tiffany, Landlord and Tenant, Vol.1, p. 23:

> One having a license . . . has merely a permission to do certain acts, which he can assert against the licensor only, and which is ordinarily terminable or revocable at the will of the latter, and is not transferable.

[2] Barnett, 162 Wash. at 618. The lessees in the instant case have more than permission to do certain acts. They are, in fact, contractually authorized to occupy the premises. Moreover, the interest that they have in the real property of the hospital is not terminable or revocable at the will of the party who gave it. The agreement unequivocally provides for notice to the other party before termination of the agreement.

We conclude that the arrangement at issue is a rental of real property. As such it is exempt of the business and occupation tax. RCW 82.04.390; Rule 118. See also, Det. No. 96-173, 18 WTD 1 (1999). Taxpayer's petition as to this issue is granted.

2. Applicability of RCW 82.04.4289 and RCW 82.04.260(12). Taxpayer argues that certain educational programs . . . – were, prior to July 1, 1993, services rendered to patients by a non-profit hospital, and were not taxable. After that date, argues Taxpayer, they were "hospital activities" taxable under the non-profit hospital classification.

Taxpayer disagrees that the interest received on overdue patient accounts receivable was correctly taxable under the service and other activities classification of the B&O tax. Taxpayer argues that this classification is not appropriate after the July 1, 1993 change in the law, and that it should have been taxed under the public and non-profit hospital rate provided for by RCW 82.04.260(12). Taxpayer argues that, unlike most industries, much of its revenue is written off as a bad debt, and, in doing so, there is no distinction made between patient revenues and interest due. Credit is often extended to give patients a sense of contributing to their own care. Taxpayer thus believes that the very nature of the way it handles patient credit makes this activity different than the average business that expects to make money on extending credit.

Taxpayer also disagrees with the reclassification of two education programs in audit Schedule 2 -- "Diet Consulting" and "Womens' Health Conference" -- from the non-profit service B&O tax classification under RCW 82.04.260 to the service and other activities classification. Taxpayer contends this is inappropriate because these are properly hospital activities. Diet Consulting,

according to Taxpayer, is primarily a service provided to hospital inpatients (i.e., diabetics). Taxpayer contends the Women's Health Conference is a normal hospital activity featuring various speakers on medical subjects. Enrollment is open to the public. Taxpayer states that the Board of Tax Appeals in Docket No. . . . ruled these activities were services rendered to patients by a non-profit hospital, and that, as such., they certainly meet the broader language of "hospital activities" under RCW 82.04.260(12).

Taxpayer disagrees with the auditor's characterization of amounts received for the transcription of medical records as the "making of copies of medical records . . . ." The revenue on this schedule, according to Taxpayer, is from transcribing services rendered to physicians. Taxpayer believes this activity is common to hospitals and is encompassed by the "hospital activities" of RCW 82.04.260(12).

Prior to July 1, 1993, RCW 82.04.4289[4] provided a deduction for nonprofit hospitals as follows:

> In computing tax there may be deducted from the measure of tax amounts derived as compensation for services rendered to patients or from sales of prescription drugs as defined in RCW 82.08.0281 furnished as an integral part of services rendered to patients by a hospital, as defined in chapter 70.41 RCW, which is operated as a nonprofit corporation, . . . but only if no part of the net earnings received by such an institution inures directly or indirectly, to any person other than the institution entitled to deduction hereunder. In no event shall any such deduction be allowed, unless the hospital building is entitled to exemption from taxation under the property tax laws of this state.

(Emphasis added.) WAC 458-20-168 (Rule 168), as in effect before July 1, 1993, provided in pertinent part as follows:

> (4) DEDUCTIONS.
>
> (a) Hospitals operated by the United States or its instrumentalities or the state of Washington or its political subdivisions may deduct amounts derived as compensation for medical services to patients and sales of prescription drugs and medical supplies furnished as an integral part of such services. (See RCW 82.04.4288.)
>
> (b) Other hospitals operated as nonprofit corporations . . . may also deduct the amounts described in subsection (a) above (see RCW 82.04.4289), provided that:
>
> (i) No part of the net earnings received by such an institution inures, directly or indirectly, to any person other than the institution entitled to deduction hereunder; and
>
> (ii) No deduction will be allowed under (a) of this subsection, unless written evidence is submitted to the department of revenue showing that the hospital building is entitled to exemption from taxation under the property tax laws of this state.

(Emphasis added.) The nonprofit hospital deduction was also interpreted by the Washington Supreme Court in Group Health Cooperative v. Washington State Tax Commission, 72 Wn.2d

[4] Before that, the deduction was contained in RCW 82.04.430(9).

422, 433 P.2d 201 (1967) (Group Health). This case concerned Group Health's entitlement to a B&O tax deduction under RCW 82.04.430(9)[5] for revenue from its "central clinic." RCW 82.04.430(9) provided:

> In computing tax there may be deducted from the measure of tax the following items:. . . (9) Amounts derived as compensation for services rendered to patients by a hospital, as defined in chapter 70.41 RCW, which is operated as a nonprofit corporation . . . .

RCW 70.41.020(3) provided (as it does today) the following definition of "hospital":

> "Hospital" means any institution, place, building, or agency which provides accommodations, facilities and services over a continuous period of twenty-four hours or more, for observation, diagnosis, or care, of two or more individuals not related to the operator who are suffering from illness, injury, deformity, or abnormality, or from any other condition for which obstetrical, medical, or surgical services would be appropriate for care or diagnosis. "Hospital" as used in this chapter does not include . . . clinics, or physician's offices where patients are not regularly kept as bed patients for twenty-four hours or more.

The Supreme Court in Group Health, combining the pertinent portions of both these statutes, concluded that the legislature, basically, had in mind that the deduction applied to amounts received for services furnished to patients by a hospital, as such facilities and services are ordinarily comprehended." Group Health first reasoned that the RCW 82.04.430(9) deduction did not contemplate ordinary medical consultation and treatment, such as one seeks and obtains in a doctor's office or clinic.[6] The Court then went on to conclude that, even though Group Health was organizationally integrated and its various activities interrelated, that its "services to patients" could still be broken down into two different categories:

> ***medical*** consultation, diagnosis, treatment, and care by way of home or office calls, and
>
> ***hospitalization*** together with the usual services accompanying such a confinement.

(Group Health, 72 Wn.2d at 432, italicized emphasis in original text.) The Court noted that the bulk of the first type of service -- "medical" -- was essentially furnished and performed in respondent's outlying clinics. The second type of service -- "hospitalization" -- was supplied through respondent's central or hospital facility, including in some measure, at least, "the central clinic which served the central complex on a basis akin to the ordinary intake or emergency room in the average hospital":

> [T]he line of demarcation between the character of the services supplied by respondent is reasonably discernible. Likewise, the division between the facilities which afford the respective services is, with the exception of the central clinic, fairly observable. . . .[T]he outlying clinics are staffed, equipped, administered, and provide that type of medical

[5] Before it was re-codified as RCW 82.04.4289.
[6] Group Health, 72 Wn.2d at 431.

> service to the members which one would expect to find and receive in the average private physician's office or clinic. They are open only during regular business hours, provide no domiciliary care or overnight facilities, and are physically separate and apart from the central or hospital complex. And, as with the ordinary doctor's office, when the patient's needs exceed the resources at hand referral to specialists or to the hospital, as the case may be, is recommended and becomes available. . . .
>
> On the other hand, the central facility, including the central clinic, furnishes modern as well as all of the traditional hospital services, i.e., bed wards, surgery rooms, laboratories, X-ray equipment, pharmaceutical supplies, specialized professional staff, nursing staff, catering services, and 24 hour intake and emergency facilities. These services differ in no substantial way, except in their over-all organizational scheme, from the ordinary hospital. Within the framework of this aspect of respondent's service, the central clinic truly forms an integral, interrelated and essential part of the central facility, for, although it undertakes to provide some out-patient services akin to the outlying clinical service, it nevertheless provides the round-the-clock intake and emergency services which form a constituent part of the normal hospital operation. In this sense, then, the central clinic is no more separable from the central or hospital facility than the surgery rooms, the bed wards, the laboratory or the other components of the hospital activity, all of which might incidentally perform some out-patient service.

(Group Health, 72 Wn.2d at 432, 433, emphasis added.) The Group Health decision, for these reasons, found that entity's "central clinic" to be, functionally, an integral part of the "hospital" portion of Group Health's hospital activities because it provided the hospital's intake and emergency function.[7] The Court therefore determined that the clinic was rendering a deductible "hospitalization" service, as opposed to a nondeductible "medical" service. In arriving at its conclusion that the "central clinic" was part of Group Health's "hospital," the Supreme Court considered both (1) the clinic's location in the central facility and, (2) its "round-the-clock intake and emergency services" function for patients who needed immediate hospitalization as in-patients.[8]

The Department has historically taken the position that the RCW 82.04.4289 nonprofit hospital deduction applied to gross receipts by otherwise qualifying institutions when they rendered traditional hospitalization services to patients, and did not apply to income from outpatient medical clinics, even though such clinics might be owned and operated by a nonprofit hospital. Det. No. 92-192, 12 WTD 377 (1992). Departments and services available to both inpatients and outpatients -- e.g., emergency rooms, radiology services, and laboratories -- that are an "integral, interrelated and essential part" of the hospital have been evaluated using the Group Health analysis. Det. No. 90-245, 10 WTD 033 (1990).

Effective July 1, 1993, the legislature removed the RCW 82.04.4289 nonprofit hospital deduction and replaced it with the "Public or Nonprofit Hospital" rate under RCW 82.04.260(12):

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[7] As opposed to the outlying clinics. Group Health, 72 Wn.2d at 430.

[8] We also note the Court did not address the clinic staff's employment or training relationship to the hospital.

> (12) Upon every person engaging within this state in business as a hospital, as defined in chapter 70.41 RCW, that is operated as a nonprofit corporation or by the state or any of its political subdivisions, as to such persons, the amount of tax with respect to such activities shall be equal to the gross income of the business multiplied by the rate of 0.75 percent through June 30, 1995, and 1.5 percent thereafter. The moneys collected under this subsection shall be deposited in the health services account created under RCW 43.72.900.

Taxpayer argues that Washington hospitals agreed to support the July 1, 1993 change in the law, whereby they became subject to the B&O tax under RCW 82.04.260(12), only because the taxes were to be deposited in the health services account. Taxpayer argues the wording of RCW 82.04.260 would have exactly reflected the language of the prior nonprofit hospital exemption if the legislature intended to merely tax in-patient service revenue. Instead, according to Taxpayer, the language adopted was very broad and was intended to extend the special RCW 82.04.260(12) B&O tax classification to all business activities conducted by hospitals, and not just services to their inpatients.

WAC 458-20-168 (Rule 168),[9] however, implements RCW 82.04.260(12) as follows:

> (3). . .There are two B&O tax classifications which can apply to persons providing medical services through the operation of a hospital, with the tax classification dependent on the organizational structure of the hospital. The B&O tax classifications are:
>
> (a) Public or nonprofit hospitals. This B&O tax classification applies to gross income derived from personal and professional services to patients by hospitals that are operated as nonprofit corporations, operated by political subdivisions of the state, or operated but not owned by the state. These hospitals became taxable for hospital services under this B&O tax classification on July 1, 1993. These hospitals were required to report under the service B&O tax classification prior to July 1, 1993, but were entitled to a deduction for services rendered to patients.
>
> (b) Service. The gross income derived from personal and professional services of hospitals (other than hospitals operated as nonprofit corporations or by political subdivisions of the state), nursing homes, convalescent homes, clinics, rest homes, health resorts, and similar health care institutions is subject to business and occupation tax under the service and other activities classification. This classification also applies to nonprofit hospitals for personal or professional services which are performed for persons other than patients and not otherwise tax classified.

(Emphasis added.) Further, Taxpayer has been unable to provide any legislative history or other documentation in support of its argument that the legislature intended to extend the RCW 82.04.260(12) public and nonprofit hospital B&O tax classification to all business activities conducted by hospitals, and not just services to their inpatients. In fact, fiscal notes and other documents in the legislative history files[10] indicate an intent, or at least a legislative understanding, that the new RCW 82.04.260(12) tax rate (initially at .75%) would be imposed on only that non-

[9] Filed May 17, 1994 and effective 31 days later.
[10] Archives Division, Office of the Washington Secretary of State.

profit hospital revenue which had previously been deductible,[11] i.e., revenue received from hospital services to inpatients as previously interpreted by Group Health.

[3] As demonstrated by the phrase "services to patients" in Rule 168(3)(a), the Department has determined that the legislative intent of RCW 82.04.260(12), as discussed above, was to extend the special rate to hospitalization services rendered by nonprofit hospitals to inpatients. Additionally, for departments and services available to both inpatients and outpatients -- e.g., emergency rooms, radiology services, and laboratories -- the RCW 82.04.260(12) rate will be applicable to those that are an "integral, interrelated and essential part" of the hospital using the Group Health analysis.[12]

[4] In the case here at issue, Taxpayer claims interest received on overdue patient accounts receivable and physician transcribing fees should be taxed after June 30, 1993 under the RCW 82.04.260(12) rate, instead of under the service and other activities rate. We disagree. The extension of credit, no matter how generous the terms might be, is not a hospitalization service. Taxpayer's petition as to this issue is denied.

[5] Similarly, Taxpayer's transcribing service is not a hospitalization service. The service is provided by Taxpayer to physicians, who pay for the service. It is a cost of doing business of physicians with hospital privileges. As with all office expenses, physicians pass this necessary expense on to their patients in their billings. It is a service rendered to doctors in the performance of their required medical duties, for which charges are billed to doctors, and not to hospital patients by Taxpayer. The transcribing service is not a hospitalization service rendered to patients. The fact that the doctors may be required to provide the transcriptions for the hospital's records does not change this analysis.

Taxpayer's petition as to these issues is denied.

As to Taxpayer's education classes, we have reviewed the BTA's decision in Good Samaritan Hospital v. Department of Rev., BTA Docket 90-10 (1992), aff'd 81 Wa. App. 1012 (1996) (Good Samaritan). Under that decision, educational offerings open to the general public lawfully qualified for the deduction under the pre-July 1, 1993 change in law under the Group Health analysis. The dissent also offered some compelling observations:

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[11] Representative language is as follows: "This bill . . . removes the B&O tax exemption for nonprofit hospitals. . . . Currently, . . . nonprofit hospitals do not pay B&O tax at all." See, Fiscal Note, Bill Number E2SSB 5304 as Passed by the Legislature, dated 5/4/93. We also note the Washington Supreme Court's observation in In re Sehome Park Care Center, 127 Wn.2d 774, 781, 903 P.2d 443 (1995), as follows: "Turning to the 1993 amendment to RCW 82.04.4289, we see that the legislature deleted hospitals from the statute entirely . . . . These [published bill summary] documents reveal that the thrust of the bill was to increase, rather than decrease, taxes in order to pay for health care reform."

[12] We note that Thurston County Superior Court in Empire Health Services v. Department of Rev., No. 99-2-00312-5 (Superior Ct., December 17, 1999), similarly concluded that, in order to qualify for taxation at the nonprofit hospital rate, a taxpayer must provide a service that relates to treatment in the hospital and must provide services that are unique to those provided in a hospital (Conclusion of Law No. 1, emphasis the Court's).

> I disagree with [the majority's] findings relating to the educational instruction provided by Good Samaritan. I find these services neither unique nor incidental to hospital purposes. They are primarily offered to either out-patients or non-patients of Good Samaritan. More importantly, I would argue the mere fact that only hospitals offer these services is insufficient grounds for exemption if the services are of the type which could be offered by others in the community outside the hospital setting. Unlike the services offered by a hospital, which would be very difficult to duplicate because of the facilities and equipment required to offer these services, there is no barrier to any physician, clinic, or even trained lay persons to offer the type of programs or services before us. At the present, one only need note the directories of US West Direct and find individuals and organizations, other than hospitals, professing to offer similar type instructions.

Since the BTA's Good Samaritan decision was issued in 1992, hospitals have generally increased their educational outreach to the general public. In reviewing Good Samaritan, we do not think an application of either the majority decision, or the dissent, any longer represents a valid interpretation of the law under Group Health.

[6] We, instead, hold that, under the rationale of Group Health, educational offerings open to, or provided to, the general public at the hospital will properly qualify as being an "integral, interrelated, and essential part" of the hospital operation if they are unique and incidental to the provision of hospitalization services (i.e., services which will be, have been, or are currently being provided to the students or participants). The mere fact that only a hospital might offer these educational services in a community is insufficient grounds for exemption if the services are of the type which could be offered by others outside the hospital setting. Only those educational programs and services offered by a hospital that would be very difficult or impossible to duplicate by a non-hospital because of the specialized body of knowledge, facilities and equipment required will qualify as a hospitalization service. Other educational programs and services will not be eligible for the public and nonprofit hospital classification rate when any physician, clinic, or even trained lay persons could offer them.

This issue of Taxpayer's Schedule 5 educational programs will be remanded to Audit, whereupon Taxpayer will be given the opportunity to present further facts relative to this issue.

. . . The conference is open to the public. We find the conference does not constitute either a hospital service to inpatients or a department or service that is an "integral, interrelated and essential part" of a hospital under Group Health. We therefore hold that the conduct of the " . . . Health Conference" in audit Schedule 2 is not eligible for either the RCW 82.04.4289 deduction prior to July 1, 1993, or for the RCW 82.04.260(12) classification effective that date.

Although Taxpayer claims Schedule 2's "Diet Consulting" is primarily a service provided to hospital inpatients (i.e., diabetics), the audit report is silent as to its nature. This matter is remanded to Audit for further review and adjustment, as necessary.

Audit's rationale for denying the RCW 82.04.260(12) public and nonprofit hospital classification to the educational programs in audit Schedule 5 for periods after June 30, 1993 is not clearly articulated. We believe, looking at the account names given, that Audit may not have considered these educational programs to be an "integral, interrelated, and essential part" of the hospital operation. If so, the RCW 82.04.260(12) rate was correctly denied. However, if any of these constituted counseling or educational services provided to inpatients, these services would be eligible for B&O tax treatment under the public or nonprofit hospital classification. This issue will be remanded to Audit for further analysis, and Taxpayer will be given the opportunity to present further arguments to Audit relative to this issue.

3. Radiology School Tuition. Taxpayer disagrees with the assessment of tax on tuition income for the Radiology Program, revenues that are a charge for instruction fees. According to Taxpayer, this revenue is similar in nature to the nursing education tuition which was deemed not to be taxable by the Board of Tax Appeals in Deaconess Hospital v. Department of Rev., Docket No. 79-26 (1980) (Deaconess). According to Taxpayer, the program is an accredited program for radiology technicians.

RCW 82.04.170 defines the term "tuition fee" as follows:

> "Tuition fee" includes library, laboratory, health service and other special fees, and amounts charged for room and board by an educational institution when the property or service for which such charges are made is furnished exclusively to the students or faculty of such institution. "Educational institution," as used in this section, means only those institutions created or generally accredited as such by the state and includes educational programs that such educational institution cosponsors with a nonprofit organization, as defined by the internal revenue code Sec. 501(c)(3), if such educational institution grants college credit for coursework successfully completed through the educational program, or an approved branch campus of a foreign degree-granting institution in compliance with chapter 28B.90 RCW, and in accordance with RCW 82.04.4332 or defined as a degree-granting institution under RCW 28B.85.010(3) and accredited by an accrediting association recognized by the United States secretary of education, and offering to students an educational program of a general academic nature or those institutions which are not operated for profit and which are privately endowed under a deed of trust to offer instruction in trade, industry, and agriculture, but not including specialty schools, business colleges, other trade schools, or similar institutions.

[Emphasis added.] RCW 82.04.4282 provides a deduction for bona fide tuition fees:

> In computing tax there may be deducted from the measure of tax amounts derived from bona fide . . . (5) tuition fees, (6) charges made by a nonprofit trade or professional organization for attending or occupying space at a trade show, convention, or educational seminar sponsored by the nonprofit trade or professional organization, which trade show, convention, or educational seminar is not open to the general public, ...

[Emphasis added.] WAC 458-20-167(3)(a), in effect from April 19, 1994 through February 7, 1999, provided that the service and other activities B&O tax applied to the following activities or sources of income:

> (1) **Introduction.** This section explains the application of Washington's B&O, retail sales, and use taxes to educational institutions
>
> (2) **Definitions.** For the purposes of this section, the following definitions apply:
>
> (a) The term "tuition fees" includes fees for instruction, library, laboratory, and health services. The term also includes special fees and amounts charged for room and board when the property or service for which such charges are made is furnished exclusively to the students or faculty of the institution.
>
> (b) "Educational institutions" means the following:
>
> (i) Institutions which are established, operated, and governed by this state or its political subdivisions under Title 28A, 28B, or 28C RCW.
>
> (i) Tuition fees received by private schools. However, educational institutions, as defined above, may deduct amounts derived from tuition fees. (Refer to RCW 82.04.4282.)
>
> . . . (iii) Degree-granting institutions offering educational credentials, instruction, or services prerequisite to or indicative of an academic or professional degree or certificate beyond the secondary level, **provided the institution is accredited by an accrediting association recognized by the United States Secretary of Education and offers to students an educational program of a general academic nature.**
>
> . . . (v) On and after July 1, 1993, the term includes educational programs that an educational institution cosponsors with a nonprofit organization, as defined by the Internal Revenue Code Sec. 501 (c)(3), provided that educational institution grants college credit for course work successfully completed through the educational program. (See chapter 18, Laws of 1993 sp.s.)

(Emphasis added.) In Deaconess, cited by Taxpayer, the School of Nursing was held to be a qualifying institution. This program offered a three year diploma program, and graduates were prepared to take the Registered Nurse licensing examination. Its curriculum was approved and accredited by the Washington State Board of Nursing. Certain credits from the program could be transferred to other state institutions. Students in the program attend any paid [sic] tuition directly to an accredited college for certain required courses in the nursing program, and the program was designed to educate well rounded individuals with the ability to function as professional nurses. For these reasons, the School of Nursing was found not to be a "specialty school."

[7] The Board found the School of Nursing to be generally accredited as such by the state and to offer to its students a program of a general academic nature appropriate to the profession of a nurse. The Board further found that it was not a specialty school, trade school or other similar institution. See also, Det. 87-297, 4 WTD 75 (1987), wherein a Bible college's curriculum was found to be of a sufficiently general academic nature to qualify for deduction of tuition fees.

In this case, Taxpayer has alleged only that the Radiology School is "similar to" the Nursing School in Deaconess. We will concede the obvious - that they both train health care workers. However, Taxpayer has not alleged that the Radiology School is accredited, offers a program of a general academic nature, or otherwise qualifies under the above-cited statutes for deduction. Tax deductions are narrowly construed. Lacey Nursing v. Dept. of Revenue, 128 Wn.2d 40, 49-50 (1995). Because facts supporting the deduction have not been alleged and proven, Taxpayer's Radiology School will be considered to be a trade or specialty school. Taxpayer's petition as to this issue is therefore denied.

4. Emergency Room Physicians. Taxpayer objects to tax on amounts received and paid to its emergency room physicians, relying on Det. No. 88-208, 5 WTD 403 (1988). Taxpayer contends that its facts are comparable to the facts in the published determination. Taxpayer contends that the BTA decision cited by the auditor, Charles Pilcher, M.D. v. Department of Rev., BTA Docket No. 46920 (1996) (Pilcher), concerned the relationship between emergency room physicians sharing revenue among themselves after receiving it from the hospital, a factual situation not germane to this case. In this case, Taxpayer argues that it is merely the billing agent for its emergency room physicians, who are independent contractors. According to Taxpayer, the hospital bills the doctors' fees as agent of the doctors, and has no legal right to keep those fees as its own. In support of these arguments, Taxpayer has provided us with a copy of its Emergency Care Agreement (Agreement) with [Emergency Room Physicians].

As to whether the billings by Taxpayer on behalf of the emergency room physicians were correctly taxable, WAC 458-20-111 (Rule 111) deals with the exemption for "advances" and "reimbursements":

> The words "advance" and "reimbursement" apply only when the customer or client alone is liable for the payment of the fees or costs and when the taxpayer making the payment has no personal liability therefor, either primarily or secondarily, other than as agent for the customer or client.
>
> . . .
>
> The foregoing is limited to cases wherein the taxpayer, as an incident to the business, undertakes, on behalf of the customer, guest or client, the payment of money, either upon an obligation owing by the customer, guest or client to a third person, or in procuring a service for the customer, guest or client which the taxpayer does not or cannot render and for which no liability attaches to the taxpayer. It does not apply to cases where the customer, guest or client makes advances to the taxpayer upon services to be rendered by the taxpayer or upon goods to be purchased by the taxpayer in carrying on the business in which the taxpayer engages.

(Emphasis added.)

Taxpayer argues the cases on which Audit relied are not applicable to its situation. We agree that the issues involved in these decisions did not concern the tax liability of a hospital for patient receipts passed through to its emergency room physicians.[13]

Taxpayer instead urges us to rely on Det. No. 88-208, 5 WTD 403 (1988), arguing that in that case, as in the instant case, the hospital was merely a billing agent for its emergency room physicians. Taxpayer argues that, in both cases, the hospitals bill fees on behalf of their emergency room doctors, all of whom are independent contractors, as the doctors' agents, and have no legal right to keep the fees, once received, as their own.

Det. No. 88-208, supra, does in fact concern the taxation of amounts paid to a hospital and passed through to physicians supplying emergency care on an "on call" basis. The hospital-taxpayer billed patients for their emergency room care. Patient billings contained a "professional component," representing the physician's services, and a "technical component," consisting of the hospital's contribution toward the service rendered (i.e., medical/surgical/pharmaceutical supplies plus equipment rental). In Det. No. 88-208, amounts paid to the taxpayer-hospital were held to be excludable "advances." Some of the factors leading to that conclusion include:

(a) In billing patients for the "professional component," the name of the physician who provided the care was clearly stated on the itemized bill.
(b) If an emergency room patient did not pay the physician's fee, the physician suffered the loss without recourse to the hospital for payment.
(c) The hospital-taxpayer did not retain any part of the physician's fees; they were entirely remitted to the physicians.
(d) The physician had sole discretion in setting the professional fees to be charged to patients.
(e) The "on call" physicians who made themselves available on an emergency basis were not employees of Taxpayer (there being insufficient supervision or control over their professional and business activities). Because the emergency room physicians' primary contractual relationships were with their patients (they were retroactively deemed to be the patients' primary care physicians), and because the hospital-taxpayer itself was found to have no obligation to render emergency medical care to patients, the "on call" physicians were held not to be subcontractors of the hospital.

In the case here at hand, however:

(a) Taxpayer's patient billings reflect the entire amount of the emergency room charge. Patients are not advised they have contracted with a third party for services rendered. (Agreement, para 14.)

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[13] Det. No. 86-305, supra, concerned a pathology laboratory co-located with a second party and sharing and receiving reimbursement for its facilities, personnel, equipment and supply expenses. Det. No. 87-340, supra, similarly dealt with two physicians sharing office space and expenses. Det. No. 91-023, supra, ruled on the tax consequences of a corporation receiving payment for providing emergency room physicians to a hospital when the majority of income was passed through to the individual physicians hired by that taxpayer to perform the medical services. The BTA decision in Pilcher, supra, concerned the taxation of the physician who contractually undertook the full-time provision of emergency room care to a hospital, and passed those payments along to the physicians he hired to help him provide the service.

(b) The emergency room physicians were paid their agreed-upon fee percentages by Taxpayer even if emergency room patients did not pay their bills. (Agreement, para 7.)
(c) The emergency room physicians did not receive all of their fees; Taxpayer paid [Emergency Room Physicians] only . . . (now . . .) percent of total patient billings for the previous month. Taxpayer absorbs the cost of uncollectible amounts (Agreement, para 7.)
(d) Taxpayer did not allow emergency room physicians sole discretion in setting their fees; patient fees are set at competitive rates and must be agreed to by both [Emergency Room Physicians] and Taxpayer (Agreement, para . . . .)
(e) The emergency room physician contract indicates, by virtue of a covenant-not-to-compete, that emergency room patients are considered to be Taxpayer's patients. (Agreement, para 17.)

[8] Because of the above attributes of Taxpayer's contracts with emergency room physicians, we must conclude that payments received by Taxpayer were not properly excludable as "advances and reimbursements" under Rule 111. Patient billings did not indicate that that their billings were on behalf of the physicians, and did not even identify the physicians by name. Unlike the taxpayer in Det. No. 88-208, Taxpayer's role in collecting and paying physicians' professional fees was more than that of a mere agent. Taxpayer's contractual obligation to pay its emergency room physicians was completely independent of the collections actually made. Although the amount owed physicians for future periods could be reviewed and adjusted to allow for uncollectables and contractual allowances, even these adjustments for future periods would be mere approximations. Taxpayer's liability to its emergency room physicians was absolute, and Taxpayer was therefore primarily liable for the emergency room physician fees.

Lastly, Taxpayer's own contract with [Emergency Room Physicians] made it clear that the patients were those of the Taxpayer and not the physician. Taxpayer contracted with these physicians to actually staff its emergency room on an ongoing basis, and to provide other related services deemed necessary to Taxpayer's operation. Taxpayer, by contracting with the physicians, was merely procuring the professionals necessary for Taxpayer to render its emergency service to patients. Thus, the following necessary elements of Rule 111 were not met: First, the patients alone were not liable for the emergency room physicians' fees – Taxpayer, by its contract, was liable for their payment whether or not patients paid their bills. Second, Taxpayer's contract makes it clear that patients coming to the emergency room for treatment are Taxpayer's patients, and are thus being supplied emergency treatment by Taxpayer through its subcontractors; in doing so, Taxpayer is not "procuring a service for the customer . . . which the taxpayer does not or cannot render and for which no liability attaches to the taxpayer."

Because the necessary elements of Rule 111 have not been met, Taxpayer's petition as to this issue is denied.

5. CHAMPUS. Taxpayer has consistently taken a B&O tax deduction as a health or social welfare organization for treatment of patients under the CHAMPUS program. Taxpayer objects to the auditor's characterization of these revenues as received under "one of the United States government health insurance plans for employees and dependents," i.e., an employee benefit plan, arguing that the auditor has been unable to provide Taxpayer with any written documentation to justify this

position. Taxpayer argues that CHAMPUS does not cover active duty military personnel, and is a program solely for dependents of the military. Taxpayer further argues that for there to be an "employee benefit plan," there must first be "employees," and military members are not "employees." Taxpayer further argues that the CHAMPUS program is not similar to the health insurance programs offered by the federal government to its civilian employees.

As to the deductibility of CHAMPUS revenues, RCW 82.04.4297 provides an exemption from B&O tax for:

> . . . amounts received from the United States or any instrumentality thereof from the state of Washington or any municipal corporation or political subdivision thereof as compensation for, or to support, health or social welfare services rendered by a health or social welfare organization or by a municipal corporation or political subdivision, except deductions are not allowed under this section for amounts received under an employee benefit plan.

(Emphasis added.)

For Taxpayer to deduct CHAMPUS revenues under RCW 82.04.4297, therefore:

(1) Payment must be received from the United States,
(2) The compensation must be for "health or social welfare services,"
(3) Taxpayer must be a "health or social welfare organization. and."
(4) Payment must not be for amounts received under an "employee benefit plan."

Because the first three elements were not discussed in either the audit report or Taxpayer's petition, we will assume, without a finding, for the limited purpose of resolving this administrative appeal, that the first three elements were satisfied. Therefore, the issue before us is whether payments by CHAMPUS were received under an "employee benefit plan."

Taxpayer has always treated CHAMPUS revenue as deductible under RCW 82.04.4297. Taxpayer disagrees with Audit's characterization of CHAMPUS as an employee benefit plan. Taxpayer instead argues that CHAMPUS does not cover active military personnel, but is a program solely for dependents of the military. Thus, Taxpayer argues, there must be employees before there can be "an employee benefit plan," and "soldiers are not employees." Taxpayer has presented, in support of its argument, a letter from a third party attorney (the letter), which states:

> This definition [of "employee benefit plan in RCW 82.04.293] establishes four major types of arrangements which constitute employee benefit plans, namely: ERISA covered plans; arrangements which enjoy special federal tax treatment; similar plans maintained by state or local governments; and self-insured benefits mandated by federal, state or local law.

The letter further argues that the definition in RCW 82.04.293 is the "common understanding" of "employee benefit plan," and goes on to explain "our view" of the "common meaning" of that term. In particular, the letter states:

> We believe[14] that employee benefit plans are characterized by the following:
>
> 1. Benefits under employee benefit plans are not mandated by law.
> 2. The level of benefits is determined by the employer or by agreement between the employer and the employee(s).
> 3. Benefit levels are often subject to unilateral change by the employer.
> 4. Benefits arise out of, and in the context of, the employer-employee(s).
> 5. Benefits are often regulated by ERISA.
>
> CHAMPUS is very different form an employee benefit plan. The following is a partial list of these differences:
>
> 1. Coverage under CHAMPUS is "not a mere act of grace . . . [it is] a full-fledged matter of right." Barnett v. Weinberger, 818 F.2d 953, 957 (D.C. Cir. 1987).
> 2. CHAMPUS coverage satisfies a "statutory entitlement to medical care."
> 3. CHAMPUS is not covered by ERISA (See, McGee v. Funderburg, 17 F.3d 1122, 1125 (8th Cir. 1994)).
> 4. Benefits arise not out of the employment contract, but as "an earned entitlement in gratitude for services [by members of the armed forces] to their country and as a means of making more attractive service in the armed forces of the United States." Id. at 1125.
> 5. Benefits levels are statutorily determined.
>
> We believe that CHAMPUS is not an employee benefit plan. In our view, it is a government entitlement program. . . .

As Taxpayer has correctly noted, RCW 82.04.293 (which relates to B&O taxes applied to international investment management services) defines an "employee benefit plan" as including:

> . . . any plan, trust, commingled employee benefit trust, or custodial arrangement that is subject to the Employee Retirement Income Security Act of 1974, as amended, 29 U.S.C. Sec. 1010 et seq., or that is described in sections 125, 401, 403, 408, 457 and 501(c)(9) and (17) through (23) of the internal revenue code of 1986, as amended, or a similar plan maintained by a state or local government, or a plan, trust, or custodial arrangement established to self-insure benefits required by federal, state, or local law.

(Emphasis added.)

Taxpayer has further admitted that:

[14] We note that no authority is given for these beliefs.

> CHAMPUS is a program of medical benefits provided by the U.S. Government under public law to specified categories of individuals who are qualified for these benefits by virtue of their relationship to one of the seven Uniformed Services.

(32 CFR 199.1(d), emphasis added.) The history and intent of CHAMPUS has been more fully described in Barnett v. Weinberger, 818 F.2 953 (1987):

> Traditionally, dependents of members of the Armed Forces have been provided health care in military facilities whenever the space and staff essential thereto could be utilized without jeopardizing medical service to personnel on active duty. The dependent-care practices long pursued in military circles, however, left much to be desired. Positive statutory authority to accommodate dependent medical service was fragmentary; this bred disparities in the types of care afforded and the categories of dependents able to seek them. Moreover, an estimated 40 percent of dependents could not obtain medical care in military facilities, primarily because of overcrowding, physician shortages, or residence outside the areas served by those facilities. Inadequacies of these sorts in the dependent medical care system in vogue generated what ultimately came to be recognized as "one of the most serious morale problems facing our Armed Forces.
>
> In 1956, Congress passed the Dependent's Medical Care Act [codified as 10 U.S.C. § 1071, et seq.] as the means of rectifying these shortcomings. The broad purpose of the Act was "to create and maintain high morale throughout the uniformed services by providing an improved and uniform program of medical care for members of the uniformed services and their dependents." Uniformity was attained by explication of the types of medical care that can and cannot be provided and precise definition of the categories of dependents eligible for them. The principal improvement was authority to contract for provision of medical care by civilian hospitals and physicians to dependents of active-duty military personnel, thus increasing the availability of medical services beyond the capacity of military hospitals and staffs. Ten years later, by the Military Medical Benefits Amendments of 1966, medical care available to dependents of active-duty personnel was expanded even further, and still other changes have been wrought by subsequent legislation.
>
> This legislation also enlarged the class of beneficiaries by establishing inpatient and outpatient programs in civilian facilities for retired military personnel, their spouses and children, and spouses and children of deceased active-duty and retired personnel,. . . and by inaugurating a new program of financial assistance for mentally retarded or physically handicapped dependents of active-duty personnel. . . .
>
> The truly outstanding feature of the Dependents' Medical Care Act, however, is that it converted the provision of military-dependent medical care from a mere act of grace to a full-fledged matter of right. The Act specifies, in the respects pertinent to this case, that "[a] dependent of a member of a uniformed service who is on active duty for a period of more than 30 days . . . is entitled, upon request, to the medical and dental care proscribed by [the

> Act] in facilities of the uniformed services, subject to the availability of space and facilities and the capabilities of the medical and dental staff." And, "to assure that medical care is available for spouses and children of members of the uniformed services who are on active duty for a period of more than 30 days," the Act commands the Secretary of Defense, "after consulting with the other administering Secretaries, [to] contract . . . for medical care for those persons under such insurance, medical service, or health plans as he considers appropriate." With but a single exception, an eligible dependent may elect to receive authorized medical care either in a military facility or a facility provided under a plan contracted for. As the House Report declared, "for the first time in the history of the uniformed services, dependents will be provided with a statutory entitlement to medical care on a uniform basis throughout all the uniformed services."

(Emphasis added; citations and footnotes omitted.) It is clear that CHAMPUS is "a plan . . . established to self-insure benefits required by federal . . . law" as described in the RCW 82.04.293 definition of "employee benefit plan."

We further find no support for Taxpayer's "beliefs" that, because a plan is a statutorily determined matter of right, because it is a governmental plan not regulated by ERISA, and because it is described as "an earned entitlement" for dependents "in gratitude" for the services of those in the military, that it is not an "employee benefit plan." Indeed, even though ERISA does not regulate "governmental plans" such as CHAMPUS,[15] ERISA's definition of "employee benefit plan" in 29 USC § 1002(1) (1998) is all-inclusive:

> The term "employee welfare benefit plan" and "welfare plan" means any plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or by an employee organization, or by both, to the extent that such plan, fund, or program was established or is maintained for the purpose of providing for its participants or their beneficiaries, through the purchase of insurance or otherwise.

[Emphasis added.] Neither is Taxpayer's contention that military personnel are not "employees" well-taken. Such a conclusion would come as a surprise to many agencies and courts. See, for example: In re Kraft, 119 Wn.2d 438; 832 P.2d 871 (1992);[16] Kirtley ex rel. Kirtley v. Washington,

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[15] (b) The provisions of this title shall not apply to any employee benefit plan if--
(1) Such a plan is a governmental plan (as defined in section 3(32) [29 USCS § 1002(32)]). 29 USC 1003(b)(1). 29 USC § 1002(32), in turn, provides: "The term 'governmental plan' means a plan established or maintained for its employees by the Government of the United States, by the government of any State or political subdivision thereof, or by any agency or instrumentality of any of the foregoing. The term "governmental plan" also includes any plan to which the Railroad Retirement Act of 1935 or 1937 applies, and which is financed by contributions required under that Act and any plan of an international organization which is exempt from taxation under the provisions of the International Organizations Immunities Act (59 Stat. 669).

[16] Concerning inequity in divorce decrees because of "the payment of disability benefits to the military employee . . . ."

49 Wn.App. 894, 748 P.2d 1128 (1988);[17] In re Parks, 48 Wn.App. 166, 737 P.2d 1316 (1987);[18] Baker v. Baker, 91 Wn.2d 482, 588 P.2d 1164 (1979);[19] Wilder v. Wilder, 85 Wn.2d 364, 534 P.2d 1355 (1975);[20] Payne v. Payne, 82 Wn.2d 573, 512 P.2d 736 (1973);[21] O'Connell v. United States, 110 F. Supp. 612, U.S. District Court for the Eastern District of Washington, Southern Division (1953).[22]

Lastly, Taxpayer has argued that an employee benefit plan does not normally grant dependents different benefits than those provided to the employees themselves. No authority is cited for this proposition.

Active duty members of the military are provided medical and dental care "in any facility of any uniformed service."[23] We take administrative notice, however, that the health and dental care requirements of active duty military personnel often differ significantly from those of their civilian dependents. The health and dental records of active duty personnel are official military files that impact on members' duty assignments, training, promotions, and retention. Input into these files is standardized under military regulations and, normally, only military health and dental authorities are authorized to provide input into and maintain such files. Active members of the uniformed services are deployable into combat zones, aboard ships, and to remote locations where civilian health care is unavailable or unsuitable. Civilian dependents located in the continental United States, on the other hand, normally have access to adequate civilian care. The law recognizes and accommodates these differences.

[9] For the reasons articulated above, we conclude that CHAMPUS is clearly an employee health benefit plan, and amounts received under CHAMPUS are ineligible for the RCW 82.04.4297 deduction.[24] Taxpayer's petition as to this issue is therefore denied.

6. Installation Expense. According to Taxpayer, the . . . "installation expenses" noted on Schedule 8 of Taxpayer's 1993 and 1994 audit were neither expenses for the installation of computer hardware nor for the loading of software into the hardware. These amounts were all for training and educating hospital staff in actual use of the systems. Most of the training took place at the hospital. A small portion of the . . . training may have taken place at the . . . training

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[17] Concerning the question of whether civilian technicians were state or federal employees. The Court held that civilian as well as military employees of the National Guard are to be treated as state employees for purposes of the Federal Tort Claims Act.

[18] " . . . military pension is deferred employee compensation . . . ."

[19] "For purposes of property dissolution, this court has characterized military retirement pay as a form of employee compensation."

[20] Contingent military pensions are to be considered deferred compensation for purposes of the disposition of property in a dissolution, even though "an element of uncertainty may exist as to whether a particular employee will receive the benefits."

[21] "A military pension is a mode of employee compensation . . . ."

[22] Concerning measures of liability of the United States for the actions "of military employees" versus those of "civilian employees."

[23] 10 USC 1074(a).

[24] We note that the Thurston County Superior Court reached a similar conclusion in Empire Health Services v. Department of Rev., No. 99-2-00312-5 (Superior Ct., December 17, 1999).

center. Taxpayer relies upon Det. No. 89-43, 7 WTD 130-1 (1989), affirmed 89-43A, 8 WTD 5 (1989), in maintaining that the training activity is not subject to sales or use tax.

[10] We agree that training costs, of payments to a vendor of canned computer programs for the training of employees to use those programs, are not subject to sales or use tax when separately negotiated and severable from purchase of the canned program. Det. No. 89-43, supra. This matter will be remanded to Audit for further analysis and adjustment, if indicated.

7. Pathology Substances. Certain items . . . – items used "to fix samples, stains, and decolorizers" -- are used to diagnose disease. Taxpayer argues that, pursuant to Deaconess Medical Center, et al. v. Department of Rev., Docket Nos. 85-186, 86-29 (1987) ("38 Hospitals"), Taxpayer was given credit for these items. Taxpayer argues that it seems as if the Department of Revenue is now attempting to negate the benefit taxpayers won in 38 Hospitals by a mere notification that the decision therein was incorrect. The Department is doing this without the benefit of any supporting documentation that would offer evidence of the Department's authority to override the 38 Hospitals order. Taxpayer believes the auditor's instructions are invalid and without basis.

RCW 82.04.0281 and RCW 82.12.0275 provide parallel retail sales tax and use tax exemptions for "prescription drugs":

> The term "prescription drugs" shall include any medicine, drug, . . . or other substance . . . for use in the diagnosis, cure, mitigation, treatment, or prevention of disease or other ailment in humans . . . .

WAC 458-20-18801 (Rule 18801) provides as follows:

> (5) **Exemptions.** The following exemptions apply from the retail sales tax and use tax.
> . . . (c) Laboratory reagents and other diagnostic substances are exempt from retail sales tax when used as part of a test prescribed to diagnose disease in humans. These items include, among others, reagents, calibrators, chemicals, gases, vacutainers with heparin or other chemicals or medicines, and prepared media. Control reagents are exempt, but only when the control reagents are used in performing tests prescribed for a patient. Reagents which are used to merely calibrate equipment and are not related to a test prescribed for a specific patient are not exempt.

Taxpayer has, since the audit, identified an extensive number of "tissue substances" used in its laboratory,[25] all of which it claims fall within the RCW 82.08.0281 and Rule 18801(5)(c) definitions of "other substances used in the diagnosis . . . of disease . . . in humans." Because the Audit Division did not identify which of these substances were thought to be taxable, we remand this issue back to that division for further clarification with the following general guidelines:

[25] Listed above.

Because the terms "laboratory reagents" and "other diagnostic substances" are used in a medical context in Rule 18801, we have determined the applicable reference source for defining these terms is a medical dictionary.[26] Dorland's Illustrated Medical Dictionary, 27th Edition ("Dorland's"), defines "reagent" as: "A substance employed to produce a chemical reaction so as to detect, measure, produce, etc., other substances."[27]

Dorland's further defines "diagnostic" as: "Pertaining to or subserving diagnosis; distinctive of or serving as a criterion of a disease, as signs and symptoms." In order to be a "diagnostic substance" under this definition, application of the substance to a specimen must result in the identification of the characteristics of a particular disease.

Some of the substances at issue in this appeal will not fall within this definition because they are used by taxpayer solely for the purpose of either physically preparing specimens for examination and diagnosis, or to facilitate examination of a specimen by the pathologist. They do not themselves produce a chemical reaction resulting in the detection, measurement, or production of anything, let alone a diagnosis.

Other substances may not be used in a "test" to diagnose disease in humans. Webster's New Riverside University Dictionary, Second Edition, defines "test" in the context of chemistry as: "a. A physical or chemical reaction by which a substance may be detected or its properties ascertained; b. the reagent used in such a determination." Certain of Taxpayer's substances are not used in diagnostic tests per se, but are used to prepare specimens for diagnosis by the pathologist. As such, they are not tax exempt. To concede a more liberal definition of the terms "laboratory reagents," "other diagnostic substances," or "test" under Rule 18801 would violate the principle of statutory construction that an exemption in a statute imposing a tax must be strictly construed in favor of the application of the tax and against the person claiming the exemption.[28] Under taxpayer's broad interpretation of these terms any substance, no matter how remotely related to a diagnostic test, would be tax exempt.

[11] Accordingly, we hold that those substances used by taxpayer in its laboratory to prepare specimens for diagnosis which do not meet the foregoing definitions of "laboratory reagents" or "diagnostic substances," or which are not used as part of a "test" prescribed to diagnose disease in humans, do not fall within the scope of the prescription drug exemption. In short, any substance which merely facilitates or enables specimen testing, or which enhances the theater in which such tests are performed, are not within the scope of the statutes and administrative rules which exempt prescription drugs from retail sales and use taxes.

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[26]Lay definitions of these terms do not differ substantially from the medical definitions. For example, Webster's New Riverside University Dictionary, 2nd Edition, defines "reagent" as: "A substance used in a chemical reaction to detect, examine, measure, or produce other substances." The term "diagnostic" is defined as: "Of, relating to, or used in a diagnosis."

[27]There is no significant difference between this definition and the general description of "laboratory reagents" found in Rule 18801(8), which states: "Laboratory reagents are chemical compounds used to promote reactions in the laboratory to aid in determining disease pathology . . . ."

[28]See, e.g., Department of Revenue v. Schaake Packing Co., 100 Wn.2d 79, 666 P.2d 367 (1983).

As a result of this analysis, the Department has determined that stains, dyes, and decolorizers used by pathologists in the diagnosis of disease react with and cause a change in cellular tissue. These substances are often used to stain cell tissues in a manner that will mark, or highlight, certain portions of cells. For example, a particular stain might react with the cell, color the nucleus purple, and leave the surrounding cytoplasm pink. When used in this manner, such substances are exempt from retail sales/use tax.

Fixatives, decalcifying solution, dehydrating solution and clearing reagents are exempt reagents. Fixatives are generally used as a reagent. Immediately after removal from the body, tissues are placed in a fixative. The fixative reacts chemically with the tissue to preserve and retain its structure. Decalcifying solution chemically reacts with samples to remove calcium from the surrounding tissues. Dehydrating solutions remove the water from a sample. Typically, the water is replaced with a medium that allows the tissue to be thinly sliced for analysis. After dehydrating solution is used, a clearing reagent may be used to clear the dehydrating solution from the cell. Each of these four substances is a reagent because it chemically reacts with the sample.

Paraffin and gelatin are not reagents. Paraffin does not pass through the cell membrane. Rather, paraffin is used to provide structure by filling the empty space between cells. Since paraffin does not react with the cells, it can be extracted from a tissue sample without having chemically altered the cells. Typically, paraffin must be extracted before staining. Unlike paraffin, gelatin can pass through the cell wall. However, it does not cause a reaction. The gelatin coexists with the cell's cytoplasm. It does not exert any pressure to force the cytoplasm out of the cell or react in any way with the cell. Gelatin is typically used in a water bath to help the tissue adhere to the slide. Like paraffin, it is extracted out of the sample before staining, and leaves the cell structures unaffected.

Certain substances have multiple uses. For example, one such substance is alcohol, which can either be used to react with cellular tissue or clean counters.[29] Such substances are exempt only when used to react with cells.

This issue is remanded to Audit for further review and adjustment, as indicated.

DECISION AND DISPOSITION:

Taxpayer's petition is granted for the following issues:

- Morgue rental is a rental of real estate. The assessment will be cancelled.

Taxpayer's petition is denied relative to the following issues:

- Rule 111 treatment for the emergency room physician revenues
- RCW 82.04.4289 deduction and RCW 82.04.260(12) B&O tax classification for the . . . Health Conference

[29] We recognize that various grades might be purchased for various uses.

- RCW 82.04.260(12) tax classification for interest on overdue patient accounts
- RCW 82.04.260(12) tax classification for physician transcribing services
- RCW 82.04.4282 deduction for Radiology Training tuition
- RCW 82.04.4297 exemption for CHAMPUS payments

The following issues are remanded to Audit for further analysis and adjustment, if indicated:

- RCW 82.04.260(12) B&O tax classification as applied to Schedule 5's education classes
- RCW 82.04.4289 deduction and RCW 82.04.260(12) B&O tax classification for Schedule 2's "diet consulting"
- Use tax issue as to Schedule 8's "Installation expenses"
- Retail sales/use taxability of pathological supplies

Dated this 31st day of January, 2001.