BEFORE THE IOWA DEPARTMENT OF REVENUE
HOOVER STATE OFFICE BUILDING
DES MOINES, IOWA

IN THE MATTER OF CJ HEALTH INC. D/B/A/ CYCLEBAR JORDAN CREEK SALES AND USE TAX	DECLARATORY ORDER DOCKET NO. 2019-300-2-0291

Pursuant to a Petition for Declaratory Order (hereinafter referred to as "Petition") filed with the Iowa Department of Revenue (hereinafter referred to as "Department") by CycleBar Jordan Creek, and in accordance with Iowa Code section 17A.9 and Iowa Administrative Code rule 701-7.24(17A), "Declaratory order-in general," the Director issues the following order.

I. FACTS

The findings of fact are based on the Petition, further communications with Petitioner, and additional undisputed facts relevant to this Order.

CycleBar Franchising, LLC is an indoor, stationary cycling fitness franchisor of over 400 CycleBar studios in the United States, Canada, and the United Kingdom. Petitioner CJ Health Inc. d/b/a CycleBar Jordan Creek is the franchisee of a CycleBar studio that it operates in West Des Moines, Iowa (hereinafter referred to as "Studio"). The Studio offers instructor-led classes on a membership basis. Customers may also pay for classes by the session. For example, a customer can pay for one class, or buy a pass for five classes. Customers may only use the stationary bikes during instructor-led classes. The Studio also sells retail merchandise.

Classes are designed to give riders a unique exercise experience through a group atmosphere, music, lights, display screens, and instructors' motivational techniques. Classes feature riding to the beat of the music, performing choreographed moves on the stationary bike,

and individual or team races (where results are displayed on a large screen in the room). In addition to providing motivation and a group experience, instructors guide members on proper stationary bike set-up, cycling form, form for core and upper body exercises performed while stationary cycling, and the proper intensity for members of different skill levels. Some of these services are intended to help prevent overuse injuries such as knee pain, lower back pain, Achilles tendonitis, and neck pain.

CycleBar instructors, or "CycleStars," must audition and complete a "boot camp" training before they may instruct CycleBar classes. The audition tests instructors' ability to ride "out of the saddle" at eighty beats per minute, maintain cycling to the beat of the music, cue riders, as well as demonstrate their personality. Candidates may only audition twice.

Once a candidate passes the audition, CycleBar requires prospective instructors to attend a four-day boot camp for eight hours per day, wherein they must do physical conditioning, master a twelve-song instruction sequence, and learn how to teach proper cycling form. This includes learning how to instruct members to cycle to the beat of the music; cue riders on upcoming moves; build a playlist; display rider statistics on a big screen; engage members on social media; act as role models and mentors for members and the community; show members how to properly set up bikes and safely clip and unclip from bikes; lead members in warming up, cooling down, and stretching; inform members on proper form for riding and for core and upper body exercises performed while riding; and guide members to ride at the appropriate intensity for their skill levels. Candidates typically only get one chance to pass the boot camp.

All candidates must be CPR certified and pass the boot camp before they become CycleStars. The Studio offers a chance for further training to become a lead instructor, wherein instructors are flown to Southern California for a three-day training involving more intensive

instruction in industry trends and leadership. A lead instructor can then become a master instructor over several years of commitment to the CycleBar brand. The Studio only offers access to its facilities during classes or individual sessions taught by its instructors; the Studio does not offer any services outside of these scheduled classes, and its members cannot freely use the premises or equipment to exercise absent instruction and supervision.

Studio currently does not collect Iowa sales tax on the sales price of its membership fees, but does collect sales tax on the sale of retail merchandise that it sells.[1]

II. ISSUE PRESENTED

Studio presents one issue for consideration: Whether its Studio's membership fees are subject to Iowa sales tax.

III. STANDARD OF REVIEW

A. Declaratory Orders under the Iowa Administrative Procedure Act

The function of a declaratory order is to provide "reliable advice from an agency as to the applicability of unclear law." Arthur Earl Bonfield, *The Iowa Administrative Procedure Act: Background, Construction, Applicability, Public Access to Agency Law, The Rulemaking Process*, 60 Iowa L. Rev. 731, 805 (1975). Iowa Code section 17A.9 contemplates declaratory orders by administrative agencies on a disclosed set of facts. *City of Des Moines v. P.E.R.B.*, 275 N.W.2d 753, 758 (Iowa 1979). A declaratory order enables the public to secure definitive binding advice as to the applicability of agency-enforced law to a particular set of facts. Bonfield, *supra*, at 822–23.

[1] Iowa imposes sales tax "upon the sales price of all sales of tangible personal property, consisting of goods, wares, or merchandise, sold at retail in the state to consumers or users." Iowa Code § 423.2(1) (2019).

It is not the function of a declaratory order to resolve issues involving factual analysis "too complicated to handle outside of an actual adjudication." *Id.* at 807. A declaratory order is not a "contested case" as defined in Iowa Code section 17A.2(5); namely, it is not an evidentiary hearing, which is a separate administrative remedy set forth in Iowa Code chapter 17A and in the Department's rules. *See* Iowa Admin. Code r. 701—7.24(17A). Consequently, for the purposes of any declaratory order, the Director views the issues raised in the petition as questions of law applicable to future factual situations as disclosed in the petition. This view is consistent with Iowa Administrative Code rule 701—7.24(17A) concerning the issuance of declaratory orders.

B. Statutory Construction and Interpretation of Tax Statutes

"When engaging in statutory interpretation," the Department "first examine[s] the language of the statute and determine[s] whether it is ambiguous." *Kay-Decker v. Iowa State Bd. of Tax Review*, 857 N.W.2d 216, 223 (Iowa 2014) (citing *Rolfe State Bank v. Gunderson*, 794 N.W.2d 561, 564 (Iowa 2011)). "'Generally, we presume words used in a statute have their ordinary and commonly understood meaning.'" *Kay-Decker*, 857 N.W.2d at 223 (quoting *McGill v. Fish*, 790 N.W.2d 113, 119 (Iowa 2010)). "Legislative intent is expressed by what the legislature has said, not what it could or might have said. When a statute's language is clear, we look no further for meaning than its express terms. Intent may be expressed by the omission, as well as the inclusion of statutory terms . . . ." *Hawkeye Land Co. v. Iowa Utilities Bd.*, 847 N.W.2d 199, 210 (Iowa 2014) (quoting *State v. Beach*, 630 N.W.2d 598, 600 (Iowa 2001) (internal citations omitted)).

"The rules of statutory construction and interpretation also govern the construction and interpretation of administrative rules and regulations." *State v. Albrecht*, 657 N.W.2d 474, 479 (Iowa 2003). Agencies have a "reasonable range of informed discretion in the interpretation and

application of their own administrative rules." *Fernandez v. Iowa Dep't of Human Servs.*, 375 N.W.2d 701, 705 (Iowa 1985). Courts afford agencies substantial deference when interpreting their own regulations, "so long as such interpretation is not in violation of the rule's plain language and clear meaning." *Des Moines Area Regional Transit Authority v. Young*, 867 N.W.2d 839, 842 (Iowa 2015).

In addition to applying the general principles of statutory construction, "[s]tatutes which impose taxes are construed liberally in favor of the taxpayer and strictly against the taxing body. It must appear from the language of a statute that the tax assessed against the taxpayer was clearly intended." *Iowa Auto Dealers Ass'n v. Iowa Dep't of Revenue*, 301 N.W.2d 760, 762 (Iowa 1981). However, the Department construes tax exemption statutes narrowly in favor of taxation. *See Dial Corp. v. Iowa Dep't of Revenue*, 634 N.W.2d 643, 646 (Iowa 2001) ("Tax exemption statutes are construed strictly, with all doubts resolved in favor of taxation."); *see also Sherwin-Williams Co. v. Iowa Dep't of Revenue*, 789 N.W.2d 417, 424 (Iowa 2010).

IV. ANALYSIS AND CONCLUSIONS

Iowa imposes sales tax on the sales price of "all commercial recreation." Iowa Code § 423.2(6)(v) (2019). The Department's long-standing administrative rules define "recreation" to include "all activities pursued for pleasure, including sports, games and activities which promote physical fitness," excluding tickets to admission separately taxable elsewhere in Iowa Code section 423.2. Iowa Admin. Code r. 701-26.24.

Rule 701-26.24, however, distinguishes between "commercial recreation" and "instruction in recreational activities": "If a person provides both facilities for recreation and instruction in recreational activities, charges for instruction in the recreational activities shall not be subject to tax" if the instruction meets the following conditions:

1. The instruction charges are contracted for separately, separately billed, and reasonable in amount when compared to the taxable charges of providing facilities for recreation. . . .

2. The persons receiving the instruction must be under the guidance and direction of a person training them in how to perform the recreational activity. If the persons receiving what purports to be "instruction" are allowed any substantial amount of time to pursue recreational activities, no instruction is taking place. The instruction should be received in what would ordinarily be thought of as a "class" with a fixed time and place for meeting. . . .

3. The "instruction" must impart to the learner a level of knowledge or skill in the recreational activity which would not be known to the ordinary person engaging in the recreational activity without instruction. Also, the person providing the instruction must have received some special training in the recreational activity taught if charges for that person's instruction are to be exempt from tax.

Iowa Admin. Code r. 701-26.24. Stated differently, a service that actually constitutes "instruction" that meets all of the above criteria is excluded from the definition of taxable "recreational activities" and is not subject to Iowa sales tax.

The Studio's classes are taxable commercial recreation. The Studio's classes do not satisfy the level of instruction necessary to make the classes not taxable. Furthermore, any amount of instruction featured in a class is incidental to the predominant service, which is taxable commercial recreation.

The Department has long interpreted the sales tax on "all commercial recreation," and regulations promulgated under this statute, to apply to sales of gym memberships, workout classes, and non-specialized instructor-led workout sessions. *See* Memorandum on Aerobic Exercise Classes (Sept. 24, 1984)[2]; Policy Letter RE: Sales Subject to Tax (April 1, 1994)[3];

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[2] Available at: http://itrl.idr.iowa.gov/Browse/OpenFile/5096%7CFlockhart%7CAll%7C%7CAll (finding that instructor-led aerobics dance classes, which involved "simple movements done to music to stretch and tone the body, improve the heart and lungs and lose weight" were taxable commercial recreation, in contrast to formal dance classes in tap, ballet, jazz, or break dancing).

[3] Available at:http://itrl.idr.iowa.gov/Browse/OpenFile/4677%7CSales%20Subject%20to%20Tax%7CExact%7C%7CAll (finding "private, individual, exercise training sessions" to be taxable commercial recreation);

Policy Letter RE: Curves Franchise and Sales/Use Tax (Feb. 24, 2004)[4]; Policy Letter RE: Commercial Recreation (April 24, 2000)[5]. These long-standing Department interpretations of the statute and rule on "commercial recreation" support the Department's conclusion that the Studio's services are taxable. *See, e.g., City of Marion v. Iowa Dep't of Rev. and Finance*, 643 N.W.2d 205, 207-08 (Iowa 2002).

The Studio highlights several factors to support its request for the Director to find the classes to be exempt instruction, instead of taxable commercial recreation. The Studio points to what it terms as CycleBar's required "rigorous certification training." The Studio also states that "CycleBar Premium Indoor Cycling is NOT a skill possessed or understood without instruction." Petition for Declaratory Order at p. 2 (emphasis in original). The Director disagrees. These factors do not make the classes non-taxable, for at least two reasons.

First, the classes do not meet the requirements of nontaxable "instruction in commercial recreation." No instructional element "impart[s] to the learner a level of knowledge or skill in the recreational activity which would not be known to the ordinary person engaging in the recreational activity without instruction." *See* Iowa Admin. Code r. 701-26.24(3). Ordinary people know, without instruction, how to ride a stationary exercise bike, when a bike seat or handles need adjusting, how to clip and unclip from the pedals, when they are exceeding their physical limits, and understand warming up and cooling down. In fact, CycleBar describes the complexity of the exercise experience for novices very differently than the Studio described it in

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[4] Available at: http://itrl.idr.iowa.gov/Browse/OpenFile/3552%7CCurves%7CExact%7C%7CAll (finding initiation and introductory fees and monthly dues to be taxable commercial recreation because providing "initial instruction on the machines used at Curves and the subsequent monitoring, occasional instruction, and encouragement" did not qualify as "instruction" under Rule 701-26.24).

[5] Available at: http://itrl.idr.iowa.gov/Browse/OpenFile/3908%7CCommercial%20Recreation%7CExact%7CCommercial%20Recreation%7CAll (finding a registration fee and an annual fee for a fitness center that featured "instructor-led interval training, regular aerobics, and step aerobics" to be taxable commercial recreation).

the petition. CycleBar informs prospective customers that "[s]igning up and jumping on a bike is a quick and easy process. Best of all, anyone can do it!" *New Riders*, CycleBar, https://www.cyclebar.com/new-riders (last visited July 29, 2019).

Second, any amount of instruction is incidental to the true object of the class, which is taxable commercial recreation. *See In re Soccer and Sports Center L.C.*, Dep't of Revenue Declaratory Order, Docket No. 97-30-6-0153 (1997) (holding the essence of renting of a sports arena for practicing and playing a sport constituted commercial recreation, not a non-taxable real estate rental); *In re Soccer and Sports Center L.C.*, Dep't of Revenue Declaratory Order, Docket No. 97-30-6-0154 (1997) (holding the rental of batting cages constituted taxable commercial recreation, not a non-taxable real estate rental, because "the true item" rented was commercial recreation); *accord* Policy Letter Re: Taxability of the Sale of Certain Services (Aug. 14, 2012)[6]. The overwhelming predominant feature of the class is the entertaining group-exercise experience, motivational class leaders, lights, music, big-screen display, and competitions. Even assuming some portion of a class can feature guidance from instructors that constituted "instruction" of the type described in Rule 701-26.24, the classes remain taxable. *See In re Sundown Mountain*, Dep't of Revenue Declaratory Order, Docket No. 99-30-6-0079 (June 4, 1999) (holding the movement of customers by ski lifts was an integral part of the service of skiing, which was taxable commercial recreation, and rejecting the argument that the ski lift constituted exempt personal transportation); *see also* Policy Letter Re: Sales Subject to Tax (April 1, 1994) (available at footnote 3) (finding a service to be taxable commercial recreation where the service featured a limited number of private, individual, exercise training sessions and meal planning, because the "predominant service" was the exercise sessions which were

commercial recreation). Preliminary, brief, and basic instructions on stationary bicycling form, setting up stationary bicycles, or warming up and cooling down does not transform the entire class into an exempt instructional service of the level described in the Department's rules. A CycleBar class constitutes the sale of single, indistinguishable service that is commercial recreation. *See* Iowa Code § 423.2(8)(a) (2019). Alternatively, even if a CycleBar class constituted the sale of taxable commercial recreation and exempt instruction under Rule 701-26.24 for one non-itemized price, any instruction would be incidental to the true object of the commercial recreation. *See* Iowa Code § 423.2(8)(d)(2) (2019). Either way, CycleBar classes are simply the sale of a single service that is taxable commercial recreation. *See, e.g., In re Sundown Mountain*, Dep't of Revenue Declaratory Order, Docket No. 99-30-6-0079 (June 4, 1999) (finding the sale of a ski ticket and lift ticket to be a single taxable service that was commercial recreation and rejecting the petitioner's request to find the ski lift charge to be exempt personal transportation).

This case is distinguishable from the Pilates instruction described in *The Tice Group, Inc.*, Dep't of Revenue, Declaratory Order Docket No. 2019-300-2-0020 (Feb. 13, 2019). The declaratory order in *Tice* described a specialized exercise regime that would not be known to an ordinary person absent the instruction. *Id.* The Pilates in *Tice* was provided in various levels of courses, that required customers to pursue months of training in order to progress through higher course levels. *Id.* Overall, the instruction provided to customers in *Tice* was more similar to other instruction the Department has found to be exempt instruction. *See* Letter of Findings,

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[6] Available at: http://itrl.idr.iowa.gov/Browse/OpenFile/5148%7CTaxability%20of%20Certain%20Services%7CExact%7CCommercial%20Recreation%7CAll.

Kim's Nautilus Gym Centers, Inc. (1984)[7]; Policy Letter re Sales Tax on Tennis Lessons (1992)[8]. CycleBar classes are not stationary bicycle instruction lessons. Instead, CycleBar classes are more similar to recreation activity the Department has found taxable, even though it involves basic initial in-person instruction and ongoing, in-person oversight and motivation. *See* Policy Letter RE: Curves Franchise and Sales/Use Tax, Doc. Ref. 04300030 (Feb. 24, 2004) (available at footnote 4) ("[I]nitial instruction on the machines used at 'Curves' and the subsequent monitoring, occasional instruction, and encouragement [we]re not sufficient to constitute 'instruction.'").

The instructors in *Tice* were also required to complete over 10 times more training hours in a specialized exercise regime than the hours required to be an CycleStar instructor (in a more generalized exercise regime). In addition to the discrepancy in the hours of training, the training to become a Pilates instructor in *Tice* differed qualitatively from the training in this case. Instructors in Tice's Pilates Studio were required to have extensive training in Pilates instruction before they were permitted to engage in in-studio apprentice training, including completion of Club Pilates' 450-plus-hour certification program. CycleStar's 32-hour boot camp training covered matters such as stationary-cycling form and proper weight-training form. But it also included topics such as "finding you instructor voice for motivation, mentoring system, community engagement, playlist building, branded 12-song sequence and how to execute that sequence, how to cue riders on upcoming moves, strategy on increasing class size, motivating riders, social media engagement, system training (electronics training, software training,

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[7] Available at:
http://itrl.idr.iowa.gov/Browse/OpenFile/5113%7CNautilus%7CExact%7CCommercial%20Recreation%7CAll
(finding fees paid exclusively for Tae Kwon-do instruction to be not taxable).

[8] Available at:
http://itrl.idr.iowa.gov/Browse/OpenFile/4486%7Ctennis%20lessons%7CExact%7CCommercial%20Recreation%7CAll (finding private tennis lessons to be exempt instruction).

displaying races and race statistics on the big screen TV in the workout theater), and sending playlists to customers." These portions of CycleStar's training are consistent with the Director's characterization of the classes as commercial recreation.*Id.* at 6.

The Director concludes that the indoor, stationary cycling classes sold by the Studio are taxable commercial recreation. Therefore, Studio must collect sales tax on sales of the indoor cycling services offered at its West Des Moines Studio.

ORDER

THEREFORE, based on the facts presented, foregoing reasoning, and applicable provisions of the law, the Director finds that the services offered by Studio at its Studio constitute taxable commercial recreation and are therefore subject to Iowa sales tax.

Issued at Des Moines, Iowa this 26th day of September, 2019.

IOWA DEPARTMENT OF REVENUE

By _____
Kraig Paulsen, Director

CERTIFICATE OF SERVICE

I certify that on this 26th day of September, 2019, I caused a true and correct copy of the Declaratory Order of the Director of Revenue to be forwarded by U.S. Mail to the following person:

Jeff Hodges
160 Jordan Creek Parkway, Suite 130
West Des Moines, Iowa 50266

Hollie Welch

Hollie Welch, Executive Secretary