

Cite as Det. No. 15-0354, 35 WTD 504 (2016)

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>
Assessment of	)	
	)	No. 15-0354
	)	
...	)	Registration No. . . .
	)	

1] RCW 82.04.170; RCW 82.04.192(3)(b); RCW 82.04.192(6)(b); RCW 82.08.0208: RETAIL SALES TAX – EXCLUSION – DIGITAL AUTOMATED SERVICES – DIGITAL GOODS – DIGITAL CODES – ONLINE EDUCATIONAL PROGRAMS – TUITION FEES. Charges for educational programs offered by accredited institutions of higher learning and that are included within the institution’s accreditation, which are comprised of digital automated services, digital goods and/or related digital codes, are excluded from the definition of retail sale and are not subject to retail sales tax. Mandatory fees charged universally to all students, faculty, or other staff of the institution as part of tuition, even if separately stated from tuition charges, and are paid only by students, faculty, or other staff of the institution for digital resources available only to them, such as electronic textbooks, online libraries, and other online learning resources, are tuition fees subject to the Service and Other Activities B&O tax classification.

[2] RCW 82.04.050, RCW 82.04.290(2), RCW 82.04.170; Rule 167(2): RETAIL SALES TAX – TUITION FEES – SCIENCE LAB FEES – NURSING PROGRAM FEES. When a fee is charged to students and includes uniforms, science lab kits or other tangible personal property, or includes services otherwise subject to retail sales tax, the fee is a tuition fee that is not subject to retail sales tax if the goods and services are provided exclusively to students, faculty, or other staff of the institution as part of a tuition charge.

[3] RCW 82.12.020; RCW 82.32.178: USE TAX – DEFERRED SALES TAX – CONSUMER – DIGITAL PRODUCTS – DIGITAL CODES. Although certain charges for tuition and tuition fees, including digital products and digital codes, are not subject to retail sales tax, the seller may be liable for use tax to the extent that it first uses in this state, as a consumer, tangible personal property, or digital products and codes, for which sales tax was not paid and for which an exemption is not otherwise available.

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.

LaMarche, A.L.J. – A private educational institution (Taxpayer) that provides educational programs solely through the internet, disputes the assessment of retail sales tax and Retailing Business and Occupation (B&O) tax on certain charges to its students, arguing that fees for online educational programs are specifically excluded from the definition of “digital automated service” and not subject to taxation as retail sales. We conclude that Taxpayer’s fees for its online educational programs are not taxable as retail sales, and that Taxpayer’s library and resource fees, science lab fees, and nursing program fees are tuition fees not subject to tax as retail sales. However, Taxpayer may owe use tax on certain property it used in this state as a consumer, for which sales tax was not paid. We grant the petition, but raise the issue of possible use tax liability and remand to the operating division for further findings and adjustments.<sup>1</sup>

### ISSUES

1. Under RCW 82.04.192(3)(b)(ix)(B) and RCW 82.04.192(6)(b)(v), and WAC 458-20-15503(202) and (303), are charges for Resource and Library Fees for Online Educational Programs excluded from the definition of “digital automated services,” and, thereby, not included within the definition of “retail sales” under RCW 82.04.050(8)(a)?
2. Under RCW 82.04.050, RCW 82.04.290(2), RCW 82.04.170, and WAC 458-20-167(2), are Taxpayer’s Resource, Library, Science Lab, and Nursing Program fees “tuition fees” subject to service and other activities B&O tax?
3. Under RCW 82.12.020 and RCW 82.32.178, does Taxpayer owe use tax and/or deferred sales tax on tangible personal property, digital codes, and digital automated services that it used in this state as a consumer?

### FINDINGS OF FACT

[Taxpayer] is a nonprofit, accredited educational institution, with an online educational program encompassed within its accreditation.<sup>2</sup> Taxpayer offers bachelor’s and master’s degrees in the fields of teaching and education, business, information technology, nursing, and healthcare management. *See* . . . website, . . . (last accessed December 11, 2015). Taxpayer’s educational programs are available exclusively through the internet. *Id.*

Taxpayer uses a simplified fee structure, charging between \$ . . . and \$ . . . per term for tuition, and separately imposes a one-time \$ . . . Application Fee and a Resource Fee of \$ . . . per term. *Id.* Previously entitled “Library Fee,” but changed in 2011 to be more descriptive in an online environment, the Resource Fee “helps cover [the] use of the online library, e-textbooks, and many other learning resources.” *Id.* The Resource Fee is a mandatory fee charged to all students along with their tuition, regardless of what program they choose; students do not have the option

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

<sup>2</sup> *See* . . . (accessed December 11, 2015).

accessing Taxpayer's educational programs without paying the fee. The Resource Fee is charged only to enrolled students.

Taxpayer charges additional fees for students enrolling in certain programs, and students not in those programs do not have to pay these fees. For students pursuing a bachelor's or master's degree in science education, Taxpayer separately charges a one-time Science Lab Fee for a home science lab. *Id.* For students pursuing a nursing degree, Taxpayer separately charges a one-time [Nursing Program Fee] to cover expenses related to nursing coursework, including uniforms, lab work, third-party exams, and selected learning resources. *Id.*

Students in programs that include student teaching are charged a standard \$ . . . [Teaching Fee] (composed of a \$ . . . application fee, plus a \$ . . . [teaching fee]), prior to their in-classroom teaching practicum. *Id.* Taxpayer also charges a one-time \$ . . . fee to students in the [Educational Leadership] program or Master of Science program in their last term as they complete their practicum experience; these fees and the [Teaching Fees] are treated under the service and other activities B&O tax classification, are not in dispute. *Id.*

The facts are not clear whether Taxpayer paid retail sales or use tax on property it used as a consumer in this state, including certain tangible personal property, such as science lab kits and nursing uniforms, and certain digital goods, services and codes, including online research databases . . . .

The Audit Division (Audit) of the Department of Revenue (Department) audited Taxpayer for the period of June 1, 2010 through December 31, 2013, and concluded, in relevant part, that certain charges for supplies and resources Taxpayer provided to its students were subject to retailing B&O tax and retail sales tax. Audit set forth the tuition and fees Taxpayer received from students during the Audit Period on Workpaper A of the Audit Report, and classified those charges as "tuition," "service," or "retail." The dispute here relates solely to those charges that Audit labeled "retail."

The charges labeled "retail" on Workpaper A were reclassified on the basis that students were sent tangible personal property or were given access to digital products in exchange for paying the fees. Taxpayer does not dispute that it owes retail sales taxes on the Web Cam Replacement Fee (\$ . . . ), Whiteboard Purchase (\$ . . . ), and Duplicate Diploma Fees (\$ . . . ). However, Taxpayer disputes the remainder of the reclassified charges (Disputed Fees), listed with the rounded totals of each, as follows: Science Lab Fees (\$ . . . ); Nursing Program Fees (\$ . . . ); Library Fees (\$ . . . ); and Resource Fees (\$ . . . ). *See* Workpaper A, *supra*. Schedule 3B calculates the retail sales tax due on Disputed Fees from Workpaper A, which comes to \$ . . . tax on Disputed Fees totaling \$ . . . . Audit issued an assessment on November 30, 2014, Document No. . . . , totaling \$ . . . .<sup>3</sup>

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<sup>3</sup> The assessment issued on November 3, 2014, Document No. . . . , totaled \$ . . . , which consisted of \$ . . . retail sales tax, \$ . . . retaining B&O tax, a credit of \$ . . . for service and other activities B&O tax, \$ . . . in use tax, \$ . . . interest, and a 5% assessment (substantial underpayment) penalty of \$ . . . .

The Auditor's Detail of Differences and Instructions to Taxpayer (Auditor's Detail) accompanying the assessment states, in relevant part:

WAC 458-20-167 states that sales of tangible personal property or services classified as retail sales are subject to the Retailing and Retail Sales tax classifications. This includes sales of books and supplies to students where these materials are not supplied as part of the tuition charge. The supplies and resources you provide to your students for a charge that are sent electronically or accessed electronically are considered digital products and are subject to the Retailing and Retail Sales tax classifications as well.

Taxpayer timely filed an appeal.

#### ANALYSIS

Washington imposes a B&O tax for the act or privilege of engaging in business in the state of Washington. RCW 82.04.220. RCW 82.04.250 and RCW 82.04.257 impose Retailing B&O tax on persons making retail sales of tangible personal property under RCW 82.04.050(1), and sales of digital goods, digital codes, and digital automated services. "Retail sale" also includes sales of prewritten computer software, regardless of the method of delivery to the end user, which include the sale or charge made for a key or an enabling activation code, where the key or code is required to put the software into use. RCW 82.04.050(6)(a).

"Educational institutions" are required to collect the retail sales tax on retail sales of tangible personal property and retail services to consumers, although some such sales may be exempt from the retailing B&O tax. RCW 82.08.020; RCW 82.04.050; Rule 167(4)(a).

Business activities other than, or in addition to, those that are specifically enumerated elsewhere in chapter 82.04 RCW or RCW 82.04.290(1) or (3), are taxed under the service and other activities B&O tax classification. RCW 82.04.290(2). The charge by educational institutions of tuition fees are subject to the service and other B&O tax, as they are not elsewhere classified. [RCW 82.04.170] defines "educational institution" in pertinent part as:

[T]hose institutions created or generally accredited as such by the state . . . 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 general academic nature, . . .

RCW 82.04.170 [further] defines "tuition fees" to include:

[L]ibrary, 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 . . . .

. . . ([E]mphasis included). Rule 167 explains the application of Washington's B&O, retail sales, and use taxes to educational institutions. Rule 167(2) further clarifies the term "tuition fees" under RCW 82.04.170 and includes "fees for instruction" as well. *Id.*

## 1. Online Educational Programs

RCW 82.04.050(8)(a) provides that sales to consumers of “digital goods,” “digital codes,” and “digital automated services” are generally subject to retail sales tax. However, RCW 82.04.192(3)(b)(ix)(B) excludes from the definition of “digital automated service” online educational programs provided by:

(B) an institution of higher education as defined in sections 1001 or 1002 of the federal higher education act of 1965 (Title 20 U.S.C. Secs. 1001 and 1002), as existing on July 1, 2009. For purposes of this subsection (3)(b)(ix)(B), an online educational program must be encompassed within the institution's accreditation; . . .

RCW 82.04.192(3)(b)(ix)(B) (emphasis provided). RCW 82.04.192(6)(b)(v) applies the latter exclusion to “digital goods” as well, defined under RCW 82.04.192(6)(a) as “sounds, images, data, facts, or information, or any combination thereof, transferred electronically, including, but not limited to, specified digital products and other products transferred electronically not included within the definition of specified digital products. . . .” Finally, RCW 82.08.0208 excludes from the definition of “retail sale” sales of digital code for one or more digital products, if the use of the digital products to which the code relates is exempt from retail sales tax.

Audit does not dispute that Taxpayer is a qualifying “institution of higher education” as that term is used under RCW 82.04.192(3)(b)(ix)(B), or that Taxpayer’s online educational programs are encompassed within its accreditation. Accordingly, we assume without deciding that Taxpayer is an accredited institution of higher learning, and that all of its online educational programs are encompassed within its accreditation.

The Department adopted WAC 458-20-15503 (Rule 15503) for the purpose of providing “a structured approach for determining tax liability for digital products and digital codes.” Rule 15503 provides an example of the tax treatment of online programs similar to those provided by Taxpayer:

**Example 11.** ABC University, a qualifying institution of higher education under the federal Higher Education Act of 1965, provides an accredited online Spanish course for which it charges a quarterly access and use fee to students. The course is remotely accessed by students logging into a web site and accessing a fully interactive program that includes components of video, text, and audio, as well as extensive software code. This service would generally be considered a digital automated service. However, it is specifically excluded from the definition of digital automated service as an online educational program and may be subject to service and other activities B&O tax if another exclusion, deduction, or exemption does not apply. . . .<sup>4</sup>

Rule 15503(303)(i)(ii).

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<sup>4</sup> We note that services that are excluded by statute from the definitions of digital good or digital automated service (e.g., telecommunications services and ancillary services) may continue to be separately taxed as retail services. See Rule 15503(301) and (601). However, that is not the case here, because RCW 82.04.050 does not otherwise separately subject Taxpayer’s educational services to retail sales tax.

Here, Taxpayer's fees for its online educational programs are not subject to retail sales tax or Retailing B&O tax, because, like Example 11 above, Taxpayer is a qualifying educational institution whose online educational programs are specifically excluded from the definitions of digital goods, digital codes, and digital services. RCW 82.04.192(3) and (6); Rule 15503. Taxpayer's educational programs are offered exclusively online, and its charges for Resource and Library Fees (collectively, Resource Fees) are part of their tuition fees, payment of which are required for access to and use of Taxpayer's online educational programs.

Audit contends that the Resource Fee should be taxable as a retail sale because the fee pays in part for electronic textbooks (etextbooks), or digital codes to access etextbooks, which would normally be subject to retail sales tax as digital products under RCW 82.04.050(8). Here, however, even though Taxpayer lists a Resource Fee separately, the fee is a tuition fee charged universally to all students as part of tuition, is mandatory, and is paid only by students for resources available only to students.

Prior to 2011, Taxpayer used the term "Library Fee," which it changed to "Resource Fee," a more descriptive term in the context of an online environment. RCW 82.04.170 and Rule 167(2) specifically list "library fees" and "other special fees" as kinds of "tuition fees." Regardless of how titled, Resource Fees are a universal and mandatory part of the charges to all students, and as Taxpayer explains on its website, partially offset the costs of Taxpayer's provision of online educational resources, such as etextbooks, its online library, and other online learning resources—the digital era's equivalent of a brick-and-mortar library. Only students pay the Resource Fee, and only students have access to the online educational programs after they pay the fee. Therefore, it is a tuition fee under RCW 82.04.170 and Rule 167(2). Like the example of ABC University in Example 11 in Rule 167, we consider the Resource Fee to be a kind of "access and use fee" as contemplated under Rule 15503(303)(i)(ii) that Taxpayer charges all of its students to access and use the resources that are the foundation of its online educational programs.<sup>5</sup>

We conclude that the Resource Fees are part of Taxpayer's tuition fees as defined in RCW 82.04.170, and are not subject to retail sales tax or Retailing B&O tax. Accordingly, we grant the petition as to the Resource Fees, inclusive of Library Fees.

## 2. Science Lab and Nursing Program Fees

RCW 82.04.170 and Rule 167(2) specifically include "lab fees" in the definition of "tuition fees" and also include "other special fees" charged to students as tuition fees. Thus, when a tuition fee is charged to students and includes uniforms, science lab kits and other tangible personal property, or includes services otherwise subject to retail sales tax, the tuition fee is not subject to retail sales tax when the goods and services are provided exclusively to students, faculty, or other staff of the institution, as a part of a tuition charge. RCW 82.04.170; Rule 167(2). Therefore, we conclude that Taxpayer's Science Lab Fees and Nursing Program Fees are tuition fees, and are not subject to retail sales tax and Retailing B&O tax.

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<sup>5</sup> Because we grant relief to Taxpayer on other grounds, we do not reach the issue of whether the resource fee is part of the tuition charge itself.

We grant the petition as to the Science Lab and Nursing Program Fees. However, as we shall discuss, Taxpayer may be subject to use tax on certain property or services included in its tuition fees.

### 3. Use Tax

A use tax is imposed under RCW 82.12.020(1) for the privilege of using within this state, as a consumer, any article of tangible personal property acquired by the user in any manner. RCW 82.12.020(1) likewise imposes the use within this state, as a consumer, certain digital goods, services, and codes, and retail services, as follows:

. . . (b) Prewritten computer software, regardless of the method of delivery, but excluding prewritten computer software that is either provided free of charge or is provided for temporary use in viewing information, or both;

(c) Services defined as a retail sale in RCW [82.04.050](#) (2)(a) or (g), (3)(a), or (6)(b), excluding services defined as a retail sale in RCW [82.04.050](#)(6)(b) that are provided free of charge;

(d) Extended warranty; or

(e)(i) Digital good, digital code, or digital automated service, including the use of any services provided by a seller exclusively in connection with digital goods, digital codes, or digital automated services, whether or not a separate charge is made for such services.

(ii) With respect to the use of digital goods, digital automated services, and digital codes acquired by purchase, the tax imposed in this subsection (1)(e) applies in respect to:

- (A) Sales in which the seller has granted the purchaser the right of permanent use;
- (B) Sales in which the seller has granted the purchaser a right of use that is less than permanent;
- (C) Sales in which the purchaser is not obligated to make continued payment as a condition of the sale; and
- (D) Sales in which the purchaser is obligated to make continued payment as a condition of the sale.

(iii) With respect to digital goods, digital automated services, and digital codes acquired other than by purchase, the tax imposed in this subsection (1)(e) applies regardless of whether or not the consumer has a right of permanent use or is obligated to make continued payment as a condition of use. . . .

The use tax supplements the retail sales tax by imposing a tax of like amount upon the use within this state as a consumer the retail service or any article of tangible personal property acquired in any manner, where the user has not paid retail sales tax under chapter 82.08 RCW with respect to the service or property used. RCW 82.12.020(2); [RCW 82.12.010(6) (definition of “use”);] WAC 458-20-178(1) and (2) (Rule 178).<sup>6</sup> However, if the user has paid sales tax on the purchases, use tax is not owed. RCW 82.12.020(2); Rule 178(2).

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<sup>6</sup>The Department promulgated an updated version of Rule 178. The changes to the rule do not affect the outcome in this case. The citations in this determination are to the prior version of the rule.

“Consumer” includes any person taxable under RCW 82.04.290. [RCW 82.04.190(2)(a).] Liability for the use tax arises at the time the property is first put to use in this state. RCW 82.12.020; Rule 178(3). The tax is levied and collected on an amount equal to the value of the article used by the Taxpayer. Rule 178(13); RCW 82.12.020(4); *see* Det. No. 13-0237R, 33 WTD 349 (2014). Educational institutions must report the deferred sales or use tax upon the use in this state as a consumer of all tangible personal property, digital goods, digital code, or digital automated services, purchased or acquired under conditions where the Washington retail sales tax has not been paid, unless a specific statutory exemption applies. RCW 82.12.020(1); Rule 167(5).

Here, although Taxpayer’s charges for tuition fees are not retail sales to its students or faculty, Taxpayer itself may be liable for use tax as the consumer of certain digital goods (e.g., . . . etextbooks), digital automated services and associated digital codes, that it provides to its students in Washington State as a part of their tuition charges, to the extent not otherwise excluded from taxation. Similarly, Taxpayer itself appears to be the consumer of tangible personal property, such as nursing uniforms and science lab kits, which Taxpayer provides to its students as part of tuition fees. Therefore, Taxpayer may be liable for use tax to the extent that Taxpayer first used in this state, as a consumer, certain tangible personal property, or digital products and codes, for which sales tax was not paid and for which an exemption is not otherwise available. RCW 82.12.020; Rule 178.

Because the facts are not clear in regard to the types of goods and services Taxpayer first put to use as a consumer in this state, the value of the goods and services it purchased, and whether Taxpayer paid sales tax on those purchases, we remand to Audit for further findings and possible adjustments.

In summary, we conclude that Taxpayer’s Resource Fees (inclusive of Library Fees), are for Taxpayer’s Online Educational Programs, which are exempt from retail sales tax because they are excluded from the definition of a digital good, code, or service. Taxpayer’s Resource Fees, Science Lab Fees, and Nursing Program Fees are tuition fees subject to service and other activities B&O tax. However, Taxpayer may be subject to use tax on certain . . . purchases.

We grant the petition, raise the issue of possible use tax liability as a result of the conclusions reached in the decision, and remand to the Audit Division for adjustments to retail sales and retailing B&O taxes, to verify Taxpayer’s qualification for the B&O tax deduction for tuition fees [with proof that it is an accredited institution under RCW 82.04.192(3)(b)(ix)(B)], and to make further findings and possible adjustments with regard to the issue of use tax.

#### DECISION AND DISPOSITION

Taxpayer’s petition is granted in part and denied in part.

Dated this 31st day of December, 2015.