September 15, 2004

<name>
<company>
<address>

Formal Ruling 04-08

Dear <name>:

You have requested rulings as to the applicability of the Vermont sales tax under 32 V.S.A. §9771(4) to refundable deposits received by <company>, (the "Club") from new members. The Club specifically requests the following rulings:

A. The receipt of a refundable deposit by the Club does not constitute a transaction that is subject to the Vermont sales tax.

B. Alternatively, if the receipt of refundable deposit by the Club is determined to constitute a transaction that is subject to the Vermont sales tax, the "sales price" for purposes of calculating the sales tax may be based on the amount by which the refundable deposit exceeds the present value of the Club's obligation to return the refundable deposit, as determined by using (i) the applicable federal rate for the month in which the refundable deposit is received and (ii) the average period of time that the Club anticipates refundable deposits will be held.

The following rulings rely upon the facts as presented in your written request dated June 21, 2004 that are summarized, in pertinent part, as follows:

FACTS

The Club will be the owner and operator of a four-season resort club featuring an [athletic and other facilities]. The Club is offering a limited number of membership interests, of different classes, to interested persons. Each class of membership entitles its holder to certain rights and privileges specific to that membership interest. Membership in the Club does not provide a member with an equity or other property interest in the Club. A member only acquires a revocable license to use the Club facilities in accordance with the terms and conditions of the Membership Plan. All members, regardless of class, will be required to pay monthly membership dues that will be phased in as the facilities are completed. All members are also required to pay a refundable, non-interest bearing deposit (the "Refundable Deposit"). Deposits are entirely refundable to a continuing member after thirty years, and refundable in whole or in part, depending upon member class, to a resigned member with the balance refundable upon the member's thirtieth anniversary. Each Member's right to the return of the Refundable Deposit is subject to the Club's right of setoff for any dues, fees or other charges that a member owes to the Club. The amount of the Refundable Deposit, each member's right to a refund, and the number of membership interests to be offered, varies slightly with each membership class.

DISCUSSION and RULING

A. Applicability of Vermont Sales Tax to Refundable Deposit

32 V.S.A. § 9771(4) imposes a six-percent sales tax "upon receipts from…[a]musement charges." An "amusement charge" is defined, in pertinent part, as;

> …the admission charge (including any subsidiary, service or cover charge) to, and any charge for the use of any place of recreation or amusement including athletic events and facilities, exhibitions, dramatic and musical performances, motion picture theatres, golf courses and ski areas…. 32 V.S.A. § 9701(10).

32 V.S.A. § 9701(11) defines "place of amusement" as "…any place where any facilities for entertainment, recreation, amusement or sports are provided."

The factual description of the Club's membership benefits as featuring access to an 18-hole golf course, spa/fitness center, alpine ski club, restaurant and year-round swimming facility, falls squarely within the definition of a "place of amusement." It is well established that "amusement charges" include charges for membership in clubs, such as the Club at issue, where the purpose of membership is access to a recreation facility. *See* Brattleboro Tennis Club, Inc. v. Dept. of Taxes, 166 Vt. 604, 609 (1997). It has also been established that the term "amusement charges" includes both periodic charges and initiation charges. Mountain Cable Co. v. Dept. of Taxes, 168 Vt. 454 (1998). The remaining determinative question, therefore, is whether or not the Refundable Deposits at issue constitute taxable "receipts" from an amusement charge?

The term "receipt" is defined as follows:

> Receipt: means the amount of the sales price of any property and the charge for any amusement taxable under this chapter valued in money, *whether received as*

> *money or otherwise*, without any deduction for expenses or early payment discount; but *excluding any amount for which credit is allowed by the vendor to the purchaser*; and excluding any allowance, including core charges, made for a trade-in of like-kind property; and excluding any allowance in cash or by credit made upon the return of merchandise pursuant to warranty or the price of property returned by customers when the *full price* thereof is refunded either in cash or by credit. 32 V.S.A. § 9701(4) (*emphasis added*).

The plain language in the definition of "receipts" contemplates circumstances in which the "sales price" (or consideration) paid for products or services and upon which tax shall be levied, may or may not take the form of "money." *Id.* For practicality purposes in levying tax on such receipts, "sales price" is nevertheless required to be "valued in money" and must exclude cash or credit allowances to the purchaser. *Id.* Under the facts as described in the present case, the Club requires payment of a non-interest bearing Refundable Deposit as a condition precedent to a prospective member being granted a revocable license to use the Club facilities. The "value" of such a Refundable Deposit, thus, constitutes a "receipt" subject to sales tax. 32 V.S.A. § 9701(4).

It is commonly understood that the right to the interest-free use of money (thirty-years in the present case with Refundable Deposits ranging from $5,000 to $55,000) has significant value. The Club clearly contemplates receiving this value as partial payment in consideration of the benefits to be provided to its members. Accordingly, the Department disagrees with the Club's assertion that the Department lacks authority to impute an "amusement charge" relative to the Refundable Deposits at issue. In effectuating the statutory sales tax levy on receipts "…whether received as money or otherwise," it is incumbent upon the Department to ensure that taxpayers appropriately identify "sales price…*valued* in money" for purposes of accurately determining sales tax

liability. 32 V.S.A. § 9701(4) (*emphasis added*). In assigning monetary value for purposes of calculating sales or use tax in barter transactions, for example, the Department of Taxes relies upon the fair market value of what is received in order to identify the monetary base upon which tax must be calculated and remitted. *See Generally* Technical Bulletin TB-27. Similarly, transactions involving non-interest bearing, refundable membership deposits to places of amusement are subject to Vermont sales tax based upon the monetary value of the consideration paid (in the present case, the value of the interest-free use of money over thirty-years or some portion thereof). In such cases, the Department applies a reasonableness standard in examining valuation methodologies employed by taxpayers.

B. Net Present Value Method of Calculating Tax Base for Refundable Deposits

As the Department has ruled that the receipt of Refundable Deposits by the Club constitute transactions subject to the Vermont sales tax, the Club seeks a ruling permitting it to calculate and collect sales tax at the time the Refundable Deposit is made based upon the Deposit's "net present value." For this purpose, the net present value of the Refundable Deposit would be the amount by which such Deposit exceeds the present value of the Club's obligation to make the refund. The Club asks that the present value of the Club's refund obligation be determined using the applicable federal rate for the month in which the Refundable Deposit is received and the period such amount is reasonably expected to remain on deposit. *See generally,* I.R.C. §1274(d). The Club demonstrates the mechanics of the proposed methodology with the following example:

> The present value of a $50,000 Refundable Deposit would be $37,311 assuming an applicable federal interest rate of 5 percent and a 6-year membership period.

> Accordingly, the net present value of the Refundable Deposit would be $12,689 ($50,000 - $37,311). Under the net present value approach, Vermont sales tax would be imposed and collected on that amount which would give rise to a $761 sales tax liability (6 percent of $12,689).

In support of its position, the Club notes that the net present value approach is recognized by the Securities and Exchange Commission as an acceptable method for reporting earnings in connection with refundable membership fees or deposits. *Citing* SEC Staff Accounting Bulletin, No. 101 *Revenue Recognition in Financial Statements* (Dec. 3, 1999). The Club notes that SAB 101 allows the ratable inclusion of refundable membership deposits, net of the present value of the refund obligation, over the anticipated term of the membership if a reliable estimate of the expected refund can be made. As the Club currently has no history by which to determine the typical life of a membership for purposes of estimating expected refunds due its members, the Club proposes employing the average expected life of memberships as determined by one of the largest existing owners of private clubs as the most reliable indicator of the typical period of membership (currently six years for golf and resort memberships and five years for business and sports club memberships). The Department will rely upon the factual representations contained in this paragraph as well as those expressed elsewhere in this ruling in rendering its determination.

The Department acknowledges the potentially unwieldy compliance burden the Club would endure if required to calculate interest accruing on each member's Refundable Deposit throughout the period such Deposits remain outstanding in order to accurately collect and remit tax on a periodic basis. It is, therefore, the determination of the

Department that the Club's use of the proposed "net present value" approach employing (i) the applicable federal rate of interest for the month in which Refundable Deposits are received and (ii) six years as the anticipated term of a membership (until such time as the Club's own experience suggests a more accurate period of time) is a reasonable and acceptable means by which the Club may calculate, collect and remit sales tax on the Refundable Deposits at the time of sale.

This ruling is issued solely to the Club and is limited to the facts presented as affected by current statutes and regulations. Other taxpayers may refer to this ruling to determine the Department's general approach, however, the Department will not be bound by this ruling in the case of any other taxpayer or in the case of any change in the relevant statutes or regulations. 3 V.S.A. §808 provides that this ruling will have the same status as an agency decision or order in a contested case. You have the right to appeal this ruling within thirty (30) days.

Sincerely,

Michael J. Wasser
Policy Analyst

Approved this _____ day of _____ , 2004

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Tom Pelham
Commissioner of Taxes