

Cite as Det. No. 18-0014, 37 WTD 224 (2018)

BEFORE THE ADMINISTRATIVE REVIEW AND HEARINGS 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. 18-0014
)	
...)	Registration No. . . .
)	

RCW 82.04.050; WAC 458-20-183: RETAIL SALES TAX ON PHYSICAL FITNESS SERVICES. Where yoga, tai chi, or qi gong classes were conducted at a health or athletic club, fitness center, health spa, or similar facility during periods ending on or before December 31, 2015, a presumption exists that the primary focus of such activities is physical fitness, and the class therefore is a “physical fitness service” subject to retailing business and occupation (“B&O”) tax and retail sales tax. The presumption can be overcome with evidence demonstrating the primary purpose of the class is not physical fitness.

RCW 82.32.055(1): WAIVER OF INTEREST AND PENALTIES BASED ON ACTIVE DUTY MILITARY SERVICE. The Department shall waive interest and penalties if the interest and penalties are imposed during a period of armed conflict, a majority owner of the taxpayer is an individual on active duty in the military participating in a conflict and assigned to a duty station outside of the United States. To be eligible for this waiver, a copy of the owner’s deployment orders must be submitted to the Department.

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.

Fisher, T.R.O. – A business that provides “crossfit” training disputes re-classification of its income from the service and other activities B&O tax classification to the retailing B&O tax classification and the resulting assessment of [retail sales] tax. The business asserts the services it offers are primarily instructional in nature and distinguishable from retail physical fitness services offered by regular gyms. The business also requests waiver of penalties and interest because its owner was on active duty participating in an armed conflict when the tax liability accrued. The petition is denied in part and granted in part.¹

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

ISSUES

1. Whether, under RCW 82.04.050(3), RCW 82.08.190, RCW 82.08.195, and WAC 458-20-183(3), revenue received from “crossfit” instruction and training physical fitness services is subject to retailing B&O tax and retail sales tax . . . ?
2. Whether, under RCW 82.32.055, Taxpayer is eligible for waiver of penalties and interest where the majority owner of Taxpayer was on active duty in the military participating in an armed conflict and assigned to a duty station outside of the United States?

FINDINGS OF FACT

. . . (“Taxpayer”) runs three exercise gyms in . . . Washington. Taxpayer teaches its customers, whom Taxpayer calls “athletes,” how to become and stay active. Taxpayer also sells fitness apparel and supplements.

The Department of Revenue’s . . . Taxpayer Account Administration Division (“TAA”) audited Taxpayer’s excise tax returns for the period of January 1, 2012, through December 31, 2015 (the “Audit Period”) to ensure Taxpayer was properly reporting its revenue. Taxpayer provided TAA with its business records, which showed its income broken down into Fitness Classes and Product Sales. During the Audit Period, Taxpayer reported all of its income from Fitness Classes under the service and other B&O tax classification.²

TAA determined that Taxpayer’s income from Fitness Classes was properly reportable under the retailing B&O tax classification, and was also subject to retail sales tax. TAA ultimately assessed \$. . . in retailing B&O tax and retail sales tax (combined), \$. . . in a substantial underpayment penalty, and \$. . . in interest.

Taxpayer timely sought administrative review. In its petition, Taxpayer asserted that it provides instructional lessons in physical fitness and how to be fit for life, which should be classified under the service and other activities B&O classification. Taxpayer asserts that the fact that it offers yoga classes and nutritional consulting supports this classification. Taxpayer offers “passes” for its classes. Athletes can purchase a pass or passes; each pass can be used to attend any of Taxpayer’s classes meaning that amounts for yoga and nutritional consulting were included in its Fitness Classes income.

Taxpayer provided the following explanations for the four classes that make up its class offerings:

1. **CrossFit** – We provide instructional lessons in constantly varied functional movements performed at high intensity. All workouts are based on functional movements, and these movements reflect the best aspects of gymnastics, weightlifting, running, rowing, and more. Intensity is essential for results and is measurable as work divided by time – or power. By employing a constantly

² Taxpayer reported its sales of fitness apparel and supplements under the retailing B&O tax classification; Taxpayer also collected and remitted retail sales tax on these sales. There is no dispute that Taxpayer properly reported its Product Sales revenue.

- varied approach to training, functional movements and intensity lead to dramatic gains in fitness.
2. **Flow Yoga and Body Maintenance (“Yoga”)** – Flow yoga is a slow paced class that will focus on the essential elements of yoga, including the basic postures and yoga theory. Classes will begin with relaxation, a short meditation, yoga theory or breathing exercises, include a basic flow sequence and end with a meditation to help reduce stress and integrate the class through the body and the mind.
 3. **Kids Movements and Music (“KMM”)** – Based on the principle of Mechanics, Consistency and then Intensity, this course emphasizes good movement throughout childhood and adolescence. Consistently good mechanics translates to physical literacy, enhanced sports performance and fewer sports injuries for kids. KMM is meant to be fun for all ages. Fun means we provide an active alternative to sedentary pursuits, which means less childhood obesity and all-around better health for our children. KMM is designed to be minimalist; it is inexpensive and often requires little or no equipment, allowing a wide array of socioeconomic groups an opportunity to be physically fit and physically active throughout their lives.
 4. **Lifetime Integrated Gymnastics Health and Training (“LIGHT”)** – This class focuses on the benefits of [y]oga and exercise without the demands of equipment. The LIGHT class uses a variety of gymnastics and yoga skills to strengthen, tone, and condition the entire body. We also refer to this class as our “Lifetime Fitness” class, because the program is designed to support [a]thletes over the span of their entire lifetime.

April 19, 2017, e-mail from Taxpayer at the hearing, Taxpayer further explained that its LIGHT class also includes dietary advice on how athletes can change their eating habits to meet their fitness goals.

Taxpayer also requests a waiver of penalties and interest due to Taxpayer’s owner’s military service under RCW 82.32.055. Taxpayer submitted its owner’s deployment orders showing that during the Audit Period, Taxpayer’s owner was on active duty in the Air Force, and was assigned to a duty station outside of the United States. The deployment orders reflect that Taxpayer’s owner went off active duty on March 12, 2016. . . .

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. The B&O tax measure and rate are determined by the type or nature of the business activity in which a person is engaged. Ch. 82.04 RCW. Washington also levies a retail sales tax on each retail sale in this state. RCW 82.08.020 and 82.04.050. Sales of services falling within the definition of “sale at retail” or “retail sale” are subject to the retailing B&O tax classification, and the seller is required to collect retail sales tax from the buyer. RCW 82.04.250, RCW 82.08.020, and RCW 82.08.050.

RCW 82.04.050 states that the term retail sale includes the following services:

(3) The term "sale at retail" or "retail sale" shall include the sale of or charge made for personal . . . services including amounts designated as . . . fees . . . and other service emoluments however designated, received by persons engaging in the following business activities:

(g) The following personal services: [p]hysical fitness services

WAC 458-20-183(2) defines physical fitness services and provides, in part:

(l) "Physical fitness services" include, but are not limited to: All exercise classes, whether aerobic, dance, water, jazzercise, etc., providing running tracks, weight lifting, weight training, use of exercise equipment, such as treadmills, bicycles, stair-masters and rowing machines, and providing personal trainers (i.e., a person who assesses an individual's workout needs and tailors a physical fitness workout program to meet those individual needs). "Physical fitness services" do not include instructional lessons such as those for self-defense, martial arts, yoga, and stress-management. Nor do these services include instructional lessons for activities such as tennis, golf, swimming, etc. "Instructional lessons" can be distinguished from "exercise classes" in that instruction in the activity is the primary focus in the former and exercise is the primary focus in the latter.

If a service does not fall within the definition of "retail sale" and is not explicitly taxed under another section of Chapter 82.04 RCW, then the gross proceeds derived from rendering the service are subject to tax under the service & other activities B&O tax imposed in RCW 82.04.290(2), and not subject to retail sales tax.

At issue is whether Taxpayer's classes (CrossFit, Yoga, KMM, and LIGHT) are primarily "instructional lessons" or "physical fitness services." On March 14, 2016, the Department updated Excise Tax Advisory 3104.2016 (ETA 3104),³ which clarifies this distinction for periods ending on or before December 31, 2015.⁴

ETA 3104 includes the following characteristics as indicative of instructional lessons:

[T]eaching the participant how to perform certain activities, generally following a specific curriculum that includes the study of the underlying philosophy of the activity . . . the participant obtaining certification as a physical fitness trainer or group fitness instructor, or mastery of the techniques and philosophy with possible advancement in levels of achievement.

³ ETA 3104 was issued before the Audit Period.

⁴ Effective January 1, 2016, RCW 82.04.050 was amended to include within the definition of retail sale "[o]perating an athletic or fitness facility, including all charges for the use of such a facility or for any associated services and amenities..." RCW 82.04.050(3)(g)(i). "Athletic or fitness facility" means "an indoor or outdoor facility or portion of a facility that is primarily used for: Exercise classes" RCW 82.04.050(3)(g)(iv)(A). Taxpayer's facility is primarily used for exercise classes, so Taxpayer's facility is an athletic or fitness facility, and charges for use of that facility are retail sales subject to retailing B&O tax and retail sales tax [after January 1, 2016].

In contrast the primary purpose of physical fitness services is characterized as: “primarily to improve flexibility, strength, or general fitness for the participant.” *Id.*

We have previously found CrossFit classes to be physical fitness services subject to retailing B&O and retail sales tax because the emphasis in describing the class is on exercise, physical fitness, and improved strength and conditioning. *See* Det. No. 15-0039, 34 WTD 406 (2015); Det. No. 13-0270, 32 WTD 18 (2014). Taxpayer’s description of its CrossFit class similarly focuses on increases in power (strength) and fitness. Similarly, Taxpayer’s description of its KMM and LIGHT⁵ classes place an emphasis on exercise, physical fitness, and improved strength and conditioning. Accordingly, we conclude that Taxpayer’s CrossFit, KMM, and LIGHT classes are a “physical fitness service” subject to retailing B&O and retail sales tax.

For Taxpayer’s Yoga classes, we turn to a different Excise Tax Advisory that applies the primary purpose test to distinguish “physical fitness services” from personal services or activities not subject to retail sale tax in the context of yoga classes: ETA 3003.2016 “Taxability of Yoga, Tai Chi, and Qi Gong,” issued March 14, 2016 (“ETA 3003”).⁶ ETA 3003 applies to periods ending on or before December 31, 2015.⁷

ETA 3003 provides:

The Department generally presumes that classes offering the traditional practices of Yoga, Tai Chi and Qi Gong do not constitute “physical fitness services” because physical fitness is a secondary or incidental benefit of these classes, but it is not typically the primary focus. This presumption may be overcome by showing that the primary purpose of the class is physical fitness.

However, when these classes are conducted at a health or athletic club, fitness center, health spa, or similar facility (“fitness facility”), the presumption is that the primary focus of any such class is physical fitness, and that the class therefore does constitute a “physical fitness service.” Community centers, parks, school gymnasiums, universities, colleges, hospitals, medical facilities, and private residences are not considered fitness facilities for purposes of this advisory.

A person providing Yoga, Tai Chi and Qi Gong class(es) at a fitness facility may overcome these presumptions that the class is a physical fitness service with

⁵ The LIGHT classes also have an element of nutrition advice. Effective January 1, 2016, RCW 82.04.050 was amended to exclude from the definition of a retail sale “[s]eparately stated charges for services, such . . . nutritional consulting . . . that do not require the customer to engage in physical fitness activities to receive the service.” RCW 82.04.050(3)(g)(ii)(C). However, this exclusion further explains that it does not apply to “personal training services and instruction in a physical fitness activity.” *Id.*

⁶ ETA 3003 was issued before the Audit Period.

⁷ Effective January 1, 2016, RCW 82.04.050 was amended to exclude from the definition of retail sale “[y]oga . . . held at a community center, park, school gymnasium, college or university, hospital or other medical facility, private residence, or any other facility that is not operated within and as part of an athletic or fitness facility.” RCW 82.04.050(3)(g)(ii)(H). Here, because the yoga classes are operated as part of an athletic or fitness facility, Taxpayer’s Yoga classes would be included within the definition of a retail sale under RCW 82.04.050(3)(g)(i) as a charge for the use of an athletic or fitness facility after January 1, 2016.

evidence demonstrating the primary purpose of the class. Such evidence may include, but is not limited to, lesson plans or other similar materials that identify the specific curriculum followed in the class indicating that physical fitness related activities are not the primary focus of the class. For example, in the case of a Yoga class this would include a class curriculum that places significant emphasis on breath regulation, meditation, and/or discussion of the historical and philosophical origins of Yoga with the incidental physical fitness related activities.

(Emphasis in original.)

Here, Taxpayer operates a fitness facility, because Taxpayer's facility is similar to an athletic club or fitness center, so there is a presumption that the primary focus of the Yoga class offered at Taxpayer's facility is on physical fitness. We conclude that Taxpayer's Yoga class description does not overcome the presumption in ETA 3003. First, the full name of the Yoga class is "flow yoga and **body maintenance**" (emphasis added). The "body maintenance" in the title of the class suggests that physical fitness is a primary focus of the class. Second, nothing in the class description indicates a discussion of anything related to the historical and philosophical origins of yoga. The Yoga class seems to be focused on improving postures and reducing physical stress, both of which are associated with physical fitness. Accordingly, because Taxpayer's Yoga class does not overcome the presumption in ETA 3003, we conclude that Taxpayer's Yoga class is also subject to retailing B&O and retail sales tax.

Because all of Taxpayer's classes are subject to retailing B&O and retail sales tax, the Department properly assessed Taxpayer with retailing B&O and retail sales tax on income received from sales of those classes.

Taxpayer also requests a waiver of penalties and interest based on RCW 82.32.055. RCW 82.32.055(1) provides:

Subject to the requirements in subsections (2) through (4) of this section, the department shall waive or cancel interest and penalties imposed under this chapter if the interest and penalties are:

- (a) Imposed during any period of armed conflict; and
- (b) Imposed on a taxpayer where a majority owner of the taxpayer is an individual who is on active duty in the military, and the individual is participating in a conflict and assigned to a duty station outside the territorial boundaries of the United States.

RCW 82.32.055(2) provides that a copy of deployment orders for deployment outside the territorial boundaries of the United States must be submitted. Here, Taxpayer has submitted deployment orders showing that its majority owner was on active duty in the military, participating in an armed conflict, and assigned to a duty station outside of the United States during the Audit Period. Accordingly, the penalties and interest must be waived for the period during which Taxpayer's owner was on active duty.

DECISION AND DISPOSITION

Taxpayer's petition is granted as to the penalties and interest, and denied as to the retailing B&O tax and retail sales tax. Interest must be calculated from the day Taxpayer's owner was no longer on active duty: March 12, 2016.

Dated this 17th day of January 2018.