

Cite as Det. No. 17-0289, 37 WTD 153 (2018)

[1] RULE 100(4)(d): ADMINISTRATIVE REVIEW OF TAX RULING – LETTER RULING. Review of a tax ruling is limited to the documents and records reviewed by the Department of Revenue during the tax ruling process, and any written statements included with the petition for review. The review of a tax ruling is limited to correcting an error that occurred in the course of the tax ruling process.

[2] RULE 258; RCW 82.04.260(5); RCW 82.04.290: SERVICE AND OTHER ACTIVITIES B&O TAX – “TOUR OPERATOR” B&O TAX– TOUR OPERATOR – YOUTH EXCHANGE PROGRAM – STUDENT EXCHANGE PROGRAM. The gross revenue of a non-profit organization that coordinates and conducts international youth exchange programs is subject to the Service and Other Activities B&O tax rate, and not the lower “tour operator” rate. Only a minor portion of the organization’s gross income was attributable to the services it claimed were those of a tour operator, which did not support its assertion that all of its gross income should be taxed at the tour operator B&O tax rate.

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.

November 22, 2017

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Re: ...  
Determination No. 17-0289

Dear . . . :

This is the Department of Revenue’s (Department) decision regarding your petition dated August 25, 2016, requesting administrative review of the above-referenced tax ruling on behalf of . . . (Taxpayer).<sup>1</sup>

#### Taxpayer’s Ruling Request

On April 20, 2016, Taxpayer emailed a request for a binding tax ruling regarding the appropriate Washington business and occupation (B&O) tax classification of its receipts. Taxpayer’s request stated that Taxpayer coordinates and conducts international youth exchange programs in the United States and a number of foreign countries. Students pay Taxpayer to participate in the exchange program. Taxpayer indicated that it partners with other organizations, who pay a portion of the program fees that students pay to participate in the exchange programs. Taxpayer argued that because it provides transportation, hotel lodging, and meal services, all of its income should

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

be classified under the B&O tax rate for tour operators in RCW 82.04.260(5) and WAC 458-20-258.

### The Department's Tax Ruling

The Department's Taxpayer Information and Education (TI&E) unit of the Taxpayer Services Division initially responded to Taxpayer's request on May 27, 2016, ruling that Taxpayer's receipts did not qualify as those of a "tour operator" under RCW 82.04.260(5) and were instead properly classified under the Service and Other Activities B&O tax classification in RCW 82.04.290(2). The basis for the ruling was that providing tours was not Taxpayer's primary business activity.

Taxpayer disagreed, and presented additional arguments and facts. TI&E agreed to reconsider the issue, and on July 27, 2016, issued a second and final response that superseded its initial ruling, stating as follows:

#### **Facts as Presented**

[Taxpayer] exists for the purpose of coordinating and conducting international youth exchange programs in the United States and a number of foreign countries. The organization's mission is ". . ." It achieves this mission by conducting short-term summer exchange programs (typically four weeks in length) for both inbound and outbound students, as well as an academic year program for inbound and outbound students.

[Taxpayer] partners with international education organizations in each of the countries it works with. These international partners are responsible for student recruitment/selection, and collect a program fee from each student to cover program expenses and administrative costs, of which a portion is forwarded to [Taxpayer]. For outbound students, the initial application is made to the [affiliated organization] in the home state; the state coordinator forwards applications and deposits to [Taxpayer] which makes the final selection of participants. Program fees in excess of the deposit are typically paid by the selected students' families directly to [Taxpayer].

[Taxpayer] retains a portion of the program fee for both inbound and outbound students. The remainder of the fee is forwarded directly by [Taxpayer] to its partner organizations and universities in the U.S. and abroad. The local organizations/universities use their portion of the fee to cover the costs of in-state student and host family orientations, criminal background checks for host families/chaperones, and program implementation and promotion.

The amounts retained by [Taxpayer] go towards the purchase of comprehensive insurance coverage for the students, host families, volunteers, board and staff; program development including capacity building and training for in-state partners; administrative costs such as salaries and office expense; and program implementation. Program implementation costs include in-country transportation, hotel/meal expenses when students are not staying with their host family, educational materials, travel materials (t-shirts, luggage tags, passport holder, etc.), and emergency funds.

Although [Taxpayer] characterizes its activities as organizing [cultural exchange programs] rather than as selling packaged tours, its activities are functionally very similar to those of a traditional, for-profit tour operator. The participating students pay a program fee, which covers

ground transportation, hotel lodging when the student is not staying with their host family, insurance, and the costs of screening / selecting host families and training program coordinators.

The program fee collected by [Taxpayer] is intended to cover the cost of operating the exchange programs – both direct travel costs, as well as the organization’s overhead and general operating costs. This is analogous to a traditional tour operator selling a packaged tour – the amount charged would typically cover some or all of the direct costs of the tour, such as transportation and lodging, as well as the tour operator’s overhead / administrative costs and a profit margin.

Although [Taxpayer] does not describe itself to the public as a tour operator, we are not aware of any factual distinction in how it operates that would cause it to fall outside of the “tour operator” definition provided in Rule 258. Thus, we conclude that [Taxpayer] should report its program fees and any other miscellaneous receipts associated with the exchange programs it operates under the “travel agent and tour operator” B&O tax classification.

### **Question**

Are [Taxpayer’s] receipts properly classified for B&O tax purposes under the “travel agent and tour operator” classification described in RCW 82.04.260(5) and WAC 458-20-258?

### **Ruling**

No. Based on the information provided, [Taxpayer] is providing student exchange program services and is subject to business and occupation (B&O) tax under the Service and Other Activities classification.

A tour operator is defined in WAC 458-20-258(3) as:

[A] person engaging in the business activity of providing tours directly or through third-party providers including, but not limited to, transportation, lodging, meals and other associated services that are purchased by the customer. The tour operator generally either purchases or provides some or all of the services offered, and is itself liable for paying for any services it purchases.

[WAC 458-20-258(3)(a)(i).] We do not agree that [Taxpayer] should report under the Tour Operator B&O tax classification for the following reasons:

1. Based on the information available, [Taxpayer] is not paid a fee primarily for providing tours. Rather, participants pay a fee to [Taxpayer] for providing student exchange program services that may include but are not limited to administering the exchange program, recruiting participants, selecting participants, processing applications, conducting orientation seminars for participants, providing background checks, hiring chaperones, purchasing insurance, training in-state partners and having administrative staff available for services.
2. [Taxpayer] is not currently registered with the Washington Department of Licensing RCW Chapter 19.138 and WAC Chapter 308-129 as a “seller of travel.”

The Department continues to rely on (in several published determinations) the primary purpose test (i.e., true object test) to determine the proper tax classification of a taxpayer's business activities. Therefore, we conclude that [Taxpayer's] income is properly classified under the Service and Other Activities B&O tax classification because [Taxpayer's] primary business activity is providing student exchange program services.

### Petition for Administrative Review

Taxpayer timely petitioned the Department's Administrative Review and Hearings Division (ARHD) for administrative review of the tax ruling.

WAC 458-20-100 (Rule 100) is the Department's administrative rule that addresses informal administrative reviews, including taxpayer requests for letter rulings. Rule 100(4)(d) states, in part, as follows:

Review of a tax ruling is limited to the documents and records reviewed by TI&E and any written statements included with the petition. This review is limited to correcting an error that occurred in the course of the tax ruling process. . . .

In addition to the facts presented to TI&E with its letter ruling request, Taxpayer included written statements with its petition, as follows:

[Taxpayer] is a non-profit organization that exists for the purpose of coordinating and conducting international youth exchange programs in the United States and a number of foreign countries. The organization's mission is . . . . It achieves this mission by conducting short-term summer exchange programs (typically four weeks in length) for both inbound and outbound students, as well as an academic year program for inbound and outbound students, as well as international tours for adult professionals.<sup>2</sup> As described below, [Taxpayer] arranges for the transportation, lodging, meals, and other associated services provided to participants during the exchange program, either directly or through host families and corresponding organizations in foreign countries.

[Taxpayer] partners with international education organizations [(Partner Organizations)]<sup>3</sup> in each of the countries it works with. These international partners are responsible for student recruitment/selection, and collect a program fee from each student to cover program expenses and administrative costs, of which a portion is forwarded to [Taxpayer]. [(Emphasis added.)] For outbound students, the initial application is made to the [affiliated organization] in the home state; the state coordinator forwards applications and deposits to [Taxpayer] which makes the final selection of participants. Program fees in excess of the deposit are typically paid by the selected students' families directly to [Taxpayer].

[Taxpayer] retains a portion of the program fee for both inbound and outbound students. The remainder of the fee is forwarded directly by [Taxpayer] to its partner organizations and universities in the U.S. and abroad. [(Emphasis added.)] The local

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<sup>2</sup> We note that Taxpayer did not mention the international tours for adult professionals in its TI&E ruling request.

<sup>3</sup> The Partner Organization in Washington State is. . . .

organizations/universities use their portion of the fee to cover the costs of in-state student and host family orientations, criminal background checks for host families/chaperones, and program implementation and promotion. [(Emphasis added.)]

The amounts retained by [Taxpayer] go towards the purchase of [1] comprehensive insurance coverage for the students, host families, volunteers, board and staff; [2] program development including capacity building and training for in-state partners; [3] administrative costs such as salaries and office expense; and [4] program implementation. [(Bracketed material and underlined emphasis added.)] Program implementation costs include in-country transportation, hotel/meal expenses when students are not staying with their host family, educational materials, travel materials (t-shirts, luggage tags, passport holder, etc.), and emergency funds. [(Emphasis added.)]

In regard to the international tours for adult professionals, [Taxpayer] operates two-week tours each year for adult academics and [affiliated organization] professionals. The tours visit the countries with which [Taxpayer] conducts youth programs. The purpose of the tour is “cultural immersion,” and the activities are primarily based around conventional tourism activities. As with the summer programs,<sup>4</sup> [Taxpayer], manages the transportation, lodging, meals, and other associated services for all participants—functioning in the same role as a traditional tour company.

[Taxpayer] is not currently registered with the Washington Department of Licensing as a “seller of travel” under RCW Chapter 19.138 and WAC Chapter 308-129, nor has it been registered as such on the past.

Taxpayer argues that it is in the business of acting as a travel agent or tour operator under RCW 82.04.260(5), stating,

Although [Taxpayer] characterizes its activities as organizing [cultural exchange programs] rather than as selling packaged tours, its activities are functionally very similar to those of a traditional, for-profit tour operator. The participating students pay a program fee, which covers ground transportation, hotel lodging when the student is not staying with their host family, insurance, and the costs of screening / selecting host families and training program coordinators . . . .

### ARHD Decision

### **ANALYSIS**

Persons engaged in any business activity, other than or in addition to those for which a specific rate is provided in chapter 82.04. RCW, are taxable under the Service & Other Activities B&O tax classification. RCW 82.04.290(2). The tax is imposed on the gross income of the business at the

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<sup>4</sup> Taxpayer refers here to the youth summer programs, but not the academic year programs, when it discusses its management of the “transportation, lodging, meals and other associated services for all participants.” This implies that Taxpayer may have a different role in the academic-year youth programs; however, Taxpayer has not clarified this distinction.

rate of 1.5%. *Id.* However, RCW 82.04.260(5) provides a lower B&O tax rate of 0.275% for “every person engaging within this state in the business of acting as a travel agent or tour operator.”

RCW 82.04.260(5) does not define the term “tour operator.” However, the term is defined by WAC 458-20-258 (Rule 258), the Department’s administrative rule that addresses the activities of travel agents and tour operators. Rule 258 defines the term “tour operator” as follows:

A "tour operator" is a person engaging in the business activity of providing tours directly or through third-party providers including, but not limited to, transportation, lodging, meals and other associated services that are purchased by the customer. The tour operator generally either purchases or provides some or all of the services offered, and is itself liable for paying for any services it purchases.

Rule 258(3)(a)(i) (emphasis provided).

Rule 258(3)(b) provides the following example of tax treatment for a tour operator:

**Example 4:** TTT Travel Services offers a Washington state tour priced at \$1,500. The tour package consists of air transportation, lodging, and bus transportation. TTT is liable for paying the service providers, even if a customer fails to pay TTT for a reserved tour. The gross income of the business is the total tour sales price received, \$1,500, and is subject to the travel agent/tour operator B&O tax classification.

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Here, Taxpayer asserts that both the summer and academic year student exchange programs are “tours,” and that Taxpayer is the “tour operator” that sells those “tours.” On that basis, Taxpayer argues that all Program Fees it receives from students participating in those programs are subject to B&O tax under the tour operator classification.

Taxpayer asserts that it uses Program Fees to pay “program implementation costs,” some of which go to pay for “tour operator” services—specifically, the in-country transportation and hotel/meal expenses of students who are not staying with their host families, as well as the provision of educational materials, and travel materials (t-shirts, luggage tags, passport holders, etc.). Taxpayer states that program implementation costs also include emergency funds. Because “program implementation” costs include transportation, meals, and lodging, similar to the services provided by tour operators, Taxpayer contends that its services fall within the “tour operator” definition in Rule 258. On that basis, Taxpayer argues that *all* Program Fee income and miscellaneous income that it receives should be treated as that of a tour operator. We disagree.

First, in contrast to the activities of a “tour operator,” who engages in “the business activity of providing tours directly or through third-party providers including, but not limited to, transportation, lodging, meals and other associated services that are purchased by the customer,” Rule 258(3)(a)(i), Taxpayer’s activities consist primarily of administering a non-profit student exchange program. This is reflected in Taxpayer’s stated goal of “coordinating and conducting international youth exchange programs in the United States and a number of foreign countries.”

Unlike a tour operator, Taxpayer facilitates placement of students with host families through its relationships with its Partner Organizations and does not plan particular activities for students in their host countries or host states. Rule 258(3). Nor does Taxpayer offer a selection of activities for the students to choose from as part of a tour. *Id.* Instead, tour activities are determined by local affiliates or the Partner Organizations, but not by Taxpayer. If students later go on to engage in other activities with their host families or independently, those activities are separately planned and are not “tours” that Taxpayer sells to those students.

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Taxpayer states in its petition that it also provides tours for adults, and arranges those activities in the manner of a tour operator. However, Taxpayer did not address this issue in its ruling request, and, therefore, it will not be addressed here.<sup>5</sup>

Second, if a Program Fee is meant to pay for a “tour,” then it is readily apparent that the “tour” cannot be the entire exchange program itself, contrary to Taxpayer’s assertion. A student’s Program Fee cannot cover the total costs of an exchange program. Students in the exchange program receive the services not only of Taxpayer and the Partner Organization, but the services of the host family as well. This indicates that the services Taxpayer provides are not primarily those of a tour operator selling “tours,” but instead are the services of an organization whose primary activity is the coordination of a non-profit youth program, and implementation of that program through partnerships with other organizations and host families. It follows that rather than paying for a “tour,” students pay Program Fees that, in large part, cover the administrative costs of the exchange program.

Taxpayer indicates that it applies its portion of the Program Fees toward the following expenses: 1) comprehensive insurance coverage for the students, host families, volunteers, board and staff; 2) program development including capacity building and training for in-state partners; and 3) administrative costs, such as salaries and office expense. Only the remaining portion of the Program Fees goes toward the fourth category of “program implementation” costs, and of those costs, only a portion are attributable to in-country transportation and hotel/meal expenses for students when they are not staying with their host families. Therefore, only a minor portion of Taxpayer’s gross income is attributable to the services it claims are those of a tour operator, which does not support Taxpayer’s assertion that *all* of its gross income should be taxed at the tour operator B&O tax rate under RCW 82.04.260(5).

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<sup>5</sup> [Review of a tax ruling is limited to the documents and records reviewed by TI&E and any written statements included with the petition. This review is limited to correcting an error that occurred in the course of the tax ruling process. WAC 458-20-100(4)(d).]

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Based on the foregoing, we conclude that Taxpayer is not a “tour operator” for purposes of RCW 82.04.260(5) and WAC 458-20-258. Accordingly, we deny the petition and affirm the tax ruling dated July 27, 2016.<sup>6</sup>

LaMarche, T.R.O.

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<sup>6</sup> We note Taxpayer’s objection to the letter ruling’s reference to Taxpayer’s registration status as a “seller of travel.” However, because we base our decision on other grounds, we do not reach the issue of whether licensure as a “seller of travel” under chapter 19.138 RCW and chapter 308-129 WAC has a bearing on whether a taxpayer qualifies for the tour operator B&O tax classification.