Cite as Det. No. 21-0048, 42 WTD 025 (2023)

BEFORE THE ADMINISTRATIVE REVIEW AND HEARINGS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Correction of Assessment of	)	D E T E R M I N A T I O N
	)	No. 21-0048
. . .	)	Registration No. . . .

[1] RCW 82.08.031; WAC 458-20-249: RETAIL SALES TAX – EXEMPTIONS – ARTISTIC AND CULTURAL ORGANIZATIONS – OBJECTS FOR EXHIBITION OR PRESENTATION TO PUBLIC. Rentals consisting solely of equipment constitute "objects" for the purposes of the retail sales tax exemption provided by RCW 82.08.031 and Rule 249, even if the entity providing the rental equipment sets up and/or takes down the equipment for the customer.

[2] RCW 82.08.031; WAC 458-20-249: RETAIL SALES TAX – EXEMPTIONS – ARTISTIC AND CULTURAL ORGANIZATIONS – OBJECTS FOR EXHIBITION OR PRESENTATION TO PUBLIC. Rentals of equipment that include an operator constitute services – not objects – and sales of such are not eligible for the retail sales tax exemption provided by RCW 82.08.031 and Rule 249.

[3] RCW 82.08.050; WAC 458-20-102: RETAIL SALES TAX – EXEMPTION CERTIFICATIONS – SELLER'S LIABILITY FOR UNCOLLECTED TAX. A seller that accepts in good faith a fully-completed exemption certificate from its buyer is excused from its responsibility to collect and remit retail sales tax on the subject sale, regardless of whether the subject of the sale or the buyer actually qualifies for the subject exemption.

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.

Farquhar, T.R.O. – An audio equipment rental company protests the Department's disallowance of a retail sales tax exemption the company claimed in relation to its rentals of audio equipment to artistic or cultural organizations. The subject exemption applies only to qualified buyers on sales of certain objects, and the Department determined that the company provides a service–not a rental of an object–when an operator accompanies the rented equipment. We conclude that the company is not entitled to the exemption on rentals of audio equipment that include an operator, but is entitled to the exemption on rentals of bare equipment. The company also argues that it is not liable for retail sales tax it failed to collect on non-qualifying equipment rentals if it accepted a

certification of tax-exempt status from the buyer. We agree with the company on this second issue. We deny the petition in part and grant it in part, and remand the matter to the operating division for adjustment subject to verification of the exemption certificates the company provided.[1]

ISSUES

1. Whether the rental of audio equipment with or without an operator constitutes rental of an "object" such that it qualifies as tax-exempt under RCW 82.08.031 and WAC 458-20-249 when purchased by a qualifying artistic or cultural organization.

2. Whether RCW 82.08.050 excuses a taxpayer from liability for failing to collect retail sales tax on unqualified sales if the taxpayer accepted an exemption certificate from its buyer.

FINDINGS OF FACT

. . . ("Taxpayer") is a business based in . . . Washington that rents audio equipment to customers for use in concerts, festivals, meetings, and other events. The equipment includes speakers, cables, and other items necessary for sound amplification. Taxpayer's rentals can be categorized into two general groups: rentals of bare equipment, where the customer is responsible for providing their own personnel to operate the equipment ("bare rentals"), and rentals that include one of Taxpayer's employees to set up, remove, and operate the equipment. We have previously referred to such rentals as "rentals of equipment with an operator." *See* Det. No. 00-073, 19 WTD 1032 (2000). It is unclear what percentage of Taxpayer's sales fall into each category. When a rental includes an operator, the customer may direct the operator on where to set up the equipment and how to operate it during the event. After an event ends, the customer or operator removes the equipment from the venue. Taxpayer does not permanently install audio equipment.

For the purposes of this case, Taxpayer's customers also can be categorized into two general groups: artistic or cultural organizations, as defined by RCW 82.04.4328 and WAC 458-20-249 ("Rule 249"), and all other customers. RCW 82.08.031 entitles qualifying artistic or cultural organizations to an exemption from retail sales tax on purchases of certain objects ("the Exemption"). In order to utilize the Exemption, such qualifying organizations are required to provide Taxpayer with an exemption certificate that contains certain language to document the organization's eligibility for the Exemption. It is unclear what percentage of Taxpayer's customers provided an exemption certificate when making purchases from Taxpayer.

During the subject periods, one of Taxpayer's customers was . . . ("the Customer"). The Customer is a registered 501(c)(3) nonprofit organization that operates a . . . in . . . Washington. *See* www. . . . . The Customer presented Taxpayer with an exemption certificate and, in doing so, represented to Taxpayer that it was eligible for the Exemption. Taxpayer asserts that it believed the Customer was eligible for the Exemption when the sales occurred and, therefore, Taxpayer did not collect retail sales tax from the Customer. The Department later determined that the Customer was ineligible for the Exemption.

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

In April of 2017, the Department's Taxpayer Account Administration Division ("TAA") began a review of Taxpayer's records and business activities for the period of April 1, 2013, through December 31, 2013 ("the Examination Period").[2] TAA sought to verify Taxpayer was entitled to "deductions taken as 'Sales to Nonprofit Organizations of Artistic/Cultural Art Objects for Display[.]'" TAA's Response to Taxpayer's Petition, pg. 1. TAA requested that Taxpayer provide documentation to support the deductions, as well as copies of "any related exemption certificates . . . [Taxpayer] received from clients." *Id*. Taxpayer initially did not respond to the request, but eventually provided copies of exemption certificates it received from its customers. However, Taxpayer did not provide copies of sales invoices or contracts with its customers.

After reviewing the documentation provided by Taxpayer, TAA determined that the rentals with an operator constituted a retail service, not an object. As such, TAA disallowed the deductions for those sales, reasoning that the Exemption only applies to objects.

On February 9, 2018, TAA issued eight invoices to Taxpayer totaling $. . . . The amounts due represent the value of the disallowed deductions Taxpayer claimed during the Examination Period. Taxpayer has not paid the invoices. The invoices are summarized in the following table:

Invoice Number	Period/Year	Balance Due
24	April 2013	$ . . .
25	May 2013	$ . . .
26	June 2013	$ . . .
27	July 2013	$ . . .
28	August 2013	$ . . .
29	September 2013	$ . . .
31	November 2013	$ . . .
32	December 2013	$ . . .
	Total	**$ . . .**

On June 18, 2018, Taxpayer submitted a timely petition for review. In it, Taxpayer argues that TAA improperly disallowed the deductions. Taxpayer stated that it received exemption certificates from its customers for all of the subject sales and that the equipment it provides should constitute rental of an "object" regardless of whether an operator accompanies the equipment. Taxpayer also argues that it should not be held liable for the retail sales tax it failed to collect from any customers that provided an exemption certificate.

ANALYSIS

1. *Whether Taxpayer's Rentals Constitute Rentals of "Objects."*

Washington imposes a retail sales tax on each retail sale made in this state. RCW 82.08.020. The term "retail sale" includes renting or leasing tangible personal property to consumers. RCW 82.04.050(4); *see also* WAC 458-20-211(6). WAC 458-20-211 ("Rule 211"), the Department's

[2] TAA is also examining Taxpayer's business for the same issue for the periods of January 1, 2014, through December 31, 2016, and for other periods as recent as May of 2019, though it has not yet completed its examination. TAA has indicated that it is awaiting the results of our review before completing its examination.

administrative rule regarding leases or rentals of tangible personal property, refers to rentals of "unoperated" equipment as rentals of "bare . . . equipment." Rule 211(5).

The definition of "retail sale" also includes rentals of equipment with an operator. RCW 82.04.050(9) includes the following in the definition of "retail sale:"

> [T]he charge made for providing tangible personal property along with an operator for a fixed or indeterminate period of time. A consideration of this is that the operator is necessary for the tangible personal property to perform as designed. For the purpose of this subsection (9), an operator must do more than maintain, inspect, or set up the tangible personal property.

Rule 211 defines "rental of equipment with operator" as follows:

> [T]he provision of equipment with an operator to a lessee to perform work under the specific direction of the lessee. In such cases the lessor is generally not responsible for performing work to contract specification and does not determine how the work will be performed. . . .

Rule 211(2)(d).

Here, Taxpayer is engaged in the business of renting audio equipment. Taxpayer offers both bare rentals and operated rentals.[3] Because rentals of equipment with or without an operator are both subject to retail sales tax under RCW 82.04.050(4) and (9), Taxpayer must, pursuant to RCW 82.08.020, collect retail sales tax from all of its customers, unless an exemption or exclusion applies. As such, we will now discuss whether the Exemption applies to any of Taxpayer's sales.

RCW 82.08.031 provides the following exemption from retail sales tax:

> The tax levied by RCW 82.08.020 shall not apply to sales to artistic or cultural organizations of *objects* which are acquired for the purpose of exhibition or presentation to the general public if the objects are:
>
> (1) Objects of art;
> (2) Objects of cultural value;
> (3) Objects to be used in the creation of a work of art, other than tools; or

[3] In this case, we presume that Taxpayer's operated rentals are indeed rentals of equipment with an operator under RCW 82.04.050(9). Rule 211 explains that some sales that involve an individual using equipment will constitute a professional service, which would be subject to the service and other activities B&O tax. Rule 211(2)(e). In such cases, Rule 211 instructs that we use a "true object test" to determine "if the lessee is simply purchasing the use of the equipment or purchasing the knowledge, skills, and expertise of the operator beyond those needed to operate the equipment." *Id.* A familiar example of a professional service is a wedding DJ who utilizes sound equipment, but who is, in fact, hired for the DJ's services, not the DJ's sound equipment. *See* Det. No. 08-0356, 28 WTD 81 (2009). However, ultimately, whether Taxpayer's services in this case are retail services or services subject to the service and other activities B&O tax classification is irrelevant because, in either situation, the services would not be objects under RCW 82.08.031—and therefore not eligible for the Exemption—as discussed in the body of this determination.

(4) *Objects to be used in displaying art objects or presenting artistic or cultural exhibitions or performances*."

RCW 82.08.031 (emphasis added).

Rule 249 is the Department's administrative rule interpreting sales involving artistic and cultural organizations. Rule 249 states that the word "objects" in RCW 82.08.031 "means *items of tangible personal property* . . . [and] does not include professional or commercial *services* rendered by third parties." Rule 249(4)(c) ("Retail Sales Tax" section) (emphasis added). Rule 249 also states that "exempt sales include rentals of exempt objects." *Id*. Rule 249 goes on to provide examples of objects that may be purchased by qualifying artistic or cultural organizations without payment of retail sales tax. Rule 249(e). Such objects include "sound systems, video and sound equipment . . . directly used exclusively in the staging of performances or actual display of art objects." *Id*.

Before continuing our analysis, we first note that in order for a sale to qualify for the Exemption under RCW 82.08.031, the sale or rental must feature a qualifying object *and* a qualifying buyer. RCW 82.08.031. Our analysis will focus only on the first element: whether Taxpayer's rentals are of qualifying "objects." Whether Taxpayer's customers qualify as artistic or cultural organizations was not raised in the Petition or by TAA and, therefore, we will not address that issue here.

In order for the Exemption to apply to any of Taxpayer's sales, we must find that the subject of the rental is an "object," which is defined by Rule 249 as an item of tangible personal properly. Taxpayer offers bare rentals and operated rentals. We will address the two categories in turn.

a. Bare Rentals

The first category—bare rentals—requires little analysis. Because bare rentals include only physical equipment, and Rule 249 specifically lists "sound systems" and "sound equipment" as examples of exempt objects, we conclude that Taxpayer's bare rentals constitute rentals of "objects" for the purposes of the Exemption and are exempt from retail sales tax under RCW 82.08.031 when the sales are made to qualifying buyers.[4]

We also conclude that instances in which one of Taxpayer's employees merely sets up or takes down equipment for the customer also constitute bare rentals. The basis for this comes from RCW 82.04.050(9), which states that, to be considered a rental "with an operator," the "operator must do more than maintain, inspect, or set up the tangible personal property." Therefore, RCW 82.04.050(9) establishes the demarcation between bare rentals and operated rentals: if a

[4] We note that TAA denied all of the deductions Taxpayer claimed, which may include both bare rentals and operated rentals. Presumably, under TAA's theory that operated rentals constitute a "service," only those sales involving operated rentals should have been denied. While we conclude that Taxpayer's bare rentals are eligible for the Exemption, we note that Taxpayer has failed to produce sales invoices, contracts, or other documents that would allow us to identify which rentals actually meet the "bare equipment" definition. While such documentation would normally be required to determine whether a sale qualified, our analysis of Issue 2 below concludes that Taxpayer is absolved from liability for failing to collect retail sales tax in instances where Taxpayer received an exemption certificate from the buyer. Therefore, Taxpayer need not produce additional documentation for sales that are covered by an exemption certificate in order to receive relief from retail sales tax liability for those sales.

representative of the entity offering the rental equipment does more than "maintain, inspect, or set up" the rental equipment, the rental can no longer be considered a bare rental.

b. Operated Rentals

The second category of sales are "operated rentals." These rentals include physical equipment like bare rentals, as well as the services of one of Taxpayer's employees who operate the equipment during the customer's event, in addition to setting up and removing the equipment. The operator sometimes takes direction from the customer on where to place the equipment and how to operate it (e.g., adjusting volume) during the event. Therefore, an operated rental meets Rule 211's definition of a "rental of equipment with operator." Rule 211(2)(d).

Ultimately, we conclude that operated rentals constitute a service—not an object—and sales of such are not eligible for the Exemption. We reached this conclusion by reviewing several sources that indicate the Department considers such rentals to be retail *services*, not sales of tangible personal property. For instance, Rule 211 includes the following provision regarding whether the Department treats such rentals as objects or services:

> Persons who provide equipment or other tangible personal property and, in addition, operate the equipment or supply an employee to operate the same for a charge, without relinquishing substantial dominion and control to the customer, *are providing a service* that is classified as a retail sale unless the nature of the activity is specifically classified under another tax classification.

Rule 211(5)(b) (emphasis added.)

We can also look to Excise Tax Advisory ("ETA") 3118.2009 (2009), which discusses whether rentals that include an operator are considered "tangible personal property" (i.e. objects) for the purposes of the machinery and equipment exemption available to manufacturers under RCW 82.08.02565 and RCW 82.12.02565. ETA 3118.2009 states, in pertinent part, that "[p]roviding tangible personal property along with an operator is a sale of a service and not a sale of tangible personal property." *See also* Washington Department of Revenue, Services Subject to Sales Tax, https://dor.wa.gov/find-taxes-rates/retail-sales-tax/services-subject-sales-tax, (last visited Feb. 16, 2021) (providing a list of services that are subject to sales tax, including "providing tangible personal property with an operator").

As noted above, TAA disallowed all of the deductions Taxpayer claimed. We find that TAA was correct to disallow deductions for operated rentals, as they constitute retail services and are not eligible for the Exemption. However, in cases where Taxpayer received an exemption certificate for the operated rentals, Taxpayer might still be relieved of its obligation to collect retail sales tax on those sales, as we will discuss in our analysis below.

2. Whether Taxpayer is Excused from Liability for Uncollected Retail Sales Tax.

The second issue raised in the Petition is whether Taxpayer can be held liable for retail sales tax it did not collect on sales where Taxpayer accepted an exemption certificate (e.g., in the case of sales

to the Customer). RCW 82.56.010, the statutory provision that codifies the Multistate Tax Compact (MTC), states as follows:

> Whenever a vendor receives and accepts in good faith from a purchaser a resale or other exemption certificate or other written evidence of exemption authorized by the appropriate state or subdivision taxing authority, the vendor shall be relieved of liability for a sales or use tax with respect to the transaction.

RCW 82.56.010, Article V, paragraph 2.

RCW 82.08.050(7) also states that sellers will be relieved from retail sales tax liability if they obtain an exemption certificate from their buyers. The seller is required to obtain the exemption certificate within ninety days of the date of sale. However, if a seller does not obtain an exemption certificate within ninety days of the sale, RCW 82.08.050(7)(b) allows the seller to obtain a fully completed exemption certificate from the purchaser within one hundred-twenty days of a Department request. RCW 82.08.050(7) provides the following:

> (a) Sellers are relieved from personal liability for the amount of tax if they obtain a fully completed exemption certificate or capture the relevant data elements required under the streamlined sales and use tax agreement within ninety days, or a longer period as may be provided by rule by the department, subsequent to the date of sale.
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> (b) If the seller has not obtained an exemption certificate or all relevant data elements required under the streamlined sales and use tax agreement within the period allowed subsequent to the date of sale, the seller may, within one hundred twenty days, or a longer period as may be provided by rule by the department, subsequent to a request for substantiation by the department, either prove that the transaction was not subject to tax by other means or obtain a fully completed exemption certificate from the purchaser, taken in good faith.

RCW 82.08.050(7). *See also* WAC 458-20-102 [(Department rule addressing reseller permits on wholesale sales)].

Notably, RCW 82.08.050(7)(a) does not require that the seller accept an exemption certificate in good faith.

Here, the Department determined that some of the sales that Taxpayer made to customers who provided an exemption certificate were ineligible for the Exemption and the Department assessed retail sales tax on those sales. For example, the Department determined that the Customer was ineligible for the Exemption after the sales in question occurred. Therefore, the Department concluded that Taxpayer's sales to the Customer did not qualify because the Customer was not an eligible buyer. In other cases, a buyer may have provided an exemption certificate for a rental that was later deemed to be a rental with operator, which constitutes a service, not [rental of] an object, and is not eligible for the Exemption. It is unclear whether any of Taxpayer's other sales involved similar circumstances—namely that Taxpayer accepted an exemption certificate, but the Department later determined the sale was not eligible for the Exemption and assessed tax.

We conclude that RCW 82.08.050(7)(a) excuses Taxpayer from its responsibility to collect and remit retail sales tax if Taxpayer accepted a fully-completed exemption certificate from its buyer, regardless of whether the subject of the rental or the buyer actually qualifies. We previously addressed this issue in Det. No. 18-0205, 38 WTD 272 (2019) where we found that "[t]axpayers have no statutory duty to investigate the validity of the exemption being claimed by the buyer, only to obtain a 'fully completed' exemption form." 38 WTD at 276. By disallowing the Exemption because the sale did not qualify, Audit "has imposed upon the seller a burden to investigate and conclusively determine the buyer's eligibility for an exemption." *Id.* at 276-277. The relevant statutes and rules contain no such burden.

Therefore, we conclude that the Department erred in assessing retail sales tax on any transaction where Taxpayer accepted a fully-completed exemption certificate from its buyer. It is unclear what percentage of the subject transactions were covered by exemption certificates that Taxpayer received from its buyers, therefore we remand this matter to the operating division for review of the documentation Taxpayer provided. The amounts assessed against Taxpayer will then be adjusted to remove any retail sales tax liability associated with sales that were covered by completed exemption certificates. Furthermore, if any of the certificates are found to be incomplete, Taxpayer would have one hundred-twenty days after the Department requested additional documentation, to provide a valid exemption certificate. RCW 82.08.050(7)(b).

DECISION AND DISPOSITION

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

Dated this 2nd day of March 2021.