STATE OF NEW MEXICO
ADMINISTRATIVE HEARINGS OFFICE
TAX ADMINISTRATION ACT

IN THE MATTER OF THE PROTEST OF
ASPEN MANAGEMENT COMPANY INC.
TO ASSESSMENT ISSUED UNDER
LETTER ID NO. L0899948336

v. **Case Number 18.12-326A, D&O #23-15**

NEW MEXICO TAXATION AND REVENUE DEPARTMENT

DECISION AND ORDER

On July 24, 2023, Hearing Officer Chris Romero, Esq., of the Administrative Hearings Office conducted an administrative hearing on the merits of the tax protest of Aspen Management Company, Inc. (hereinafter "Aspen" or "Taxpayer") pursuant to the Tax Administration Act and the Administrative Hearings Office Act. The hearing was conducted in person. The record closed on August 23, 2023.

The Administrative Hearings Office is an independent agency tasked with the fair and impartial adjudication of protests under the Tax Administration Act. As explained by Regulation 22.600.1.20 C NMAC, the Hearing Officer is not "responsible to or subject to the direction of any officer, employee or agent of the taxation and revenue department[.]" *See e.g.* Regulation 22.600.1 NMAC (2018)

Mr. Lewis J. Terr, Esq. appeared in person for Aspen along with Mr. Erik Briones. Staff Attorney, Mr. Richard Pener, Esq., appeared in person representing the opposing party in the protest, the Taxation and Revenue Department ("Department"), and was accompanied by Ms. Mary Griego, protest auditor.

Mr. Briones testified for the Taxpayer. Ms. Griego and Ms. Veronica Galewaler testified for the Department. The exhibits in this matter exceed 1,000 pages. Taxpayer Exhibit 1 and

Department Exhibits A – AAAA and CCCC – IIII were admitted without objection upon stipulation of the parties. Department Exhibit BBBB was admitted over Taxpayer's objection.[1]

According to the evidence, which will be subsequently discussed in more detail, Aspen is a for-profit corporation established to assist the operations of a non-profit licensed cannabis producer[2] (hereinafter "Producer"). The Producer is licensed by the New Mexico Department of Health under the Lynn and Erin Compassionate Use Act ("CUA"). Aspen argues that as a result of the limitations placed on the licensure and operation of licensed cannabis producers in New Mexico under the CUA and the implementing regulations of the New Mexico Department of Health, Aspen was established "as a separate for-profit entity to perform functions that would have been performed by [the Producer] itself if it had been allowed to organize as a for-profit corporation[.]" *See* Taxpayer's Closing Argument, Page 2.

Given this brief background, Aspen's main arguments for abatement of the assessment are that: (1) Aspen and the Producer are "in substance, one self-managed company with no need to pay management fees, and a consolidated financial statement would designate as dividends or wages (both deductible from gross receipts) the transfers to Aspen designated as management fees[;]" and (2) "Aspen is an affiliate of [the Producer] providing management services to [the Producer] at cost and entitled to the deduction provided for in [NMSA, 1978 Section] 7-9-69[.]"

As explained in greater detail in the subsequent discussion, the Hearing Officer finds based on the evidence and arguments presented that Aspen's protest should be DENIED for the

[1] A comprehensive examination of all exhibits after the hearing revealed the prospect that discrete portions of Department Ex. BBBB (consisting of 242 pages) included attorney-client communications on the subject of the relevant audit. *See* Department Ex. BBBB-169 – BBBB-184. This was not the basis of Aspen's objection. In any event, the communications to which this observation applies have apparently been previously disclosed in the First Judicial District Court for Santa Fe County in D-0101-CV-2018-01560.

[2] The identity of the Producer is contained in the record but will not be disclosed in this publicly available Decision and Order out of an abundance of caution for the confidentiality of taxpayer information including returns and other potentially confidential information under NMSA 1978, Section 7-1-8 (2017).

reasons stated. IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

The Assessment

1. On July 19, 2018, the Department issued a Notice of Assessment and Demand for Payment of Taxes under Letter ID No. L0899948336 to Aspen in the total amount of $414,473.18 which consisted of $320,359.17 in gross receipts tax principal, $62,957.91 in penalty, and $31,156.10 in interest ("Assessment"). [Department Ex. A; Administrative File]

2. The Assessment derived from an audit in which the Department computed an "Under Reported Gross Receipts Exception" in the amount of $4,469,697.08 in the reporting period from June 30, 2013 through December 31, 2017. [Department Ex. B-001; Department C-003]

Mr. Briones' Background

3. Mr. Erik Briones is the president and CEO of the Producer and Taxpayer. He resides in Tesuque, New Mexico. [Direct Examination of Mr. Briones]

4. Mr. Briones grew up in Santa Fe, New Mexico. He has a horticulture degree from New Mexico State University and a landscape architecture degree from Oregon State University. [Direct Examination of Mr. Briones]

5. Mr. Briones began his first business during his junior year of high school. He and a friend dug up pinon trees in Rowe Mesa and sold them to interested buyers. That evolved into a landscaping business that "put [him] through college." [Direct Examination of Mr. Briones]

6. After college, Mr. Briones taught horticulture for three years at Cibola High School in Albuquerque, New Mexico while also operating his landscaping business on the side. [Direct Examination of Mr. Briones]

7. Mr. Briones' landscaping business eventually morphed into ownership of Rio Rancho Garden Center in Rio Rancho, New Mexico which he operated for 13 years. [Direct Examination of Mr. Briones]

8. During the Great Recession of 2008 and 2009, Mr. Briones observed that "nobody needed a nursery." Mr. Briones closed the business in 2009. [Direct Examination of Mr. Briones]

The Producer

9. In 2009, Mr. Briones began to explore the possibility of business in the new area of medical cannabis which had been decriminalized under the CUA. [Direct Examination of Mr. Briones]

10. At the time, uncertainties regarding business in medical cannabis, particularly how it was viewed under federal law were concerning and unknown. [Direct Examination of Mr. Briones]

11. Around the same period of time, an acquaintance contacted Mr. Briones about serving on the board of an entity which was similarly contemplating engaging in the business of producing medical cannabis. It required the experience of a horticulturalist on its board, which Mr. Briones agreed to fill. [Direct Examination of Mr. Briones]

12. Mr. Briones also decided to pursue the possibility of obtaining his own producer license and for six months, dedicated his time to researching and preparing an application for a license. [Direct Examination of Mr. Briones]

13. Mr. Briones incorporated the Producer. The initial Certificate of Incorporation was issued on December 14, 2009. [Cross Examination of Mr. Briones; Department Ex. G-002]

14. In December of 2010, the Producer's license was approved and Mr. Briones has been engaged in the business of producing and selling medical cannabis ever since. [Direct

Examination of Mr. Briones]

15. At all relevant times, the Producer was incorporated as a New Mexico domestic non-profit corporation as required by the New Mexico Department of Health. [Direct Examination of Mr. Briones; Department Ex. D-019; E-003 (No. 2)]

16. In response to Aspen's request to inspect public records, the Department of Health provided documents suggesting that one of its considerations during the promulgation process was the objective that, "Medical cannabis must be affordable to those in need." [Taxpayer Ex. 1-014, Para. 8]

17. In response to Aspen's request to inspect public records, the Department of Health provided documents suggesting that one of its considerations during the promulgation process was the opinion that, "In order to ensure that distributors are not accused of profiteering, it is recommended that dispensaries ensure transparency, openness, financial accountability, and mechanisms for client feedback. Non-profit incorporation is one way of meeting these criteria." [Taxpayer Ex. 1-018, Para. 1]

18. Producer's Articles of Incorporation were prepared by an attorney. [Cross Examination of Mr. Briones]

19. Article Three of the Producer's Articles of Incorporation, among other terms, specified:

> No part of the net earnings of the corporations [sic] shall inure to the benefit of, or be distributable to members, trustees, officers, or other private persons, except that the corporation shall be authorized and empowered to pay reasonable compensation for services rendered and to make payments and distributions in furtherance of the purposes set forth in Article Three hereof. No substantial part of the activities of the corporation shall be the carrying on of propaganda, of otherwise attempting to influence legislation, and the corporation shall not participate in, or intervene in (including the publishing or distribution of statements) any

> political campaign on behalf of or in opposition to any candidate for public office. Notwithstanding any other provision of these Articles, the corporation shall not carry on any other activities not permitted to be carried on (a) by a corporation exempt form [sic] federal income tax under Section 501(c) (3) of the Internal Revenue Code, or (b) by a corporation, contributions to which are deductible under Section 170(c)(2) of the Internal Revenue Code, or corresponding section of any future tax code.
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> [Department Ex. G-003 – G-004]

20. In Response to Requests for Admission, Aspen admitted that the Producer was "technically registered with the Secretary of State as a nonprofit corporation as required by rules of the New Mexico Department of Health." But it went on to explain that "[t]he nonprofit status is a legal fiction, as [the Producer], is not treated as a nonprofit corporation by the New Mexico Taxation and Revenue Department or any other agency of the state or the federal government." [Department Ex. 003 (No. 2)]

21. The nonprofit corporation under which the Producer engages in business does not have, nor has it ever had, shareholders or equity owners. [Direct Examination of Mr. Briones; Department Ex. E-003 (No. 3); Department Ex. E-008 (No. 6) ("[The Producer] is technically a nonprofit corporation, it is precluded by law from having equity owners, and therefore it has no shareholders."]

22. The Producer is not, nor has it ever been a corporation exempt from federal income tax under Section 501(c) (3) of the Internal Revenue Code. [Re-Direct Examination of Mr. Briones; Department Ex. E-003]

23. Mr. Briones recalled the Producer incurring a startup cost of approximately $100,000, but it may have been closer to $130,000. [Direct Examination of Mr. Briones; Cross Examination of Mr. Briones]

24. The Producer's initial license permitted for the cultivation of 90 plants for a fee of

$90,000 per year. [Direct Examination of Mr. Briones]

25. Startup costs included acquisition of a facility as well as modifying the facility for the purpose of producing medical cannabis. [Direct Examination of Mr. Briones]

26. Mr. Briones raised the startup funds by acquiring investments or loans from family and acquaintances with Mr. Briones making the majority investment or loan. [Direct Examination of Mr. Briones; Cross Examination of Mr. Briones]

27. Despite federal income tax return filings that might suggest the loans were paid off, Mr. Briones explained his belief that the loans remained outstanding, and that his CPA would be best situated to explain the significance of any federal filings. [Cross Examination of Mr. Briones]

28. Mr. Briones has always been the Producer's majority investor. [Direct Examination of Mr. Briones]

29. The Producer's first harvest was in June or July of 2011. [Direct Examination of Mr. Briones]

30. The Producer's business has expanded naturally without further investment, meaning there has never been a subsequent need to seek additional investment in that the Producer's business activities have been self-sustaining and self-funding. [Direct Examination of Mr. Briones]

31. The Producer also reinvested revenue as it deemed necessary to satisfy its business goals of becoming or maintaining its status as "one of the top companies in New Mexico within the restraints we were operating." [Re-Direct Examination of Mr. Briones]

Aspen Management Company

32. In 2013, Mr. Briones started Aspen management seeking a "legal way to

distribute dividends." Mr. Briones described establishing Aspen to "distribute dividends because you cannot distribute a dividend in a non-profit, and nobody owns any kind of equipment, there is no equity stake in a non-profit." [Direct Examination of Mr. Briones; Department Ex. G-003 – G-004 ("No part of the net earnings of the corporations [sic] shall inure to the benefit of, or be distributable to members, trustees, officers, or other private persons[…]")]

33. Aspen was also established to acquire services that Producer was not able to acquire for itself, including banking services, credit card processing services, and payroll processing services, because providers of such services refused to provide services for a business engaged in an activity that was prohibited under federal law. [Direct Examination of Mr. Briones]

34. For example, prior to the establishment of Aspen, the Producer was banned by several banking institutions (approximately nine). At the time, Mr. Briones observed that banks did not initially inquire regarding the nature of the Producer's business, but once it became known to the institution that the Producer was engaging in the business of producing medical cannabis, the bank would "shut [the Producer] down." [Cross Examination of Mr. Briones]

35. Aspen was incorporated on May 3, 2013 as a for-profit corporation. "The purpose of forming the Corporation [was] for all lawful purposes permitted under the laws of the State of New Mexico, including but not limited to, acquiring and investing in real and personal property and other related assets and providing administrative and operational services to other business entities and all matters ancillary thereto." [Department Ex. E-119; F-003]

36. Aspen was the entity that allowed the Producer to exist as a normal business, and which enabled the Producer to avoid operating as a cash-only endeavor. It was able to acquire bank accounts, payroll services, credit card processing services, enter into leases and perform

other business activities that had been difficult for the Producer in its area of business. [Direct Examination of Mr. Briones]

37. In contrast to previous experience, when Aspen assumed the responsibility of establishing bank accounts, it only disclosed that it was a "management" company. It never disclosed it was a management company for an entity engaged in producing cannabis or that banking services concerned revenue derived by Producer because "they (the banks) never asked." [Cross Examination of Mr. Briones]

38. The Producer and Aspen were parties to a "zero sum" management agreement in which Aspen did not assertedly charge fees to the Producer. [Direct Examination of Mr. Briones; Department Ex. E-053]

39. The management agreement provides that, "Aspen is an independent contractor. Nothing herein shall be deemed to be an employment, partnership, joint venture or other similar relationship between [the Producer] and Aspen. Aspen shall be responsible for all income and other taxes, fees and expenses imposed directly or indirectly for its services pursuant to this Agreement and all compensation received hereunder. Aspen is responsible for all licensing required to provide the services contemplated under this Agreement." [Department Ex. E-053 – E-054 (Para. 3.1)]

40. Despite Mr. Briones' denial that Aspen received any fees for its services, Aspen previously described its relationship with the Producer as follows:

> Because Aspen and [the Producer] operate functionally as one company, Aspen Management, Inc. did not receive funds from [the Producer] in the same way as would a service-providing company that was unrelated to [the Producer]. Aspen has at all times been primarily responsible for paying expenses incurred by [the Producer], and it pays those expenses with funds derived from sales by [the Producer]. Therefore, fund "transfers" from [the Producer] to Aspen are not properly classified as "payments" to

> Aspen. Aside from monies "received" by Aspen to pay expenses of [the Producer], *payments by [the Producer] to Aspen are for managerial and accounting services provided by Aspen* and are *based upon Aspen's cost of providing such services. Aspen's costs consist of the salaries of the employees of Aspen and a return to Aspen's equity owners for the money they provided to start [the Producer]*.
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> [Department Ex. E-010 (Answer to Int. No. 10 (Emphasis Added); Department E-0176]

41. Mr. Briones explained, "the management agreement was the documentation of the vehicle to put in place the illusion that Aspen was a management company overseeing the operations of [the Producer]." He denied that the management agreement was a "sham" but acknowledged it was a necessary aspect of engaging in the business of producing cannabis. [Direct Examination of Mr. Briones; Cross Examination of Mr. Briones; Department Ex. E-053]

42. Mr. Briones explained his perception that the non-profit Producer and for-profit Aspen were always one business. "[The Producer] would technically make the money, but then all the money would get shifted to Aspen to make payroll, pay bills, because Aspen had the bank account." [Direct Examination of Mr. Briones]

43. All receipts, except for cash consumed by the Producer for business expenses, was transferred to Aspen. [Direct Examination of Mr. Briones]

44. Transfers from the Producer to Aspen occurred on a daily basis. [Direct Examination of Mr. Briones]

Relationships Among the Producer, Aspen, and the Investors

45. At no relevant time has Aspen provided services for any other entities, except the Producer. [Department Ex. E-012 (No. 12)]

46. Although Aspen is a separate and distinct entity from the Producer, Mr. Briones emphasized that the non-profit corporation and the for-profit corporation operated in unison.

[Department Exs. H; D-017; Cross Examination of Mr. Briones]

47. Despite the views of the Producer or Aspen that their structures and relationship were required by law, and that Mr. Briones had no other choice about how to structure his businesses, other similarly situated businesses have employed other strategies for their operation. [Department Ex. BBBB-044 – BBBB-046]

48. At no relevant time during the audit period did Aspen have an equity ownership in the Producer that: (a) represented at least 50 percent of the total voting power of the Producer; (2) that had a value equal to at least 50 percent of the total equity of the Producer. [Department Ex. E-004; Nos. 5 - 6)]

49. At no relevant time during the audit period did the Producer have an equity ownership in Aspen that: (a) represented at least 50 percent of the total voting power of Aspen; (2) that had a value equal to at least 50 percent of the total equity of Aspen. [Department Ex. E-004; Nos. 7 – 8)]

50. At no relevant time during the audit were Aspen and the Producer under the common control of another business entity that had and equity ownership: (1) in both entities that represented at least 50 percent of the total voting power of Aspen and 50 percent of the total voting power of the Producer; (2) in both entities that had a value equal to at least 50 percent of the total equity of Aspen and 50 percent of the total equity of the Producer. [Department Ex. E-005; No. 9 – 10)]

51. Aspen acknowledges its relationship with the Producer precludes it from complying "with the ownership requirement of [Section 7-9-69] and regulation notwithstanding the degree of mutual control or any other factors showing the two companies are inextricably intertwined." [Department Ex. E-013 – E-014 (No. 16)]

52. Certain limitations placed on Producer as a non-profit were undesirable. For example, it was prohibited from paying dividends to "satisfy the investors." [Direct Examination of Mr. Briones]

53. Because Producer was not permitted to distribute profits in any form, it transferred a portion of its net earnings to Aspen so that Aspen could distribute the Producer's profit to private individuals who invested in establishing the Producer. [Direct Examination of Mr. Briones; Cross Examination of Mr. Briones]

54. The total shareholder distributions were intended to provide a reasonable return on investment. Typical investors want a maximum return on their investment. [Cross Examination of Mr. Briones]

55. Despite the occasional reference to "shareholders" or "equity," as a non-profit, the Producer neither had shareholders nor equity. [Cross Examination of Mr. Briones]

56. Total shareholder distributions to the Producer's investors paid by Aspen from 2013 through 2017 totaled approximately $2,488,594 to Mr. Briones and other individuals. [Department Exs. AA – FF; Cross Examination of Mr. Briones]

57. Mr. Briones' personal return on investment paid by Aspen during the audit period was approximately $1,529,035 or a return of 129,479 percent. Investment returns to other contributing individuals ranged from 207 percent to 113,872 percent. [Cross Examination of Mr. Briones; Department Ex. IIII]

58. Decreasing the return of money paid to investors would not lower the price paid by patients in need of medical cannabis. [Cross Examination of Mr. Briones]

59. Despite previous statements that "payments by [the Producer] to Aspen are for managerial and accounting services provided by Aspen and are based upon Aspen's cost of

providing such services[,]" Mr. Briones explained there was never an actual cost for the services Aspen provided. For that reason, neither Aspen nor the Producer ever performed a cost analysis of the services Aspen provided to the Producer. [Cross Examination of Mr. Briones; Department Ex. E-010 (Answer to Int. No. 10); Department E-0176]

60. Even though Mr. Briones explained there were no costs associated with the services Aspen provided, it previously explained that "Aspen's costs consist of the salaries of the employees of Aspen and a return to Aspen's equity owners for the money they provided to start [the Producer]." [Cross Examination of Mr. Briones; Department Ex. E-010 (Answer to Int. No. 10); Department E-0176]

61. There is no satisfactory evidence in the record to establish for the purposes of the deduction provided by Section 7-9-69, that Aspen provided managerial or administrative services "at cost." [Cross Examination of Ms. Griego]

Aspen's Bookkeeping, Tax Reporting Methods, and Reporting History

62. Between 2013 and 2017, Aspen recorded income from "management fees" in the amount of $4,850,070.34 on its Profit & Loss statements, although Mr. Briones rejected the accuracy of their characterization as "management fees." [Department Exs. NN – RR; E-082 – 118; Cross Examination of Mr. Briones]

Tax Year	Aspen P&L	Exhibit
2013	$312,000.00	NN-001
2014	$813,076.00	OO-001
2015	$1,685,147.00	PP-001
2016	$575,322.00	QQ-001
2017	$1,464,525.34	RR-001
Total	**$4,850,070.34**	

63. Between 2013 and 2017, Aspen's Income Tax Return for an S Corporation (Form 1120-S (Line 1a)) reported total income of $4,845,796.00 from gross receipts or sales although

Mr. Briones disagreed that the reported income should be characterized as "gross receipts or sales." [Cross Examination of Mr. Briones; Department Exs. VVV – ZZZ]

64. The Producer's Forms 1125-A in tax years 2013 through 2016 reported amounts paid for managerial services which correspond closely to the amounts Aspen reported receiving as gross receipts or sales on its Forms 1120-S (Line 1a) in the same periods. Tax year 2017 is excluded from comparison because the Producer's Form 1125-A is not contained in the record for that year.

Tax Year	Aspen Form 1120-S (1a)	Exhibit	Form 1125-A – Line 5	Exhibit
2013	$312,000.00	VVV-003	$312,000.00	D-010
2014	$813,076.00	WWW-003	$797,834.00	D-008
2015	$1,683,647.00	XXX-001	$1,672,247.00	D-006
2016	$1,023,322.00	YYY-001	$1,009,298.00	D-004
2017	$1,013,751.00	ZZZ-001	Unavailable	
Total	**$4,845,796.00**		**$3,791,379.00**	

65. Producer, although incorporated as a non-profit under state law, has never been tax-exempt under federal law due to the federal government's treatment of cannabis. [Direct Examination of Mr. Briones]

66. The Producer and Aspen filed federal income tax returns with the assistance of a certified public accountant (CPA). [Direct Examination of Mr. Briones]

67. Mr. Briones has no knowledge or understanding of why the CPA for the Producer and Aspen reported income to Aspen when, according to Mr. Briones, Aspen did not generate revenue. He elaborated that "how the [CPA] dealt with the tax returns is really a better question for him[3] than for me." [Direct Examination of Mr. Briones]

68. Taxpayers submitting Form 1120 are required to declare under penalty of perjury,

[3] Although Mr. Briones deferred to the expertise of Aspen's CPA, Aspen did not call its CPA to testify at the hearing, nor was Aspen's CPA identified as a potential witness in any prehearing statement or other notice filed with the Administrative Hearings Office.

that they have "examined [the] return, including accompanying schedules and statements, and to the best of [their] knowledge and belief, it is true, correct, and complete." It goes on to provide, "[d]eclaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge." [Department Ex. D-003; D-005; D-007; D-013]

69. The Producer reported New Mexico gross receipts and paid the resulting tax due through an employee bookkeeper. [Direct Examination of Mr. Briones]

70. Aspen's CRS-1 filings in the relevant reporting periods never reported gross receipts because Mr. Briones did not perceive Aspen as generating any taxable receipts. He elaborated, "[Aspen] shouldn't have to pay gross receipts tax on zero income." [Direct Examination of Ms. Griego; Department Exs. SS – UUU (Line 2 of CRS-1 Long Forms); Department Ex. E-005 (No. 11); Direct Examination of Mr. Briones]

71. The Department processed Aspen's tax returns consistent with the information reported therein, including its payment of franchise tax. [Direct Examination of Ms. Galewaler; Cross Examination of Ms. Galewaler; Re-Direct Examination of Ms. Galewaler]

The Audit and the Department's Conclusions

72. Ms. Veronica Galewaler is a Corporate Income Tax supervisor employed by the Department. She has been with the Department for about 16 years. In that capacity, she regularly reviews the work product of her subordinates. [Direct Examination of Ms. Galewaler]

73. Ms. Galewaler reviewed the work product that generated the Assessment and perceived no substantive errors. [Direct Examination of Ms. Galewaler]

74. A non-profit corporation is taxed in a similar manner to a for-profit corporation unless the corporation receives tax exempt status under the Internal Revenue Code as determined by the Internal Revenue Service. [Direct Examination of Ms. Galewaler]

75. The terms "non-profit" and "tax exempt" are not analogous. A non-profit is not perceived as tax-exempt without a determination from the Internal Revenue Code. Absent tax-exempt status as determined by the Internal Revenue Service, a non-profit corporation is liable for New Mexico income tax and franchise tax in similar manner to a for-profit corporation. [Direct Examination of Ms. Galewaler; Cross Examination of Ms. Galewaler]

76. Mary Griego is a tax auditor with the Department. [Direct Examination of Ms. Griego]

77. The audit narrative and its accompanying work papers reveal no defects in the audit that affect the Assessment. [Direct Examination of Ms. Griego; Department Exs. B – C]

78. Despite some inartful terminology in the narrative which tended to conflate the terms "non-profit" and "tax-exempt," there are no material defects in the audit or its conclusions. [Direct Examination of Ms. Griego; Department Exs. B – C]

79. Aspen reported and paid corporate income tax on those amounts that it reported as gross receipts on its Forms 1120 [Direct Examination of Ms. Griego; Department Exs. VVV-003; WWW-003; XXX-001; YYY-001; ZZZ-001 (Lines 1a)]

80. Aspen's payment of a franchise fee was correct because the only exception available is for tax exempt corporations as certified by the Internal Revenue Service. [Direct Examination of Ms. Griego; Re-Direct Examination of Ms. Griego]

81. To the extent Aspen failed to provide documents requested by the Department during the audit, Mr. Briones attributes the failure to a former employee who he characterized as a "disaster." Mr. Briones expressed his belief that all requested documents were provided. [Direct Examination of Mr. Briones]

Procedural History of the Protest

82. Aspen executed a formal written protest of the Assessment on October 15, 2018 which was filed in the Department's Protest Office on October 22, 2018. [Administrative File (attachment to Hearing Request filed December 20, 2018)]

83. Taxpayer's formal protest, in part, claimed, "[N]ot all transfers of money from [the Producer] to Aspen are 'gross receipts' as defined by statute. While some are for management services rendered, some are transfers to Aspen as an agent for obligations of [the Producer], for example, for payment of rent on facilities utilized by [the Producer]. As to these funds, Aspen receives them and expends them as a disclosed agent for [the Producer]. [Administrative File (Formal Protest attachment to Hearing Request filed December 20, 2018)]

84. To the extent Aspen might come within the meaning of agent, neither Aspen nor the Producer would disclose Aspen's relationship with the Producer unless asked. [Cross Examination of Mr. Briones]

85. On November 7, 2018, the Department acknowledged Aspen's protest under Letter ID. No. L1161670832. [Administrative File (attachment to Hearing Request filed December 20, 2018)]

86. On December 20, 2018, the Department submitted a Hearing Request. [Administrative File (attachment to Hearing Request filed December 20, 2018)]

87. On December 20, 2018, the Administrative Hearings Office entered a Notice of Telephonic Scheduling Hearing which set an initial hearing in the matter for January 11, 2019. [Administrative File]

88. A telephonic scheduling hearing occurred on January 14, 2019 at which time the parties agreed that the hearing satisfied the 90-day hearing deadline and agreed that the matter was ready to proceed to a hearing on the merits of the protest. [Administrative File]

89. A Scheduling Order and Notice of Administrative Hearing was entered on January 14, 2019 which set a hearing on the merits of the protest to occur on July 15, 2019. [Administrative File]

90. On May 8. 2019, the Department filed an unopposed motion to continue the hearing set for July 15, 2019. [Administrative File]

91. On May 15, 2019, the Administrative Hearings Office entered an order continuing the hearing on the merits of the protest and set a scheduling hearing for June 3, 2019. [Administrative File]

92. On June 3, 2019, the parties agreed that they were unprepared to proceed with scheduling because discovery was ongoing. The parties with the Hearing Officer's concurrence agreed to continue scheduling. A Notice of Second Telephonic Scheduling Hearing was entered on June 3, 2019 that set a scheduling hearing to occur on August 16, 2019. [Administrative File]

93. On August 15, 2019, Aspen filed an unopposed Motion to Vacate and Continue Telephonic Scheduling Hearing. [Administrative File]

94. On August 16, 2019, the Administrative Hearings Office entered an Order Continuing Telephonic Scheduling Hearing for September 29, 2019. [Administrative File]

95. On September 29, 2019, the Department requested an additional 4 – 6 weeks to permit additional opportunity to review Aspen's discovery responses. Taxpayer did not object. [Administrative File]

96. On September 30, 2019, the Administrative Hearings Office entered a Notice of Scheduling Hearing which set the matter to be heard for that purpose on November 7, 2019. [Administrative File]

97. On November 7, 2019, the Department requested another scheduling hearing in

early 2020 in order to permit additional time for review of discovery and additional discussions with Aspen, which did not object. [Administrative File]

98. On November 7, 2019, the Administrative Hearings Office entered a Notice of Scheduling Hearing that set a scheduling hearing to occur on January 28, 2020. [Administrative File]

99. On January 28, 2020, the Department requested another scheduling hearing in April of 2020 in order to permit additional time for review of discovery and additional discussions with Aspen, which did not object. [Administrative File]

100. On January 29, 2020, the Administrative Hearings Office entered a Notice of Scheduling Hearing that set a scheduling hearing for April 16, 2020. [Administrative File]

101. On July 13, 2020, the Department requested another scheduling hearing in 30 days in order to permit additional time for review of discovery and additional discussions with Aspen, which did not object. [Administrative File]

102. On July 21, 2020, the Administrative Hearings Office entered a Notice of Scheduling Hearing that set a scheduling hearing to occur on August 17, 2020. [Administrative File]

103. On August 17, 2020, the Department requested another scheduling hearing in 60 days in order to permit additional time for review of discovery and additional discussions with Aspen, which did not object. [Administrative File]

104. On August 27, 2020, the Administrative Hearings Office entered a Notice of Scheduling Hearing that set a scheduling hearing to occur on October 13, 2020. [Administrative File]

105. On October 13, 2020, the Department requested another scheduling hearing in 60

days in order to permit additional time for review of discovery and additional discussions with Aspen, which did not object. [Administrative File]

106. On October 16, 2020, the Administrative Hearings Office entered a Notice of Scheduling Hearing that set a scheduling hearing to occur on December 10, 2020. [Administrative File]

107. On December 10, 2020, the parties agreed that they were prepared to proceed with filing dispositive motions. On December 16, 2020, the Administrative Hearings Office entered an Order Setting Briefing Schedule. [Administrative File]

108. Aspen filed Taxpayer's Motion for Summary Judgment on January 13, 2021. [Administrative File]

109. On January 26, 2021, Aspen filed Taxpayer's Motion to Supplement Filed Motion for Summary Judgment with Additional Exhibit. [Administrative File]

110. On March 1, 2021, the Department filed its response to Aspen's motion for summary judgment and its own cross motion. [Administrative File]

111. On April 13, 2021, Aspen filed Taxpayer's response to the Department's cross motion and its reply to the Department's response. [Administrative File]

112. The Hearing Officer deferred decision on the motions anticipating that a final decision in *Sacred Garden, Inc. v. New Mexico Taxation & Revenue Dep't*, 2021-NMCA-038, ¶17, 495 P.3d 576, 580, *cert. quashed Sacred Garden v. Taxation*, No. S-1-SC-38164 (Feb. 23, 2022) would be informative to issues under consideration.

113. The New Mexico Court of Appeals published its formal opinion in *Sacred Garden, Inc. v. New Mexico Taxation & Revenue Dep't*, 2021-NMCA-038, 495 P.3d 576 on January 28, 2020. The New Mexico Supreme Court granted a writ of certiorari on March 29,

2021 in No. S-1-SC-38164. On February 23, 2022, the New Mexico Supreme Court quashed its writ of certiorari as improvidently granted and ordered that a mandate immediately issue.

114. Taxpayer's Motion to Supplement Filed Motion for Summary Judgment with Additional Exhibit was accompanied by the Exhibit C (Affidavit of Erik Briones) from which additional facts are derived from the following sworn statements:

a. "Establishing the infrastructure to satisfy application requirements required a significant investment of capital that could not be obtained by financing available from any known financial institution due to the unwillingness of such lending institutions to loan money for a business that was illegal under federal law." [Affidavit of Erik Briones, Para. 6]

b. "Because startup capital was not available from traditional lenders, [the Producer] obtained it from several individuals who agreed to provide the capital in exchange for a return on their investment." [Affidavit of Erik Briones, Para. 7]

c. "As a nonprofit corporation, [the Producer] is prohibited from having equity owners." [Affidavit of Erik Briones, Para. 8]

d. "As a means of addressing the issues of providing a return on investment to those who had provided startup capital for [the Producer] and providing professional accounting services and management for [the Producer], [Mr. Briones] created an entity called Aspen Management, Inc[.]" [Affidavit of Erik Briones, Para. 11]

e. "In order to honor the fiction that [the Producer] is a nonprofit company, the receipts of [the Producer] flowing through Aspen are designated as management fees." [Affidavit of Erik Briones, Para. 14]

f. "The fees are meant to represent the cost of creating, operating, and managing [the Producer]." [Affidavit of Erik Briones, Para. 15]

115. Having considered arguments on the competing motions for summary judgment on November 1, 2022, the Administrative Hearings Office entered an Order for Additional Briefing with respect for questions that arose at the hearing which the parties had not anticipated. [Administrative File]

116. On December 15, 2022, Aspen filed Taxpayer's Brief on Applicability of Administrative Gloss. [Administrative File]

117. On January20, 2023, the Department filed its response to Taxpayer's Brief on Applicability of Administrative Gloss. [Administrative File]

118. Determining that resolution of the issues would be assisted by the live testimony of witnesses, the Administrative Hearings Office entered an Order Denying Motions for Summary Judgment, Scheduling Order and Notice of Hearing on the merits on April 27, 2023 and an in-person hearing on the merits of the protest was set for July 24, 2023. [Administrative File]

119. On June 29, 2023, Aspen filed Taxpayer's Witness and Exhibit List. [Administrative File]

120. On June 30, 3023, the Department filed its witness and exhibit list. [Administrative File]

121. On August 17, 2023, Aspen filed Taxpayer's Closing Argument. [Administrative File]

122. On August 23, 2023, the Department filed the Department's Closing Argument and Brief. [Administrative File]

DISCUSSION

At all relevant times, the Producer was engaged in the business of producing, packaging,

and dispensing medical cannabis under the Lynn and Erin Compassionate Use Act, NMSA 1978, Chapter 26, Article 2B ("CUA"). The purpose of CUA is to "make medical marijuana accessible to those with debilitating medical conditions who might benefit from the use thereof." *See* NMSA 1978, Section 26-2A-2 (2007).

In *Sacred Garden, Inc. v. New Mexico Taxation & Revenue Dep't*, 2021-NMCA-038, ¶ 17, 495 P.3d 576, 580, the Court of Appeals observed with respect to medical cannabis, "[i]t is reasonably self-evident that the deduction from gross receipts for prescription drugs was similarly intended to make medical treatment more accessible, *by lessening the expense to those who require it*." *Id.* (Emphasis Added). Thus, according to *Sacred Garden*, the legislature's underlying intent for the CUA was not only to make medical cannabis accessible, but to do so in a way that promoted affordability for those who might benefit from its use. Although the deduction central to *Sacred Garden* is not applicable to this protest, *Sacred Garden*'s extraction and discussion of the Legislature's broader policy goals and intentions underlying enactment of the CUA is germane to Taxpayer's principal argument which centers on the alleged absence of any "rational business reason" for the requirement that producers incorporate as non-profits.

The non-profit condition derives from the rules of the New Mexico Department of Health requiring producers to operate as "non-profit corporation[s] … pursuant to Section 53-8-1 et seq., NMSA 1978[.]" *See* Regulation 7.34.4.8 NMAC. However, because the non-profit entity required by the Department of Health's rules had certain limitations which to Mr. Briones were undesirable, Mr. Briones also established Aspen "as a separate *for-profit* entity to perform functions that would have been performed by [the Producer] itself if it had been allowed to organize as a for-profit corporation[.]" *See* Taxpayer's Closing Argument, Page 2 (Emphasis Added).

Thus, according to Mr. Briones, the non-profit Producer generated *all* receipts and then

transferred those receipts to for-profit Aspen. From the transfer onward, according to Mr. Briones, Aspen would perform various tasks which the Producer could not perform for itself, either because of its non-profit status, or because its tenuous status under federal law made it difficult, or sometimes impossible, to conduct commonplace business activities like entering into leases, maintaining bank accounts, or using banking services, securing payroll services, and obtaining credit card processing services.

Another of Aspen's functions included distributing the non-profit Producer's *profits* to its investors, a task that according to Mr. Briones, the Producer was not permitted to do as a New Mexico non-profit corporation. Aspen acknowledged that "[the Producer] did comply with the regulatory requirement that it be registered with the Secretary of State as a nonprofit corporation, but there [was] no explicit regulatory requirement that it be operated as a nonprofit." *See* Taxpayer's Closing Argument, Page 5 (Emphasis in Original).

With this setting in mind, Aspen argues that the assessment should be abated because "Aspen and [the Producer] are, in substance, one self-managed company with no need to pay management fees, and a consolidated financial statement would designate as dividends or wages (both deductible from gross receipts) the transfers to Aspen designated as management fees" or in the alternative, "Aspen is an affiliate of [the Producer] providing management services to [the Producer] at cost and entitled to the deduction provided for in [Section] 7-9-69." *See* Taxpayer's Closing Argument, Page 2.

The Hearing Officer notes that Aspen does not assert entitlement to any deductions or exemptions which the Producer might potentially claim if the Producer were the object of the Department's assessment. *See e.g.* NMSA 1978, Section 7-9-73.2. The Hearing Officer further notes that Aspen had previously suggested the potential application of NMSA 1978, Section 7-9-75

(deduction for receipts deriving from sale of certain services performed directly on product manufactured), but Aspen did not present evidence or explicitly assert entitlement to that deduction at the hearing or in its closing argument. Without producing such evidence or argument, Aspen abandoned and waived that specific claim.

Moreover, to the extent the facts presented herein might suggest potential applicability of the gross receipts exclusion for "amounts received solely on behalf of another in a disclosed agency capacity" under NMSA 1978, Section 7-9-3.5 A (3) (f), Aspen did not present evidence or argument in support of that potential defense. Because the evidence in the record is inadequate to establish applicability of the exclusion for "amounts received solely on behalf of another in a disclosed agency capacity," the Hearing Officer finds the exclusion to be unsupported by the evidence presented and inapplicable to the facts underlying the protest. For example, when asked several times during cross examination if Aspen's relationship with the Producer was disclosed to entities with which Aspen or the Producer sought to do business, Mr. Briones refrained from responding with a "yes" or "no" answer, choosing instead to explain, "they never asked." This response fails to establish the necessary element of disclosure under Section 7-9-3.5 A (3) (f).

Presumption of Correctness.

NMSA 1978, Section 7-1-17 (C) (2007) requires that the assessment issued in this case be presumed correct. Consequently, Taxpayer has the burden of rebutting the presumption. *See Archuleta v. O'Cheskey*, 1972-NMCA-165, ¶ 11, 84 N.M. 428. Unless otherwise specified, for the purposes of the Tax Administration Act, "tax" is defined to include interest and civil penalty. *See* NMSA 1978, Section 7-1-3 (X) (2013). Under Regulation 3.1.6.13 NMAC, the presumption of correctness under Section 7-1-17 (C) extends to the Department's assessment of penalty and interest. *See Chevron U.S.A., Inc. v. State ex rel. Dep't of Taxation & Revenue*, 2006-NMCA-50, ¶

16, 139 N.M. 498, 503 (agency regulations interpreting a statute are presumed proper and are to be given substantial weight).

Therefore, it is Taxpayer's burden to present some countervailing evidence or legal argument to rebut the presumption of correctness. *See N.M. Taxation & Revenue Dep't v. Casias Trucking*, 2014-NMCA-099, ¶8; *Gemini Las Colinas, LLC v. N.M. Taxation & Revenue Dep't*, 2023-NMCA-__, ¶ 27, No. A-1-CA-38672 (March 13, 2023)

Whether a taxpayer has satisfied the initial burden of production is a threshold legal determination in which the Hearing Officer decides whether a taxpayer has produced some countervailing evidence tending to dispute the correctness of the assessment. *See Gemini,* 2023-NMCA-__, ¶¶ 21 – 23; 25. The Hearing Officer was persuaded in this protest that Taxpayer satisfied its initial burden of production.

If a taxpayer satisfies the initial burden of production, then the burden of production shifts to the Department to present evidence showing the correctness of its assessment beyond mere assertions that a taxpayer's evidence is unreliable or not credible. *See Gemini,* 2023-NMCA-__, ¶ 29. The Hearing Officer is then to weigh the evidence presented from both parties under the preponderance standard and ultimately determine whether a taxpayer has carried its burden of persuasion in the protest. *Id*.

Because the Hearing Officer is persuaded that both parties satisfied their respective burdens of production, the remainder of this Decision and Order will concentrate on weighing the evidence presented from both parties under the preponderance standard and ultimately determine whether the taxpayer carried its burden of persuasion.

Gross Receipts Tax.

For the privilege of engaging in business in New Mexico, a gross receipts tax is imposed

on the receipts of any person engaged in business. *See* NMSA 1978, Section 7-9-4 (2010). The term "gross receipts" is defined to mean:

> [T]he total amount of money or the value of other consideration received from selling property in New Mexico, from leasing or licensing property employed in New Mexico, from granting a right to use a franchise employed in New Mexico, from selling services performed outside New Mexico, the product of which is initially used in New Mexico, or from performing services in New Mexico.
>
> *See* NMSA 1978, Section 7-9-3.5 (A) (1) (2019)

There is a statutory presumption that all receipts of a person engaged in business are taxable. *See* NMSA 1978, Section 7-9-5 (2019). "Receipts include payments received for one's own account and then expended to meet one's own responsibilities." *See MPC Ltd. v. New Mexico Taxation & Revenue Dept.*, 2003-NMCA-021, ¶ 14, 133 N.M. 217, 220, 62 P.3d 308, 311. "Engaging in business" is defined as "carrying on or causing to be carried on any activity with the purpose of direct or indirect benefit." *See* NMSA 1978, Section 7-9-3.3 (2019). *See also Comer v. State Tax Comm'n,* 1937-NMSC-032, ¶37, 41 N.M. 403 (gross receipts applies to "all activities or acts engaged in (personal, professional and corporate) or caused to be engaged in with the object of gain, benefit[,] or advantage either direct or indirect.")

As a practical matter, the initial step in an audit is to compute the amount of gross receipts at issue with reference to Section 7-9-3.5, the sum of which is presumed taxable under Section 7-9-5. Subsequent steps allow a taxpayer to reduce its total gross receipts by those amounts which are deductible or exempt with specific reference to the applicable deductions or exemptions provided in the Gross Receipts and Compensating Tax Act. The difference between total gross receipts and any applicable deductions or exemptions is the amount of taxable gross receipts.

In this protest, the evidence demonstrated how the Department conducted its audit and ultimately identified and assessed a gross receipts tax liability of $320,359.17, plus interest and

penalty. *See* Department Ex. B. Despite the occasional use of imprecise or inartful language in the Audit Narrative, the Hearing Officer does not perceive those areas with which Aspen takes issue as material to the computations that produced the Assessment. Any conflation or misuse of the terms "non-profit" and "tax exempt" do not affect the computations of gross receipts which are presumed taxable under Section 7-9-5. It is undisputed that the Producer is a non-profit corporation, it has never been tax-exempt, and Aspen is a for-profit corporation.

"The Crux of the Problem"

Taxpayer argues that "[t]he crux of the problem faced by the [T]axpayer in this case is that its very existence would never have been necessary but for the enactment of a questionable regulation of the Department of Health requiring applicants for a license to produce medical cannabis to be organized as nonprofit corporations." *See* Taxpayer's Closing Argument, Page 1.

The manner in which Aspen frames the issue suggests that the Administrative Hearings Office has the ability to disregard, or perhaps invalidate, a Department of Health regulation in the context of a tax protest under the Administrative Hearings Office Act. *See* NMSA 1978, Section 7-1B-6 C. Aspen cites no authority in support of such proposal. In any event, the Administrative Hearings Office need not consider the bounds of its authority because the Hearing Officer does not perceive the regulation which Taxpayer argued to be the crux of the issue as questionable.

"Agency regulations that interpret statutes and are promulgated under statutory authority are presumed proper, '[a]nd, of course, it is hornbook law that an interpretation of a statute by the agency charged with its administration is to be given substantial weight.'" *See Chevron U.S.A., Inc. v. State of N.M. ex rel. Taxation & Rev. Dept.*, 2006-NMCA-050, ¶ 16, 139 N.M. 498, 503, 134 P.3d 785, 790.

"A party challenging a rule adopted by an administrative agency has the burden of showing the invalidity of the rule or regulation. The reasonableness of an administrative rule or regulation is not purely a legal question; a factual basis must appear. To successfully challenge a rule promulgated by an agency exercising its delegated legislative authority, *the challenger must show, in part, that the rule's requirements are not reasonably related to the legislative purpose but are arbitrary and capricious*." *See Old Abe Co. v. New Mexico Min. Comm'n*, 1995-NMCA-134, ¶ 10, 121 N.M. 83, 88, 908 P.2d 776, 781 (Emphasis Added). "A party challenging a rule adopted by an administrative agency has the burden of establishing the invalidity of the rule or proposed regulation." *See New Mexico Mining Ass'n v. New Mexico Mining Comm'n*, 1996-NMCA-098, ¶ 8, 122 N.M. 332, 335, 924 P.2d 741, 744.

Based on the evidence and argument presented, the rule's requirements are reasonably related to the legislative purpose underlying the CUA and are not arbitrary and capricious. As explained by *Sacred Garden*, "the Compassionate Use Act was intended to make medical marijuana accessible to those with debilitating medical conditions who might benefit from the use thereof." *See Sacred Garden, Inc.*, 2021-NMCA-038, ¶17. In evaluating whether a taxpayer could obtain the benefit of a gross receipts tax deduction reserved for prescription drugs, *Sacred Garden* observed, "[i]t is reasonably self-evident that the deduction from gross receipts for prescription drugs was similarly intended to make medical treatment more accessible, *by lessening the expense to those who require it*. These statutes should be read harmoniously, to give effect to their commonality of purpose." *Id*. (Emphasis Added)

In this case, the Legislature required the secretary of the New Mexico Department of Health to promulgate rules to implement the CUA. *See* NMSA 1978, Section 26-2B-6 – 7 (2007). Specific areas of relevance for rulemaking included establishing, "*requirements for the licensure of*

producers and cannabis production facilities and set forth procedures to obtain licenses[.]" *See* Section 26-2B-7 A (5) (2007) (Emphasis Added). The Legislature then specified that "licensed producer" meant "any person or association of persons within New Mexico *that the department determines to be qualified* to produce, possess, distribute and dispense cannabis pursuant to the Lynn and Erin Compassionate Use Act and that is licensed by the department[.]" *See* NMSA 1978, Section 26-2B-3 D (2007) (Emphasis Added). Conversely stated, the Legislature provided explicit and exclusive authority to the Department of Health to determine qualifications of licensure eligibility.

Although Aspen asserts that the requirement that licensed producers be established as nonprofit corporations has no "rational business reason," the record of the rulemaking process suggests that the nonprofit requirement was consistent with the Legislature's intentions, as expressed in the CUA. *See Sacred Garden*. In response to Aspen's request to inspect public records, the Department of Health produced records revealing that, "[m]edical cannabis must be affordable to those in need." *See* Taxpayer Ex. 1-014, Para. 8. It also considered the point that, "[i]n order to ensure that distributors are not accused of profiteering, it is recommended that dispensaries ensure transparency, openness, financial accountability, and mechanisms for client feedback. Non-profit incorporation is one way of meeting these criteria." *See* Taxpayer Ex. 1-018, Para. 1.

The Hearing Officer perceives the Department of Health's rules, requiring licensed producers to be incorporated as non-profits, to be consistent with, implementing, and exemplifying the policy of establishing a system that discourages profiteering and promoting affordability for those who might benefit from the use of medical cannabis, consistent with *Sacred Garden*'s observations that affordability was a goal of the Legislature's policy.

To the extent Taxpayer asserts that the non-profit corporation requirement was not

considered by the Department of Health's advisory board, contrary to Section 26-2B-7, but simply included in the rules absent any meaningful consultation and advice, the argument is unpersuasive based on a lack of evidence presented in support of such assertion. *See New Mexico Mining*, 1996-NMCA-098, ¶ 8.

To the extent Aspen could have argued that taxation in this protest would reduce affordability by increasing expenses to patients in need, it made no such argument, and presented no such evidence. In fact, when asked during cross examination if reducing payments to private party investors could have decreased the cost of products for patients in need, Mr. Briones enthusiastically denied that affordability was a component of the CUA and told Mr. Pener, "You sound like a medical patient who's on welfare who wants everything for free." Tr. Pt. 1, 2:16:15 – 2:16:31. After some more discussion, Mr. Pener, on cross examination said, "You didn't answer my question. My question was: If this money did not go to shareholders of Aspen, it could have been used to reduce the price of the product that [the Producer] sold? That's a 'yes' or a 'no[,]'" to which Mr. Briones answered, "No." Tr. Pt. 1, 2:17:05 – 2:17:22.

These observations are relevant to *Sacred Garden*'s regard for affordability and consideration of whether a tax imposed on Aspen for management services could undercut the Legislature's policy favoring affordability for patients in need. On the whole, if a reduction in disbursements to private individuals has no effect on costs of cannabis products for eligible patients, as expressed by Mr. Briones, then a tax representing a fraction of those disbursements should be similarly unoffending.

Accordingly, the Assessment of tax in this protest does not offend the policy of the Legislature intending "to make medical treatment more accessible, by lessening the expense to those who require it." *See Sacred Garden, Inc. v. New Mexico Taxation & Revenue Dep't*, 2021-

NMCA-038, ¶ 17, 495 P.3d 576, 580.

For these reasons, the Hearing Officer does not perceive the referenced regulation as "questionable" in light of *Sacred Garden*'s thorough discussion of the Legislature's objectives in enacting the CUA. Although the Hearing Officer is mindful of Taxpayer's frustration, the Department of Health's rule that licensed producers engage in business as nonprofit corporations is presumed proper and there is no basis in the record with which to establish that the non-profit requirement contradicts the Legislature's purpose when it enacted the CUA. The Department of Health was cognizant of the Legislature's intentions in making affordable medical cannabis available to those in need and implemented rules to advance that purpose consistent with the authority granted by the Legislature.

When, as in this case, the Legislature grants agencies the discretion of promulgating rules and regulations, those rules and regulations have "the force of law." *See Duke City Lumber Co. v. New Mexico Envtl. Improvement Bd.*, 1984-NMSC-042, ¶ 7, 101 N.M. 291, 292, 681 P.2d 717, 718.

As a final observation before proceeding with the discussion of Aspen's other arguments, there is no evidence that the Producer's non-profit status alone precluded it from conducting most ordinary business activities. The obstacles it encountered arose from the fact that it was engaged in the business of producing medical cannabis. In other words, the isolated fact that it was required to incorporate as a non-profit did not contribute to its inability to procure banking services, credit card processing services, payroll services, or other necessary and ordinary business services. Thus, the primary disadvantage to the Producer, by virtue of the non-profit corporation requirement was that "you cannot distribute a dividend in a non-profit" and the Producer's investors wanted a maximum return on their investment. [Direct Examination of Mr. Briones]

Should Aspen and the Producer be taxed as "one self-managed company?"

Aspen argues that "established law justifies – if not compels – that the [Producer] – Aspen relationship should be taxed based on its substance rather than its form." *See* Taxpayer's Closing Argument, Page 2. Therefore, it argues Aspen and the Producer should be perceived as "one self-managed company with no need to pay management fees, and a consolidated financial statement would designate as dividends or wages (both deductible from gross receipts) the transfers to Aspen designated as management fees[.]" *See* Taxpayer's Closing Argument, Pages 2 – 3.

In support, Aspen cited *Feldman v. C.I.R.*, 779 F.3d 448 (7th Cir. 2015) for the proposition that the manner in which Aspen and the Producer characterize the funds should not be deemed conclusive when the receipts upon which the assessment was founded were not really management fees paid for management services. Instead, Aspen explained that "[t]he designation in the bookkeeping records of [the Producer] and Aspen of funds appearing to flow from [the Producer] to Aspen as 'management fees' is likewise 'a mere accounting device, devoid of substance.'" *See* Taxpayer's Closing Argument, Page 7.

However, characterizations that Aspen did not provide management services or that it did not generate receipts from such services is inconsistent with how Aspen kept its records, reported its income for tax purposes, or even explained its operations during the pre-hearing phases of the protest.

In its formal protest, Aspen stated that it derived receipts from "management services rendered" which was consistent with how the Producer reported its income and expenses for tax purposes, how Aspen reported its own federal income and expenses for tax purposes, and how it maintained internal accounting records. Aspen and the Producer were even parties to a management agreement in which Aspen agreed to provide management services. *See* Department Ex. E-053 – E057. Prior sworn statements also confirmed Aspen's position that it generated receipts from

providing management services for the Producer. *See e.g.* Department Ex. E-009 – E-010 (No. 9); E-010 (No. 10); E-012 (No. 12).

Yet, Mr. Briones explained at the hearing that despite previous representations to the contrary, Aspen never actually performed management services, and that even the management agreement was intended to perpetrate "the *illusion* that Aspen was a management company overseeing the operations of [the Producer]." Tr. Pt. 1, 59:54 – 1:01:25 (Emphasis Added).

When asked about the costs of such services, Mr. Briones denied there was any cost at all, contrary to prior sworn statements that services were provided and supposedly compensated on a cost basis. *See* Department Ex. E-010 ("…managerial and accounting services provided by Aspen and are based upon Aspen's cost of providing such services."). The Hearing Officer appreciates Mr. Briones' candor, but the admission that Aspen and the Producer engaged in activity intended to perpetrate an "illusion," coupled with other contradictions about the sort of services provided and the costs of those services diminish Mr. Briones' overall credibility, the trustworthiness of Aspen's evidence, and the sway of arguments that rely on them.

Nevertheless, Taxpayer asserts that the substance of its relationship with the Producer should determine how it is taxed instead of its form. *See* Taxpayer's Closing Argument, Page 2. The Department counters that this argument is futile under existing law which explains that "taxation is the rule and the claimant must show that his demand is within the letter as well as the spirit of the law." *See TPL, Inc. v. New Mexico Taxation & Revenue Dept.*, 2003-NMSC-007, ¶ 9, 133 N.M. 447, 451, 64 P.3d 474, 478. The Hearing Officer agrees with the Department that the rule explained more than 20 years ago in *TPL* establishes the footing for further evaluation.

Aspen's receipts are presumed taxable under Section 7-9-5 *and* it bears the burden of establishing entitlement to any applicable deductions or exemptions consistent with the guidance of

TPL, Inc., 2003-NMSC-007, ¶9 which instructs that: (1) "[t]he right to a deduction must be clearly and unambiguously expressed in the statute[;]" and (2) "[t]he taxpayer must show that it is clearly entitled to the statutory deduction."

Under the evidence and arguments presented, Aspen's receipts are taxable unless or until it can prove entitlement to an applicable deduction or exemption. Taxpayer cites no New Mexico authority for the proposition that Aspen's relief from the Assessment can derive from the recognition of a fictional oxymoronic entity that is one-half for-profit and one-half non-profit, but still a single unified entity for tax purposes (i.e. a *non-profit for profit* or a *for-profit non-profit*). "Where a party cites no authority to support an argument, we may assume no such authority exists." *See Curry v. Great Nw. Ins. Co.*, 2014-NMCA-031, ¶ 28, 320 P.3d 482, 489. Moreover, contemplation of Aspen's suggestion reveals myriad unresolvable conflict among the governing statutes that the Legislature would never intend, for example, how a non-profit corporation (the Producer) can operate as a for-profit corporation without offending the law controlling its creation.

Aspen and the Producer are not a "unified entity" under the evidence or the law. Relief from the Assessment must stem from long established law requiring Aspen to show that it is "clearly entitled" to a deduction or exemption that is "clearly and unambiguously expressed in the statute."

Potential Application of Section 7-9-69

NMSA 1978, Section 7-9-69 provides a deduction from gross receipts for the receipts "of a business entity for administrative, managerial, accounting and customer services performed by it for an affiliate upon a nonprofit or cost basis and receipts of a business entity from an affiliate for the joint use or sharing of office machines and facilities upon a nonprofit or cost basis[.]"

For the purpose of qualifying for the deduction, "affiliate" means a "business entity that

directly or indirectly through one or more intermediaries controls, is controlled by or is under common control with another business entity." The term "business entity" is defined to mean "a corporation, limited liability company, partnership, limited partnership, limited liability partnership or real estate investment trust, but does not mean an individual or a joint venture[.]" Finally, the term "control" means "equity ownership in a business entity that: (a) represents at least fifty percent of the total voting power of that business entity; or (b) has a value equal to at least fifty percent of the total equity of that business entity."

The problem, as Aspen has aptly summarized it, is that Aspen is technically precluded from eligibility for the deduction because its relationship with the Producer fails to satisfy the definition of "control" which in turn fails to satisfy the definition of "affiliate." Aspen has acknowledged these issues observing that "the only reason it fails to meet the statute's definition of 'affiliate' in NMSA 1978, Section 7-9-69 (B) is the fact that although it controls, is controlled by, or is under common control with [the Producer], it's de facto affiliate, it cannot meet the statutory definition of 'control' (and hence, 'affiliate') because 'equity ownership' is a definitional element of 'control' and as a nonprofit corporation, [the Producer], Aspen's only client, is prohibited from having equity owners." *See* Taxpayer's Motion for Summary Judgment, Page 5.

However, Aspen does not view this as an obstacle arguing that disqualification from eligibility relies on an "overly technical" construction of "control" in Section 7-9-69 and "unfairly elevates form over substance." *See* Taxpayer's Closing Argument, Pages 3 – 4.

The Hearing Officer, once again thoughtful of Aspen's frustrations, remains unpersuaded by its argument. It has long been recognized that tax exemptions and deductions are matters of legislative grace and ways of achieving policy objectives. They are "construed against the taxpayer." *See Sutin, Thayer & Browne v. N.M. Taxation & Revenue Dep't*, 1985-NMCA-047, ¶ 17,

104 N.M. 633, 725 P.2d 833. Construing the deduction as Aspen encourages requires that the Hearing Officer disregard *Sutin* and the plain language of the statutory deduction which Aspen has already acknowledged disqualifies it from eligibility.

Even if the Hearing Officer were persuaded that the plain language of the statute could be relaxed in order to permit a construction in favor of Aspen, it would still not qualify for the benefit of the deduction provided by Section 7-9-69 because Aspen's evidence and arguments fail to persuade that managerial services were provided "at cost." Aspen explained that "[a]side from monies 'received' by Aspen to pay expenses of [the Producer], payments by [the Producer] to Aspen are for managerial and accounting services provided by Aspen and are based upon Aspen's cost of providing such services." *See* Department Ex. E-010. Aspen went on to define its costs to include the "cost of capital" which includes "a return to Aspen's equity owners for the money they provided to start [the Producer]" in the form of a dividend. *See* Department Ex. E-010; Taxpayer's Closing Argument, Page 6.

But in terms of the evidence presented, Mr. Briones' first denied that Aspen provided services, but even if it did, then he acknowledged that there were *no costs* associated with the services provided, and for that reason, no need to perform a cost accounting analysis to determine the cost of services. Tr. Pt. 2, 16:35 – 19:25.

The contradictions are palpable. Aspen claims that payments from the Producer were for managerial and accounting services and that they were "based upon Aspen's cost of providing such services." On the other hand, Mr. Briones also explained that there were no costs incurred in providing the services. Yet, Aspen continued to argue, even after Mr. Briones' testimony that to the extent it provided services, "it provided those services at cost." *See* Taxpayer's Closing Argument, Page 6. It even went on to condemn the Department for its perceived failure to "present any

evidence to discredit the taxpayer's contention that to the extent Aspen - [the Producer] relationship can be analyzed as one involving the sale of services by Aspen to [the Producer], the services were valued at cost." Aspen's argument is unpersuasive. Aspen has the burden of establishing entitlement to the deduction. *See TPL, Inc.*, 2003-NMSC-007, ¶ 31.

However, if Mr. Briones' testimony is accurate, that there were no actual costs associated with the services provided, then Aspen fails to qualify for the deduction under Section 7-9-69. To illustrate, in the simplest terms, if Aspen's costs were zero, then receipts in excess of zero exceed Aspen's costs and would preclude it from qualifying for the deduction under Section 7-9-69, since the deduction is only available for services provided "upon a non-profit or cost basis." The evidence established that Aspen's receipts from providing services exceeded $4.8 million. If Mr. Briones' testimony is accurate, then the receipts for those services exceeded Aspen's costs in excess of $4.8 million. If that is not correct, then Aspen, not the Department, bears the burden of establishing its true costs under *TPL*. Aspen did not meet this burden.

As previously stated, Aspen has acknowledged it does not qualify for the deduction provided by Section 7-9-69, as written, because it fails to satisfy the element that the Producer and Aspen be affiliates. But even if the definition of "affiliate" could be relaxed, Aspen's claim still fails for lack of evidence to show that the services were provided on a non-profit or cost basis. Aspen did not establish entitlement to a deduction under Section 7-9-69.

Other Potential Deductions or Exemptions

As previously observed, Aspen initially asserted potential application of Section 7-9-75, but did not advance that claim at hearing. Aspen also suggested in its closing argument the possibility that other deductions and exemptions could potentially apply *if* the Hearing Officer determined that the non-profit Producer and for-profit Aspen should be perceived as a single unified business entity.

The Hearing Officer declined the request to recognize the unified business entity for the reasons discussed but will nevertheless address the potential application of other deductions or exemptions.

It asserted that if the entities were unified, then fees previously categorized as management fees would instead be categorized as dividends or wages, both of which it asserts are deductible under the Gross Receipts and Compensating Tax Act. Taxpayer does not cite the deductions it claims should apply or explain how it satisfies the elements of eligibility for such deduction.

Lack of citation requires the Hearing Officer to infer that Aspen's reference to wages and dividends is intended to refer to exemptions under Section 7-9-17 (exemption for wages) and Section 7-9-25 (exemption for interest and dividends). The Hearing Officer did not identify any other deductions or exemptions under the Gross Receipts and Compensating Tax Act[4] that corresponded with Aspen's description or which might otherwise apply.

Section 7-9-17 provides an exemption for wages. It states, "[e]xempted from the gross receipts tax are the *receipts of employees from wages*, salaries, commissions or from other form of renumeration for personal services." (Emphasis Added). This exemption is not applicable to the Producer or Aspen, either individually or collectively because the receipts at issue would not constitute "receipts of employees" for personal services. *See* also Regulation 3.2.105.7 NMAC. Instead, the receipts are those of Aspen, which is not an employee.

Section 7-9-25 provides an exemption for "receipts received as interest on money loaned or deposited, receipts received as dividends or interest from stocks, bonds or securities or receipts from the sale of stocks, bonds or securities." Again, this exemption is not applicable to the Producer or Aspen, either individually or collectively. The receipts at issue do not represent: (1) *interest* on money loaned *by Aspen* or deposited *with Aspen*. Aspen, the juridical entity never loaned money to

[4] Although other tax programs may allow a deduction for wages or dividends paid, those various deductions would not apply to an assessment arising under the Gross Receipts and Compensating Tax Act.

the Producer, and neither entity asserted that the receipts represented interest on a loan or deposits. The receipts at issue do not represent: (2) *receipts received by Aspen* as dividends or interest from stocks, bonds, or securities. There is a lack of evidence to suggest that Aspen, the juridical entity, owned stocks, bonds or securities from which dividends could be derived. The receipts at issue also do not represent: (3) receipts of Aspen from the *sale* of stocks, bonds or securities. The receipts at issue represent money derived from the Producer's business activities and transferred in whole to Aspen, with the exception of some cash, which the parties designated as "management fees" for all intents and purposes. Receipts did not derive from the sale of any interest in the Producer.

Aspen readily acknowledged the Producer was prohibited from making distributions to investors. That was one, if not the primary reason, why Aspen was established in the first place. The Hearing Officer is not persuaded based on the evidence presented that Aspen is entitled to a deduction under Section 7-9-25.

Aspen has not established the right to any deduction or exemption under the evidence presented, including deductions under Section 7-9-17 (exemption for wages) and Section 7-9-25 (exemption for interest and dividends).

For the reasons stated, Taxpayer's protest is DENIED.

CONCLUSIONS OF LAW

A. Taxpayer filed a timely, written protest to the Assessment. Jurisdiction lies over the parties and the subject matter of this protest.

B. The Department made a timely request for hearing and the Administrative Hearings Office conducted a hearing within 90 days of Taxpayer's protest under NMSA 1978, Section 7-1B-8 (2019). The parties did not object that the hearing satisfied the requirements of Section 7-1B-8.

C. Aspen's receipts from engaging in business in New Mexico are presumed taxable.

See NMSA 1978, Section 7-9-5 (2019).

D. "Engaging in business" is defined as "carrying on or causing to be carried on any activity with the purpose of direct or indirect benefit." *See* NMSA 1978, Section 7-9-3.3 (2019). *See also Comer v. State Tax Comm'n,* 1937-NMSC-032, ¶37, 41 N.M. 403 (gross receipts applies to "all activities or acts engaged in (personal, professional and corporate) or caused to be engaged in with the object of gain, benefit[,] or advantage either direct or indirect.")

E. "Gross receipts" means "The total amount of money or the value of other consideration received … from performing services in New Mexico." *See* NMSA 1978, Section 7-9-3.5 (A) (1) (2019).

F. "Receipts include payments received for one's own account and then expended to meet one's own responsibilities." *See MPC Ltd. v. New Mexico Taxation & Revenue Dept.*, 2003-NMCA-021, ¶ 14, 133 N.M. 217, 220, 62 P.3d 308, 311.

G. "Taxation is the rule and the claimant must show that his demand is within the letter as well as the spirit of the law." *See TPL, Inc. v. New Mexico Taxation & Revenue Dept.*, 2003-NMSC-007, ¶ 9, 133 N.M. 447, 451, 64 P.3d 474, 478.

H. The primary goal of statutory interpretation is "to give effect to the intent of the [L]egislature." *See Dell Catalog Sales L.P. v. N.M. Taxation & Revenue Dep't,* 2009-NMCA-001, ¶19, 145 N.M. 419, 199 P.3d 863.

I. Legislative intent is fulfilled "by first looking at the plain meaning of the language of the statute, reading the provisions ... together to produce a harmonious whole." *See Dell Catalog Sales L.P. v. N.M. Taxation & Revenue Dep't,* 2009-NMCA-001, ¶19, 145 N.M. 419, 199 P.3d 863; *Sundance Mech. & Util. Corp. v. Armijo*, 1987-NMSC-078, ¶5, 106 N.M. 249, 250, 741 P.2d 1370, 1371.

J. Tax exemptions and deductions are matters of legislative grace and ways of achieving policy objectives. They are "construed against the taxpayer." *See Sutin, Thayer & Browne v. N.M. Taxation & Revenue Dep't,* 1985-NMCA-047, ¶ 17, 104 N.M. 633, 725 P.2d 833.

K. The Lynn and Erin Compassionate Use Act, NMSA 1978, Chapter 26, Article 2B "was expressly intended 'to allow the beneficial use of medical cannabis in a regulated system for alleviating the symptoms caused by debilitating medical conditions and their medical treatments.'" *See* NMSA 1978, Section 26-2A-2 (2007); *Sacred Garden, Inc. v. New Mexico Taxation & Revenue Dep't,* 2021-NMCA-038, ¶17, 495 P.3d 576, 580, *cert. quashed Sacred Garden v. Taxation*, No. S-1-SC-38164 (Feb. 23, 2022).

L. "It is reasonably self-evident that the deduction from gross receipts for prescription drugs was similarly intended to make medical treatment more accessible, by lessening the expense to those who require it." *See Sacred Garden, Inc. v. New Mexico Taxation & Revenue Dep't,* 2021-NMCA-038, ¶ 17, 495 P.3d 576, 580.

M. The New Mexico Department of Health's rules governing licensure of medical cannabis producers require that producers operate as "non-profit corporation[s] … pursuant to Section 53-8-1 et seq., NMSA 1978[.]" *See* Regulation 7.34.4.8 NMAC

N. "Agency regulations that interpret statutes and are promulgated under statutory authority are presumed proper, '[a]nd, of course, it is hornbook law that an interpretation of a statute by the agency charged with its administration is to be given substantial weight.'" *See Chevron U.S.A., Inc. v. State of N.M. ex rel. Taxation & Rev. Dept.*, 2006-NMCA-050, ¶ 16, 139 N.M. 498, 503, 134 P.3d 785, 790.

O. "A party challenging a rule adopted by an administrative agency has the burden of establishing the invalidity of the rule or proposed regulation." *See New Mexico Mining Ass'n v.*

New Mexico Mining Comm'n, 1996-NMCA-098, ¶ 8, 122 N.M. 332, 335, 924 P.2d 741, 744.

P. When the Legislature grants agencies the discretion of promulgating rules and regulations, those rules and regulations have "the force of law." *See Duke City Lumber Co. v. New Mexico Envtl. Improvement Bd.*, 1984-NMSC-042, ¶ 7, 101 N.M. 291, 292, 681 P.2d 717, 718.

Q. Taxpayer bears the burden of establishing entitlement to a clearly and unambiguously expressed statutory deduction or exemption. *See TPL, Inc. v. N.M. Taxation & Revenue Dep't*, 2003-NMSC-007, ¶9, 133 N.M. 447, 64 P.3d 474.

R. Statutory provisions must be given "fair, unbiased, and reasonable construction, without favor or prejudice to either the taxpayer or the [s]tate, to the end that the legislative intent is effectuated and the public interests to be subserved thereby are furthered." *See Chavez v. Comm'r of Revenue*, 1970-NMCA-116, ¶7, 82 N.M. 97, 476 P.2d 67.

S. Aspen did not establish entitlement to any statutory deduction or exemption provided by the Gross Receipts and Compensating Tax act, including Section 7-9-17, Section 7-9-25, and Section 7-9-69, nor did it establish that the relevant receipts should be excluded under Section 7-9-3.5.

For the reasons stated, Taxpayer's protest is DENIED. Taxpayer, Aspen Management Company, shall be liable for outstanding principal and penalty under the Assessment, plus accrued interest as permitted by law.

DATED: November 7, 2023

Chris Romero
Hearing Officer
Administrative Hearings Office
P.O. Box 6400
Santa Fe, NM 87502

NOTICE OF RIGHT TO APPEAL

Pursuant to NMSA 1978, Section 7-1-25 (2015), the parties have the right to appeal this decision by *filing a notice of appeal with the New Mexico Court of Appeals* within 30 days of the date shown above. If an appeal is not timely filed with the Court of Appeals within 30 days, this Decision and Order will become final. Rule of Appellate Procedure 12-601 NMRA articulates the requirements of perfecting an appeal of an administrative decision with the Court of Appeals. Either party filing an appeal shall file a courtesy copy of the appeal with the Administrative Hearings Office contemporaneous with the Court of Appeals filing so that the Administrative Hearings Office may begin preparing the record proper. The parties will each be provided with a copy of the record proper at the time of the filing of the record proper with the Court of Appeals, which occurs within 14 days of the Administrative Hearings Office receipt of the docketing statement from the appealing party. *See* Rule 12-209 NMRA.

CERTIFICATE OF SERVICE

I hereby certify that I served the foregoing on the parties listed below this 7th day of November, 2023 in the following manner:

First Class Mail and Email	*First Class Mail and Email*

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