

Cite as Det. No. 98-037, 23 WTD 171 (2004)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Correction of)	<u>D E T E R M I N A T I O N</u>
Future Instructions)	
)	No. 98-037
)	
...)	Registration No. . . .
)	FY . . . /Audit No. . . .
)	
)	

RULE 183; RCW 82.08.020, RCW 82.04.050(3)(a), RCW 82.04.4282: RETAILING B&O TAX -- RETAIL SALES TAX -- DEDUCTION -- GOLF AND COUNTRY CLUB -- BONA FIDE INITIATION FEES AND DUES. From total amounts paid by its members, a country club may deduct the portions allocated for proprietary interests the members have in the club and the amount of membership fees they paid for the privilege of belonging to the club. The balance was payment in exchange for a service, the privilege to play golf, and was subject to retail sales tax and retailing B&O 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:

A non-profit corporation (the taxpayer) protests instructions it was given by the Department of Revenue (the Department) for future tax-reporting periods.¹

FACTS:

De Luca, A.L.J. -- The taxpayer is a private golf and country club. It has three classes of memberships. The first class is "regular," which allows its members to golf . . . ; socialize at the clubhouse; and vote for new members, officers, the board of directors and other taxpayer

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

business. The taxpayer issues a certificate of membership to each regular member, which includes his/her spouse. A certificate of membership evidences ownership in the taxpayer's property. Upon dissolution of the taxpayer, a regular member is entitled to a pro rata share of the remaining assets after debts have been paid. Likewise, upon terminating a membership, a regular member is given the portion of his/her initiation fee that represents his/her share of stock in the corporation. The certificate has a value that is fixed thereon from time to time by the taxpayer's board of directors. The taxpayer's bylaws require the regular members to pay all dues and assessments with respect to membership. During the subject period new regular members were charged a fee of \$ The amount includes a one-time "initiation fee" of \$. . . ; a membership certificate valued at \$. . . ; and a registration fee of \$ During 1996, regular members also paid monthly dues of \$. . . and in 1997 their monthly dues were \$ We understand that regular members do not pay green fees when they play golf.

The taxpayer also has . . . (social members). Social members have the rights and privileges of a regular member to use the club property except the golf course. Social members do not vote and do not have proprietary interests in the taxpayer because they do not have certificates of memberships. The board of directors establishes rules and regulations that permit social members to use the golf course upon payment of designated green fees. Social members pay a one-time "initiation fee" of \$ During 1996, social members paid monthly dues of \$. . . and in 1997 they paid \$

The third class of membership includes (clubhouse members). They pay a one-time initiation fee of \$ They have the same rights and privileges of regular members to use the clubhouse facilities only. Clubhouse members do not have voting rights or proprietary interests in the taxpayer. During 1997, clubhouse members paid monthly dues of \$

The Department's Audit Division (Audit) reviewed the taxpayer's books and records for the period January 1, 1992 through June 30, 1996 and assessed \$. . . in taxes and interest. Audit noted in its report that the taxpayer had reported its income as it had been instructed in a previous audit. Therefore, Audit made no adjustments to the way the taxpayer had reported its initiation fees and dues. However, Audit informed the taxpayer that [it would be] required . . . for future periods to modify the way it computed its initiation fees and dues for retailing business and occupation (B&O) tax and retail sales tax purposes.

Specifically, Audit instructed the taxpayer to report the \$. . . registration fee for regular members as income subject to service B&O tax. Audit found the \$. . . paid by regular members for the membership certificates represented "stock ownership" in the taxpayer where regular members can participate in the decision-making process. Audit stated that the [membership certificate charge] represents a regular member's "proportional equity position in the club" and determined that it was not subject to tax.

Audit divided the remaining \$. . . paid by regular members into taxable and non-taxable amounts. It found non-taxable portions are for only the "privilege of membership." The remaining amounts are taxable, according to Audit, because they are for the right or privilege to

receive goods and services provided by the taxpayer, including the unrestricted use of the golf course with no additional charges for green fees. Specifically, Audit referenced the \$. . . “initiation fee” paid by social members, which accords them the same rights and privileges of a regular member except for use of the golf course, to establish the value of membership only. Audit found the \$. . . paid by the social members to be tax-exempt “bona fide initiation fees.” Likewise, Audit found [initiation fee amount paid by social members] of the remaining \$. . . “initiation fee” paid by regular members to be tax exempt. However, Audit instructed the taxpayer that the \$. . . balance should be reported as retail sales because it is money paid by regular members for the privilege of receiving goods or services (golfing privileges) other than nominal membership. . . .

Similarly, Audit examined the monthly dues paid by the regular members (\$. . .) compared to the monthly dues paid by social members (\$. . .) during 1996. Audit found the difference (\$. . .) between the dues rates represented the available use of the golf course allowed regular members. Audit declared the \$. . . was subject to retail sales tax and retailing B&O tax because that difference was attributed to the value of goods or services rendered to regular members.

TAXPAYER’S EXCEPTIONS:

The taxpayer does not contest the amount of taxes and interest assessed in the audit report. It also agrees that service B&O tax is due on the \$. . . administrative charges and claims it has paid tax on that income. Therefore, we will not discuss either the amounts assessed or the \$. . . administrative charge any further. Similarly, the taxpayer agrees that the \$. . . certificate-of-membership fees are exempt from tax. However, the taxpayer protests Audit’s instructions for future reporting that classify the remaining \$. . . paid by regular members as retail. Instead, the taxpayer contends that the entire \$. . . fees paid by regular members are exempt as bona fide initiation fees because regular members have received no services or goods in exchange for these fees and are not entitled to any future benefits in exchange for the fees. Furthermore, the entire \$. . . must be paid before a regular member is entitled to the privileges of the club. Additionally, the taxpayer explains it charges dues to its regular members that are in excess of the direct and indirect expenses incurred.

The taxpayer quotes sections of RCW 82.04.4282 and WAC 458-20-183 (Rule 183) that allow as a deduction from the measure of the tax amounts derived from bona fide initiation fees. The taxpayer also cites Det. No. 86-310, 2 WTD 91 (1986) and Det. No. 94-062, 14 WTD 225 (1995) in support of its argument that dues and initiation fees are taxable only when there is an exchange of goods and services without any additional charge to the member. Furthermore, the taxpayer asserts that the regular members’ mere privilege of having facilities available to them, or, their mere privilege to receive goods and services, is not taxable. In other words, the taxpayer argues that the mere privilege to play golf is not taxable. Instead, the taxpayer insists golf must be played before it is a taxable event.

Finally, the taxpayer believes that Audit improperly instructed it on how to report tax on the monthly dues. As noted, Audit instructed the taxpayer to report as a retail sale the difference

between the regular members' monthly dues and the social members' monthly dues. The taxpayer contends that it should report tax on the differences between the dues paid by regular members and clubhouse members and between social members and clubhouse members.

ISSUES:

1. Are the full \$. . . payments made by persons becoming regular members of the taxpayer's golf and country club deductible from the measure of the tax as bona fide initiation fees?
2. Is the measure of tax on monthly dues the difference between the amounts regular members pay and the amounts social members pay?

DISCUSSION:

The statutory authority for the deduction of bona fide initiation fees and dues is found in RCW 82.04.4282:

In computing tax there may be deducted from the measure of tax amounts derived from bona fide (1) initiation fees, (2) dues,. . . . This section shall not be construed to exempt any person, association, or society from tax liability upon selling tangible personal property or upon providing facilities or services for which a special charge is made to members or others. If dues are in exchange for any significant amount of goods or services rendered by the recipient thereof to members without any additional charge to the member, or if the dues are graduated upon the amount of goods or services rendered, the value of such goods or services shall not be considered as a deduction under this section.

The Department adopted WAC 458-20-183 (Rule 183) to administer RCW 82.04.4282. Rule 183 provides in part:

(4) Receiving income in the form of dues and/or initiation fees.

(a) **General principles.** For the purposes of the business and occupation tax, all amounts derived from initiation fees and dues must be reported as gross income which then must be apportioned between taxable and deductible income. The following general principles apply to providing amusement, recreation, and physical fitness services when income is received in the form of dues and/or initiation fees:

(i) RCW 82.04.4282 provides for a business and occupation tax deduction for amounts derived from activities and charges of essentially a nonbusiness nature. The scope of this statutory deduction is limited to situations where no business or proprietary activity (including the rendering of goods or services) is engaged in which directly generates the income claimed for deduction. Many for-profit or nonprofit entities may receive "amounts derived," as defined in this section, which consist of a mixture of tax deductible amounts (bona fide initiation fees and dues) and taxable amounts (payment for significant goods and services rendered). To distinguish between these kinds of income, the law requires that tax exemption provisions be strictly construed against the person claiming exemption. Also,

RCW 82.32.070 requires the maintenance of suitable records as may be necessary to determine the amount of any tax due. The result of these statutory requirements is that all persons must keep adequate records sufficient to establish their entitlement to any claimed tax exemption or deduction.

(ii) The law does not contemplate that the deduction provided for by RCW 82.04.4282 should be granted merely because the payments required to be made by members or customers are designated as "initiation fees" or "dues." The statutory deduction is not available for outright sales of tangible personal property or for providing facilities or services for a specific charge. Neither is it available if dues are in exchange for any significant amounts of goods or services rendered by the recipient thereof to members without any additional charge to the member, or if the dues are graduated upon the amount of goods or services rendered. Thus, it is only those initiation fees and dues which are paid solely and exclusively for the express privilege of belonging as a member of a club, organization, or society, which are deductible.

The Department in Det. No. 95-239, 16 WTD 048 (1995), citing Automobile Club v. Department of Rev., 27 Wn. App. 781, 786, 621 P.2d 760 (1980), declared that the purpose of the bona fide initiation fees or dues deduction is to exempt from taxation only revenue exacted for the privilege of membership as, for example, initiation fees that entitle members to a proprietary interest or operational control.

Accordingly, Audit allowed in the present matter a \$. . . deduction from the \$. . . paid by new regular members because the \$. . . represented the proprietary interest that each member with a certificate of membership had in the taxpayer. As noted, a certificate of membership also allows a regular member to vote on the matters pertaining to operational control of the taxpayer's business. . . .

Audit also allowed another \$. . . deduction from the fee paid by regular members for the privilege of belonging as a member of the club. Audit found that social members each paid a \$. . . membership fee. That \$. . . fee entitled them to all of the privileges of the club held by regular members except golf. Thus, Audit determined that the remaining \$. . . was the difference between the value of the privilege of membership and the value of the privilege to play golf. That is, the [balance] was payment in exchange for a service. Similarly, Audit found the difference between the monthly dues paid by regular members and social members represented payment by the regular members for the privilege to play golf.

We agree with Audit's analysis. All payments by regular members that represent proprietary interests and the privilege of membership are identified and are exempt for the reasons stated above. Specifically, the proprietary interest of each regular member was established by the taxpayer to be worth \$. . . , as stated on the certificate of membership. A social membership for \$. . . entitles a person to all the same privileges as a regular member except golf. Therefore, we agree that the privilege of membership is worth \$ The remaining \$. . . represents the value paid by regular members for the privilege to play golf and is subject to retail sales tax and

retailing B&O tax. The same reasoning applies to the difference in monthly dues between social members and regular members.

We disagree with the taxpayer that the mere privilege to play golf is not taxable, or, as otherwise stated, a member must play golf before a taxable event occurs. The Department in Det. No. 95-239, supra, responded to a similar argument presented by a health and fitness club where it stated: “we can find no basis to deduct the dues paid to use facilities which are available to members but not used by them.”

We do not believe that Det. No. 86-310 and Det. No. 94-062, supra, support the taxpayer’s position that the fees are entirely deductible. Det. No. 94-062 cites Det. No. 86-310 where it explains the deduction in RCW 82.04.4282:

Under this statute, if the services or membership benefits derived from dues payment are both enough and of a kind which are compensated for when purchased by nonmembers in the marketplace, then the portion of dues income attributable to such benefits do not fall within the ambit of the tax deduction. Det. No. 86-310, 2 WTD 91 (1986).

We have shown that the some of the benefits received by the regular members are of a kind that are compensated for when purchased in the market place in general, or, in particular, by the taxpayer’s social members.

DECISION AND DISPOSITION:

The taxpayer’s petition is denied.

Dated this 16th day of March 1998