IN THE SUPREME COURT OF MISSOURI

TATSON, LLC d/b/a POWERHOUSE GYM OF JOPLIN,	)	
Respondent,	)	
v.	)	Case No. SC94260
DIRECTOR OF REVENUE,	)	
Appellant.	)	

RESPONDENT'S BRIEF
OF TATSON, LLC D/B/A POWERHOUSE GYM OF JOPLIN

ON WRIT OF REVIEW
FROM THE ADMINISTRATIVE HEARING COMMISSION

Paul A. Boudreau – Mo Bar #33155
BRYDON, SWEARENGEN & ENGLAND, P.C.
312 East Capitol Avenue
P.O. Box 456
Jefferson City, MO 65102-0456
Telephone: 573-635-7166
Facsimile: 573-634-7431
E-mail: paulb@brydonlaw.com
Attorney for Tatson, LLC d/b/a Powerhouse Gym of Joplin

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Constitutional Provisions

Statutes

Other Authorities

JURISDICTIONAL STATEMENT

Jurisdiction is proper in this court because this appeal involves the construction of one or more revenue laws of this state. *Mo. Const.*, Art. V, § 3; § 621.189 RSMo.

STATEMENT OF FACTS

Respondent in the case is Tatson, LLC d/b/a Powerhouse Gym of Joplin ("Powerhouse Gym" or "Respondent"). This case involves a Missouri tax audit covering the period October 2008 through September 2011. (Tr. Exh. A)[1] Appellant audited Respondent in November of 2011. (Tr. 31) The results of the audit were contained in an audit report. (Tr. Exh. A)

Powerhouse Gym is a full-service fitness facility. (Tr. 7) It offers the following services to its members: Member child care, fitness classes like Zumba, yoga and Pilates and a full selection of strength/cardiovascular equipment. (Tr. 7) There is a pro shop on the premises. (Tr. 8) Powerhouse Gym is fully staffed at all times. (Tr. 8)

Individuals that use the services offered by Powerhouse Gym must be paying members of the facility. (Tr. 8) Powerhouse Gym offers one- or two-year basic membership contracts. (Tr. 8) Powerhouse Gym collects and remits to Appellant sales taxes on membership fees collected from individuals joining the facility. (Tr. 9, 37)

As is relevant to audit period, Powerhouse Gym entered into a verbal, month-to-month agreement with Atlanta Fitness, d/b/a Custom Built ("Custom Built") for a lease of office space on premises. (Tr. 14, 19, 21) The rental for the sublease of the office paid by Custom Built was a flat $6,000 per month of occupancy. (Tr. 14-15) Custom Built

[1] The abbreviations to record or citations herein are as follows: "Tr." for transcript, "Exh." For exhibit, "L.F." for legal file and "App." for Respondent's Rule 84.04(h) appendix on appeal.

had exclusive use of the office for its own business purposes during its term of occupancy. (Tr. 15, 20) Custom Built provided its own computers. (Tr. 15, 20) Custom Built furnished its own desks and furniture. (Tr. 15, 19, 20) Custom Built provided its own office supplies and equipment. (Tr. 15, 19, 20) Custom Built paid for its own telephone and internet services. (Tr. 19) Custom Built carried liability insurance coverage for itself and its employees. (Tr. 22)

Custom Built offered personal training and other fitness services to individuals, services Powerhouse Gym did not offer. (Tr. 11, 15, 21) The office space subleased to Custom Built was used for consultations and sales interactions. (Tr. 22) The services offered by Custom Built were available only to those individuals who already were paying members of Powerhouse Gym. (Tr. 13) Custom Built contracted directly with members of Powerhouse Gym. (Tr. 14) The personal training and other fitness services were provided by employees of Custom Built. (Tr. 15) Custom Built trainers were allowed to use the fitness equipment of Powerhouse Gym in order to train individuals who signed up for personal training services. (Tr. 15) Custom Built's employee-trainers did not use the fitness equipment to work out for their own personal benefit. (Tr. 16-17) They may, however, have used the fitness equipment of Powerhouse Gym to demonstrate its proper use for gym members with whom Custom Built contracted. (Tr. 21)

Powerhouse Gym did not supervise, monitor, manage or control the activities of Custom Built's employee/trainers. (Tr. 16) Powerhouse Gym did not provide any fitness services to the employees of Custom Built. (Tr. 16) Powerhouse Gym received no

revenue from the sale of Custom Built's personal service contracts nor did it share profits indirectly through cross-ownership or affiliation with Custom Built. (Tr. 11, 13, 14)

Powerhouse Gym reported the Custom Built lease income on its state and federal income tax returns. (Tr. 15) Appellant's auditor determined that $150,000 of the lease income from Custom Built had not been included in sales tax returns filed by Respondent. (Tr. 29) The auditor's legal conclusion was that the rental income was a fee paid in or to a place of amusement within the meaning of §144.020.1(2) RSMo. (Tr. 36) The audit report concluded there is a sales tax due on the sublease revenues in the amount of $11,737.50. (Tr. 29; Tr. Exh. A)

The Commission made Findings of Fact[2] and Conclusions of Law.[3] Applying the "plain meaning and intent of §144.020.1(2) [RSMo]," the Commission found that it was Custom Built, and not Powerhouse Gym, that was charging a fee at retail in a place of recreation and that Respondent that was not liable for sales tax and interest on payments it received from Custom Built. L.F. 9-10.

[2] L.F. 5-6.

[3] L.F. 6-8.

POINT RELIED ON

I. THE COMMISSION'S ORDER IS AUTHORIZED BY LAW AND SUPPORTED BY COMPETENT AND SUBSTANTIAL EVIDENCE BECAUSE IT DID NOT ERR IN DETERMINING THAT THE MONTHLY OFFICE LEASE PAYMENTS RECEIVED FROM CUSTOM BUILT WERE RENT FOR OCCUPANCY AND NOT A SALE OR RENTAL OF TANGIBLE PERSONAL PROPERTY OR A FEE PAID TO POWERHOUSE FOR A TAXABLE SERVICE RENDERED AT RETAIL.

§144.020.1(2) RSMo.

J.B. Vending Co .v. Director of Revenue, 54 S.W.3d 183 (Mo. banc 2001)

Jaudes v. Director of Revenue, 248 S.W.3d 606 (Mo. banc 2008)

STANDARD OF REVIEW

Respondent concurs with Appellant's summary of the standard of review in this case. (Appellant's Brief, p. 13)

ARGUMENT

I. The Commission's Order is authorized by law and supported by competent and substantial evidence because it did not err in determining that the monthly office lease payments received from Custom Built were rent for occupancy and not a sale or rental of tangible personal property or a fee paid to Powerhouse for a taxable service rendered at retail.

The single question in this case presented to the Commission was whether the payments made by Custom Built to lease office space from Powerhouse Gym amounted to the rendering by Powerhouse Gym of a taxable **service at retail** to, or for the benefit of, Custom Built. It was Respondent's contention that the rental of office space to Custom Built, in order for the latter to carry on an independent business enterprise, is not a taxable service within the meaning of §144.020 RSMo and, in any event, that it is not a retail transaction even if it were to be viewed as a fee for service.

The Commission concluded that the evidence supported the conclusion that the monthly payments were "rental" for an office. (L.F. 5, 6 and 6 at ftnt. no. 1) The Commission further found that "Powerhouse Gym is neither selling or renting tangible personal property, nor is it providing a service at retail to Custom Built." (L.F. 8) These findings of fact are amply supported by the record and they are in full accord with the controlling law. In the case of *J.B. Vending Co .v. Director of Revenu*e, 54 S.W.3d 183 (Mo. banc 2001), this Court stated the following:

> Considered in context, the statute as a whole evinces a legislative intent to tax all sellers for the privilege of selling tangible personal property or rendering a taxable service.

Id. at 188. Consequently, this Court must defer to the Commission's conclusion absent a showing that its findings are against the great weight of the evidence or that they are clearly erroneous or arbitrary and capricious. Appellant has failed to make any such showing.

The record evidence demonstrated that Powerhouse Gym provided no service to Custom Built. Rather, Respondent simply rented out office space[4] and granted an associated, limited license[5] for Custom Built to accompany and instruct members of the

---

[4] The audit report and auditor testimony support this conclusion. The audit report refers to the revenue in question as "sublease payments". (Tr. 33-34) Questions put to the auditor by Respondent's counsel address it in terms of "lease income". (Tr. 29) While use of this terminology may not be determinative of the question, it certainly is strongly indicative of the nature of the business arrangement. If it looks, swims, waddles and quacks like a duck, it's probably a duck.

[5] A license is a peculiar species of right that one person can have in the real property of another. It is "in respect of real property is an authority or permission to do a particular act or series of acts upon the land of another without possessing any interest or estate in such land." *Kohlleppel v. Owens,* 613 S.W.2d 168, 176 (Mo. App. 1981). *See also*, Missouri Practice, Vol. 18 (Real Estate Law) §27:4.

gym when using the other areas of the facility; in this case, the fitness equipment. Custom Built utilized the office space to sign up its own customers (who were already Powerhouse Gym members) in order to provide personal training services. It is undisputed that Powerhouse Gym collected and remitted sales taxes on all persons who paid fees to become members of Powerhouse Gym and to use its facilities. *See, Jaudes v. Director of Revenue*, 248 S.W.3d 606 (Mo. banc 2008). As such, all fees paid to Powerhouse Gym during the period of the audit have been properly taxed and those taxes have been remitted to Appellant as required by law.

The evidence fully supports the Commission's finding that Powerhouse Gym provided no service at retail to the employees of Custom Built. The rental arrangement did not provide for employees of Custom Built to use the fitness equipment to train on themselves. No evidence was introduced showing that the employees of Custom Built were members of Powerhouse Gym. As such, the claim that the rental payments were in the nature of a fee paid to Powerhouse Gym as a place of amusement or recreation is simply not supported by the facts established at the hearing.

In essence, Appellant is arguing that the sales tax law transforms rent paid on a sublease of real estate into an admission fee and, therefore, the revenue is taxable under §144.020.1(2) RSMo. This represents a fundamental misunderstanding of the term "fee" which is not defined in the statute. In such circumstances, the word in a statute is to be given its plain and ordinary meaning. §1.090 RSMo 2000. That meaning is to be found by reference to the English language dictionary. *Roberts v. McNary*, 636 S.W. 2d 332 (Mo. banc 1982). A fee is defined as a charge or payment for professional services or a

sum or charge paid for a privilege such as an admission fee. *See*, Webster's Unabridged Dictionary, 2003. The term "fee" is not used in defining the word "rent". *Id.* The latter is understood to be in the nature of a yield or return on a piece of real estate. The term "fee" is not used in Missouri's Landlord-Tenant Law (Chapter 535 RSMo).

The essence of Appellants case is that it does not matter if the monthly payments were rent to occupy a portion of the premises. They are, Appellant asserts, a taxable service because the law says so. It is fundamentally wrong, however, to claim that the Missouri sales tax statute is substantive law that defines what the nature of a commercial transaction is. This has the statutory tail wagging the transactional dog. Whether or not a transaction is a sale at retail is a question of commercial custom and practice; not one of tax law. In other words, the applicability of the sales tax depends on the nature of the property involved (i.e., whether it is real or tangible property) and the nature of the transaction. The nature of the transaction is *not* determined by the language of the taxing law. To claim otherwise is to reveal a fundamental misapprehension of the concept of business taxation as derivative of commercial conventions.

Appellant further contends that the Commission has created ambiguity in its application of the sales tax laws. (Appellant's Brief p. 18) This is not so. The Commission applied the plain meaning of the tax law to the facts presented.

Missouri's sales tax law as relevant to this case is straightforward. Missouri has imposed a tax on sales of personal property. §144.020.1 RSMo.[6] The tax is imposed on the seller. *Id.* A sale at retail is defined as any transfer of title to **tangible personal**

[6] App. at A-4.

property for use or consumption, and not for resale. §144.010(11) RSMo.[7] (Emphasis added) The term includes, among other things, the sale of enumerated **services**, such as sales of admission charges to places of amusement or recreation.[8] §144.020.1(2) RSMo. The Commission correctly applied the plain language of the tax law to find that Powerhouse Gym did not sell or rent tangible personal property and,

[7] App. at A-2.

[8] Appellant's claim at page 15 of its brief that "[n]o one disputes that Powerhouse [Gym] was a place of recreation is an overstatement. This particular question was not an issue in the underlying case because Respondent collected and remitted to Appellant sales taxes on membership fees. Respondent has acknowledged this Court's holding in the *Jaudes* case as it concerns the collection of membership fees. However, whether resistance and cardio training are recreational within the plain meaning of the term, or whether the law was intended to apply only to fees paid for admission to spectator events, is a policy question that remains open to legitimate debate. In this regard, this past legislative session, the Missouri General Assembly passed Senate Bill 584 which included amending language for §§144.010(10)(a) and 144.020(1) RSMo., that excluded fees paid for admission to fitness centers and gymnasiums. *See,* App. at A-22 to A23 and A-26 to A-27. The bill was one of several vetoed by Governor Nixon, nevertheless, the passage of the bill is strong indication of legislative intent. This Court retains the power and discretion to revisit the matter on its own motion.

further, that did not provide any service to Custom Built. (L.F. 8) The Commission's application of the law to the facts is unassailable.

For its contention that the plain meaning of the law is apparent, Appellant places primary reliance on two opinions of this Court, neither of which is apt. *Blue Springs Bowl v. Spradling*, 551 S.W.2d 596 (Mo. 1977) addressed fees charged by a commercial bowling establishment for its customers to participate in events such as tournaments in addition to any admission fee to enter the premises. *Bally's LeMan's Family Fun Centers v. Director of Revenue*, 745 S.W.2d 683 (Mo. banc 1988) addressed proceeds from customers who used coin-operated game devices. In both cases, the issue was participation fees paid **by patrons of an establishment**.[9] This is a crucial factual distinction because there was no question in those cases that a service at retail had been provided by the seller to an end-user. In this case, the Commission found that Custom Built was not a patron of Powerhouse Gym.

The sublease payments made by Custom Built were a source of rental income that was properly reported by Powerhouse Gym on its state and federal income tax returns. Appellant has not demonstrated that Powerhouse Gym provided any taxable service at retail to Custom Built or its employees. The Court will search Appellant's brief in vain to find a description of the type of service Petitioner provided to Custom Built for which

[9] The Commission specifically noted that the *sin qua non* of taxability in prior cases turned on the fact that the transaction "has consistently inurred to the benefit of the patron." L.F. 8.

the latter can be said to have paid a fee. Powerhouse Gym did not enter into gym memberships with the employees of Custom Built. It did not assist with marketing Custom Built's business. It did not permit the lessee's trainers to use the gym's fitness equipment for their own, personal use. The bottom line is that Custom Built did not **take** a service from Respondent. Rather, it **provided** a service as an independent contractor to its own customers who also were members of Powerhouse Gym.

This argument was acknowledged in the *Jaudes* case wherein this Court stated that fitness services provided by a personal trainer at a facility not owned by him would not be taxable either to the trainer or to the facility at which he worked. *Jaudes* at 610. "Training services provided by an independent contractor are different in kind from a business that offers training services along with the provision of exercise equipment, lockers, and other amenities at a permanent, established fitness facility." *Id.* at 611.

To the extent that Appellant's office rent-as-service theory is justified (and Respondent specifically disputes that the characterization is justified), it is in the nature of a **wholesale** transaction in that Powerhouse Gym made its own facility available to Custom Built which, in turn, used the leased premises to market its own services and to enter into end-use arrangements with Powerhouse Gym members providing services which were not offered by Powerhouse Gym. A wholesale of this nature would not be subject to taxation pursuant to §144.020 RSMo, because that statute only provides for taxation of **retail** transactions.

What the Commission had before it in the underlying case was a simple office space rental arrangement (coupled with a very restricted license) that is not subject to

sales taxation under §144.020.1(2) RSMo. The month-to-month sublease involved the grant of an interest in **real estate** by Petitioner to Custom Built. This, obviously, did not involve the sale or transfer of tangible personal property which is covered by the sales tax law. Powerhouse Gym witness, Jason Zurba, explained Respondent's position by simple and compelling analogy.

> In our opinion, it would be no different than if we rented a corner of our pro shop to a smoothie company or we rented out the corner of our parking lot to a drive through coffee shop. (Tr. 23)

It was space rental. As such, the monthly payments were anchored in notions of real property conveyancing; not sales of personal property or services. In light of this and other evidence, the Commission concluded, correctly, that the monthly rent payments were not subject to Missouri sales tax.

CONCLUSION

Custom Built was not a customer of Powerhouse Gym. Custom Built merely rented office space from Powerhouse Gym. As such, Respondent provided no service to Custom Built.

Even if the lease of office space were to be considered in the nature of a service, it was wholesale in nature in that it only enabled Custom Built to provide services to its customers on the premises of Powerhouse Gym. Those payments only permitted Custom Built, as an independent contractor, to occupy space on the premises in order to market and provide services (i.e., consultation and personal training) to gym members. As pointed out above, Custom Built was not **taking** a service from Respondent. It was **providing** a service to its own customers. The sale tax statute only applies to sales or services at retail.

The Commission's factual findings that the business arrangement in question was space rental and, further, that Respondent provided no taxable service to Custom Built both are supported by competent and substantial evidence. The Commission's holding that no sales tax is due and owing on the $150,000 of rental income earned by Respondent during the period of the audit represents a correct application of the sales tax law. Consequently, its decision should be affirmed by this Court.

Respectfully submitted,

/s/ Paul A. Boudreau
Paul A. Boudreau - #33155
BRYDON, SWEARENGEN & ENGLAND P.C.
312 East Capitol Avenue
P.O. Box 456
Jefferson City, MO 65102-0456
Telephone: (573) 635-7166
Facsimile: (573) 635-0427
paulb@brydonlaw.com
Attorney for Respondent

CERTIFICATE OF COMPLIANCE

The undersigned hereby certifies pursuant to Supreme Court Rule 84.06(c) that this brief includes the information required by Rule 55.03, complies with the limitations contained in Rule 84.06(b), and contains 3,170 words (exclusive of the cover, certificates of compliance and service, and signature block), as calculated by Microsoft Word, the software used to prepare this brief.

/s/ Paul A. Boudreau
Paul A. Boudreau

CERTIFICATE OF SERVICE

The undersigned certifies that a true and correct copy of the foregoing document was sent by electronic mail, US Mail or hand delivery to the following party this 14th day of October, 2014:

Evan J. Buchheim
Assistant Attorney General
P.O. Box 899
Jefferson City, MO 65102
Phone: (573) 751-4129
Fax: (573) 751-5391
Evan.buchheim@ago.mo.gov

/s/ Paul A. Boudreau
Paul A. Boudreau