

New York State Department of Taxation and Finance
Taxpayer Services Division
Technical Services Bureau

TSB-A-92 (66) S
Sales Tax
September 17, 1992

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S920630B

On June 30, 1992, a Petition for Advisory Opinion was received from Costco Wholesale Corporation, 10809 120th Avenue N.E., Kirkland, WA 98083-9777.

The issue raised by Petitioner, Costco Wholesale Corporation, is whether the annual membership fee paid by members for access to its warehouses is subject to New York State and local sales and use taxes.

Petitioner is a Washington corporation that operates a chain of cash and carry membership warehouses in thirteen states and Canada. Petitioner's operations are based on the concept that offering very low prices on a limited selection of national brand products, over a wide range of merchandise categories, will produce rapid inventory turnover and high sales volume. Petitioner sells a variety of merchandise including food, candy, tobacco, sundries, appliances, electronics, tools, office supplies, furniture, automotive supplies, apparel, linens, jewelry, housewares, books, optical, prescription and over-the-counter medicines. Petitioner planned to open its first New York warehouse in Nanuet on June 30, 1992.

Petitioner operates in the membership warehouse segment of specialty retailing. Petitioner's membership format is designed to reinforce customer loyalty and to reduce credit risks. Petitioner has two types of members: business members and individual members. Business memberships are available to owners or managers of a business. A business member may shop for business or personal use. The business membership fee is \$25 annually. The fee includes a free spouse card. Two additional business cards may be obtained under the same membership for an additional \$10 annual fee.

Individual memberships are available to persons from certain eligible groups, such as state and local government employees, civilian federal employees, school and hospital workers, bank employees, public utility employees, and other eligible groups. Individual membership requires payment of a \$30 annual fee and includes a free spouse card.

Upon payment of the annual membership fee Petitioner issues a plastic membership identification card, which grants the member access to any of Petitioner's warehouses in the United States and Canada. Only members who have paid a membership fee and obtained a membership identification card, are allowed access to a warehouse sales facility. All of Petitioner's members, whether business or individual, pay the same posted prices for merchandise sold at Petitioner's warehouses. Payment of the annual membership fee does not entitle a member to any free merchandise nor is the fee used to reduce the purchase price of any subsequent purchase. Members are not required to purchase any specific merchandise nor is there a maximum or minimum purchase requirement. In addition, Petitioner allows a full membership fee refund at any time before the membership's annual renewal date.

Petitioner's stock is traded on the NASDAQ over-the-counter market. Petitioner's Board of Directors is elected by its shareholders. It is not controlled by its membership. Members do not participate in the operation or management of Petitioner. They do not participate in the selection of new members or have a proprietary interest in the Petitioner unless they also happen to be a shareholder.

The following statement appears in the Petitioner's catalog which is given to all new members:

Costco is a membership wholesale distribution center that operates 120,000 square foot warehouses and carries only quality name brands at substantially lower prices than other wholesale sources.

Costco's lower wholesale prices are made possible by eliminating many of the traditional costs inherent in conventional wholesale procedures and by income from a modest annual fee from its members.

This combination makes it possible for you to select from hundreds of quality name brands at dramatically lower prices for business supplies, equipment, merchandise for resale and personal use.

Section 1105(a) of the Tax Law imposes sales tax on the receipts from every retail sale of tangible personal property, except as otherwise provided.

In the Matter of Credit Bureau of Central New York v. State Tax Commission, 105 AD2d 1042 (1984), the court determined that membership fees paid to a credit reporting agency were merely part of the members' cost of the credit reports since the credit reports were the only things provided to members by the credit bureau in return for the fee. The court concluded that such fees are subject to tax since they are, in reality, prepayments which only entitled members to reduced charges for the credit reports.

In Norman Eiger, Adv Op St Tx Comm, December 3, 1985, TSB-A-81(20.1)S the State Tax Commission held that membership fees charged by petitioner which entitled members only to a reduced rental charge on movies and no other rights or benefits, was subject to sales tax since the membership fee represented a prepayment for the rental of the movies.

Technical Services Bureau Memorandum TSB-M-86(8)S, July 7, 1986 states as follows:

This memorandum reflects the policy of the Tax Department on the taxability of video club membership fees.

Video club "memberships" generally enable purchasers to rent movies at rates lower than the rates charged to persons who do not purchase memberships.

Even though vendors of memberships in video clubs characterize the charges as "membership fees", the substance of the charge is the of a prepayment for the rental of a movie. Therefore, the fee for joining is determined to be taxable (section 1105(a) of the Tax Law).

Petitioner charges its members "dramatically lower prices" on the merchandise it sells because of the "income from the modest annual fee from its members" Accordingly, pursuant to Credit Bureau of Central New York v. State Tax Commission, *supra*, Norman Eiger, *supra*, and TSB-M-86(8)S the annual membership fee paid by members for access to its warehouse sales facilities is subject to sales tax pursuant to Section 1105(a) of the Tax Law since in substance, the membership fee is a prepayment for the merchandise sold by Petitioner.

DATED: September 17, 1992

s/PAUL B. COBURN
Deputy Director
Taxpayer Services Division

NOTE: The opinions expressed in Advisory Opinions
are limited to the facts set forth therein.