BEFORE THE HEARING OFFICER
OF THE TAXATION AND REVENUE DEPARTMENT
OF THE STATE OF NEW MEXICO

IN THE MATTER OF THE PROTEST OF
ITT EDUCATIONAL SERVICES, INC., NO. 97-02
I.D. NO. 02-133184-00 7, PROTEST
TO ASSESSMENT NO. 1940766

DECISION AND ORDER

This matter came on for formal hearing on August 22, 1996 before Gerald B. Richardson, Hearing Officer. ITT Educational Services, Inc., hereinafter, "Taxpayer," was represented by Curtis W. Schwartz, Esq. The Taxation and Revenue Department, hereinafter, "Department," was represented by Frank D. Katz, Chief Counsel. At the close of the hearing the record was held open to allow the parties to submit briefs and proposed findings of fact and conclusions of law. Briefing was completed on November 21, 1996 and the matter was considered submitted for decision at that time. The parties have agreed that the Hearing Officer may have until January 15, 1997 to render his decision herein. Based upon the evidence and the arguments submitted, it is decided and ordered as follows:

FINDINGS OF FACT

1. The Taxpayer is a Delaware corporation whose corporate headquarters and principal place of business are located in Indianapolis, Indiana.

2. During the audit period the Taxpayer owned and operated approximately 54 educational facilities which will be referred to as "ITT Technical Institutes."

3. During the audit period the ITT Technical Institutes were located in approximately 25 states.

4. At present, the Taxpayer operates 59 ITT Technical Institutes in 26 states.

5. The Taxpayer is the largest proprietary (private, for profit) college in the United States.

6. One of the ITT Technical Institutes, ITT Tech, is located in Albuquerque, New Mexico.

7. ITT Tech is the only ITT Technical Institute in New Mexico.

8. ITT Tech began operations in Albuquerque in December, 1989.

9. In late 1989, the Taxpayer obtained authority to do business in New Mexico from the State Corporation Commission, obtained the necessary business license from the City of Albuquerque and registered with the Department of Labor.

10. In late 1989, the Taxpayer applied for a tax identification number with the Department.

11. As part of its operations in Albuquerque, the Taxpayer sells text books, kits with tools, components and other materials necessary for classes the student is taking and miscellaneous clothing and other items of school memorabilia. These items are sold separately from and are not included in the tuition paid by the students.

12. The Taxpayer has always paid gross receipts tax on its receipts derived from the sale of the items described in paragraph 11, above, which would typically be associated with the operation of a campus bookstore.

13. Beginning in April, 1995, the Department conducted an audit of the Taxpayer.

14. The Department's audit determined that the Taxpayer had reported and paid gross receipts tax on the sales of the bookstore related items, but that the Taxpayer had not reported or paid gross receipts tax on its receipts from providing educational services at its Albuquerque campus, ITT Tech.

15. As a result of the Department's audit, the Department issued Assessment No. 1940766, dated June 21, 1995, to the Taxpayer.

16. The total amount assessed pursuant to Assessment No. 1940766 is $832,963.14 That amount consists of gross receipts tax in the amount of $569,423.69, penalty in the amount of

$55,493.16 and interest in the amount of $208,046.29, calculated through June 25, 1995.

17. The audit period covered by Assessment No. 1940766 is January 1, 1989 through March 31, 1995.

18. The Taxpayer requested an extension of time of 60 days in which to file its protest to Assessment No. 1940766. The Department granted the Taxpayer's request for a 60 day extension on July 13, 1995.

19. On September 6, 1995, the Taxpayer timely filed its protest to Assessment No. 1940766.

20. ITT Tech leases a building containing approximately 21,500 square feet located at 5100 Masthead Street, N.E., Albuquerque, New Mexico 87109.

21. The facility houses classrooms, lecture rooms,laboratories, a learning resource center and its own parking area. The annual rent for the building is approximately $200,000. The computer lab contains approximately 25 computers with CAD (computer aided drafting) software, costing $335,000 loaded on them.

22. During the relevant periods, ITT Tech had an administrative staff of approximately 15 employees assigned to five departments: recruitment, finance, placement, education and maintenance.

23. During the relevant periods, ITT Tech employed the following number of instructors:

Year	Instructors
1991	5
1992	11
1993	10
1994	10
1995	10

24. From 1991 through 1995, ITT Tech instructors held the following post-secondary degrees:

Year	No Degree	AAS	BA or BS
1991	3	0	2

1992	4	1	6
1993	5	1	4
1994	5	2	3
1995	2	3	5

During 1991, one instructor employed also had a master's degree and another instructor also had a PH.D. In 1992, one of the instructors employed also had a master's degree.

25. During the relevant periods ITT Tech had approximately 223 students enrolled each quarter.

26. The payroll for ITT Tech during 1993 was $831,000. Current payroll is approximately $1 million.

27. When ITT Tech commenced in 1989 it offered only one technical post-secondary degree program. That program was electronics engineering technology.

28. From the fall of 1990 to the present, ITT Tech has offered two technical post-secondary degree programs. The second degree program added in 1990 was in computer-aided drafting technology.

29. Prior to 1994, ITT Tech offered only one degree, as Associate of Specialized Technology.

30. The program leading to the Associate of Specialized Technology degree was a one (1) year program.

31. From 1994 to the present, ITT Tech has awarded Associate of Applied Science degrees in both Electronics Engineering Technology and Computer-Aided Drafting Technology.

32. From 1993 to the present, the electronics engineering technology program has been a two (2) year program.

33. From 1993 to the present, completion of the electronics engineering technology program has required a minimum of eight quarters of class work (2 years).

34. From 1993 to the present, the computer-aided drafting program has been an eighteen (18) month program.

35. From 1993 to the present, completion of the computer-aided drafting technology program has required a minimum of six quarters of class work (18 months).

36. Students attend class four hours a day, five days a week. Class sessions run from 8:00 A.M. to 12:00 P.M, 1:00 P.M. to 5:00 P.M, and 6:00 P.M. to 10:00 P.M.

37. Integrated into both programs are "lifelong learning courses" which teach the students oral communications, written communications, economics, critical thinking, problem-solving, how to write resumés, how to handle interviews, proper attire and the like.

38. The staff at ITT Tech also offer the students various support services, such as assisting students in locating housing, part-time employment and car-pooling arrangements, and providing extra tutoring, financial aid services and placement services.

39. Tuition for each program was as follows:

Year	Electronics Program	Drafting Program
1990	$10,922	$10,922
1991	$11,568	$11,568
1992	$11,568	$11,568
1993	$15,359	$13,530
1994	$16,032	$14,136
1995	$17,690	$15,599

40. ITT Tech is fully accredited by the Accrediting Commission of Career Schools and Colleges of Technology (the "ACCSCT").

41. ACCSCT is a national accrediting body located in the Washington, D.C. area. It has responsibility for the accreditation of approximately 750 career school and colleges of technology.

42. The bases for the full accreditation include, among other things, ITT Tech's curriculum, its facilities and its faculty.

43. Accreditation functions are handled at the Taxpayer's corporate headquarters with the exception of occasional site visits by representatives of ACCSCT.

44. ITT Tech has a detailed, standardized curriculum for each of the programs it teaches.

45. The standardized curriculum includes objectives to be taught and mastered each week, weekly lesson plans, lab experiments that must be completed and exams with answer keys.

46. The standardized curriculum utilized by ITT Tech and ITT Technical Institutes throughout the country is developed at the Taxpayer's corporate headquarters by curriculum specialists.

47. The curriculum specialists have either masters or doctorate degrees.

48. To maintain the timeliness and relevancy of its curriculum, the Taxpayer employs a national advisory committee for each of its curriculum areas. These national advisory committees are made up of employer representatives. These representatives allow the Taxpayer to gather information on new developments in technology, new industry trends and practices and on industry needs so that the Taxpayer can modify its curriculum to meet employer needs.

49. The various curricula and related materials are continually reviewed and revised by

these curriculum specialists.

50. Updates to the curriculum for a particular class may be sent to ITT Tech throughout the semester.

51. The uniformity of the Taxpayer's curriculum and its ability to meet employer needs are very important in establishing and maintaining the Taxpayer's excellent reputation for providing a quality education.

52. Because of the uniformity in the curriculum, a student can transfer between the Taxpayer's campuses around the country.

53. The uniformity of the curriculum allows national employers to confidently hire a graduate from any of the Taxpayer's campuses.

54. The Taxpayer's staff at its corporate headquarters chooses the text books that will be used by the students at ITT Tech and in all ITT Technical Institute locations throughout the country.

55. The text books used are text books used in courses taught by others than the Taxpayer and are generally available.

56. The Taxpayer's policies for grades and attendance are developed and implemented on a nationwide basis from the Taxpayer's corporate headquarters.

57. The instructor's job is to teach the curriculum, answer questions with regard to lab experiments and other teaching materials and other curriculum related matters. The instructor must cover the material in the curriculum within the curriculum time deadlines (broken down into material to be covered each week), but the instructor has flexibility with regard to how they choose to cover the material, whether it be by lecture, group discussion, question and answer, class field trips, etc. Instructors also work individually with students, assisting them in selecting their final projects and advising them in the course of their projects, assessing whether the student has weak areas and needs additional tutoring, etc. The instructors are also responsible for grading student projects and examinations and for determining the student's final grade. Instructors spend approximately six

hours a day in contact with students.

58. ITT Tech instructors also administer standardized tests provided from the Taxpayer's corporate headquarters.

59. The tests are designed to be graded by using a template or an electronic scanner.

60. During the audit period tests were graded in New Mexico by ITT Tech employees using a template showing the correct answers.

61. A benefit of a degree from the Taxpayer at any of its technical institutes is education pursuant to the Taxpayer's uniform curriculum.

62. The Taxpayer has never licensed its curriculum. Other institutions sometimes license their curriculum for twenty to twenty-five percent of gross tuition revenue.

63. The Taxpayer spends about $1 million annually on curriculum development and on updating its curriculum.

64. Approximately one percent of the Taxpayer's national enrollment attend its Albuquerque campus.

65. The apportioned cost of curriculum development and maintenance attributable to the Taxpayer's Albuquerque campus is approximately $10,000 per year.

66. When a student enrolls at ITT Tech, ITT Tech personnel gather necessary documentation related to the student's eligibility for financial aid.

67. Applications for government loans and other financial aid are prepared by ITT Tech students with assistance from employees of ITT Tech.

68. ITT Tech employees spend about forty-five minutes with each student who they assist in filling out applications for financial aid.

69. The Taxpayer's staff at corporate headquarters spend, on average, about twenty minutes reviewing each student application for financial aid.

70. The applications are then forwarded to Edtech, a private contractor who runs the

applications through a computerized rating program. The Taxpayer pays Edtech about $65,000 per year to process the applications for all of the Taxpayer's students. Since about one percent of the Taxpayer's students attend ITT Tech, this amounts to a cost of about $650 per year for ITT Tech students.

71. Applications for government loans for ITT Tech students are submitted from the Taxpayer's corporate headquarters on behalf of ITT Tech.

72. Approximately ninety percent of the students at ITT Tech receive some form of financial aid to enable them to attend ITT Tech.

73. The Taxpayer does not charge a separate fee to its students for the assistance it renders in obtaining and processing financial aid applications for its students. Similarly, there is no tuition credit or rebate to those students who do not use the financial aid assistance provided by the Taxpayer.

74. The financial aid assistance offered by the Taxpayer is not available to those who are not students at any of the ITT Technical Institutes.

75. ITT Tech has no direct involvement in the financial aid process other than providing assistance in information gathering and application completion.

76. All government loan applications from ITT Tech students are processed by Bank One in Arizona pursuant to an agreement with the Taxpayer.

77. Payments to or on behalf of ITT Tech students under financial aid programs are sent to the Taxpayer's corporate headquarters.

78. Financial aid services such as disbursing of funds and collection of funds from the funding sources are all provided by the Taxpayer outside of New Mexico.

79. If a federal financial aid grant is received by a student, the Taxpayer receives the payment directly from the federal government at its corporate headquarters.

80. It is to the Taxpayer's financial interest to assist its students with applying for and

receiving financial aid. Otherwise, the Taxpayer would have substantially fewer students able to attend its educational programs. Because the financial aid is paid directly to the Taxpayer, it also ensures that tuition is paid.

81. The Taxpayer is a member of the National Association of Colleges and Employers.

82. Upon completion of the curriculum at ITT Tech, the Taxpayer assists in the job placement of students who wish to avail themselves of that service.

83. ITT Tech graduates, as well as the graduates from any of the Taxpayer's technical institutes, can use the placement service offered by the Taxpayer at any time, anywhere in the country and as many times as the graduate desires, free of charge.

84. The placement services offered by the Taxpayer are not offered or sold separately. Similarly, there is no rebate or tuition credit for students who either do not use the Taxpayer's placement services or who do not find employment through the Taxpayer's placement services.

85. The Taxpayer employs over 50 placement employees throughout the country. Only three of the placement employees are located at the Taxpayer's corporate headquarters.

86. The Taxpayer employs one placement employee at ITT Tech.

87. The great majority (at least 70%) of the students at ITT Tech only desire to locate jobs in the local (New Mexico) job market.

88. Placement employees continually work with employers nationwide to identify job opportunities for the Taxpayer's graduates.

89. The Taxpayer maintains a national database of employers and a career search database for potential job openings at the Taxpayer's corporate headquarters. This database may be used by any of the Taxpayer's graduates.

90. Career search materials are prepared at the Taxpayer's corporate headquarters and are made available to all of the Taxpayer's students around the country.

91. The Taxpayer provides its students job placement services from its corporate

headquarters via electronic mail.

92. The Taxpayer provides packets of information regarding its technical institutes to potential employers. This assists the Taxpayer's students in obtaining employment with those potential employers.

93. The Taxpayer also maintains a national alumni association from its headquarters. The alumni association produces a periodic newsletter which keeps graduates abreast of new developments in their fields and of job opportunities.

94. The Director of Placement located at ITT Tech in Albuquerque acts as a liaison to assist ITT Tech students use the Taxpayer's national placement services and to also provide local job search assistance.

95. The job placement services offered by the Taxpayer and the success of its efforts to place its graduates in jobs are a significant factor in the Taxpayer's effort to recruit potential students to attend its technical institutes. Thus, these services benefit the Taxpayer as well as the graduates receiving the placement services.

DISCUSSION

The Taxpayer operates a vocational school in Albuquerque, which is one of 59 schools it operates nationally. After an audit by the Department, it was determined that although the Taxpayer had reported and paid gross receipts tax on the books and other tangible personal property it sold from its bookstore operation, the Taxpayer had never paid or reported gross receipts tax upon the tuition it received from its students for the educational services provided to them at the Taxpayer's Albuquerque campus. This resulted in an assessment of over $800,000 in gross receipts tax, penalty and interest for the period from January, 1989 through March, 1995.

The Taxpayer has protested the assessment. While the Taxpayer does not argue that it is not subject to gross receipts tax for the educational services it provides at its Albuquerque campus, it argues that the tuition payments it receives may be broken down into payment for various types of

services, some of which are performed in New Mexico, and some of which are performed out-of-state at the Taxpayer's Indianapolis, Indiana corporate headquarters. The Taxpayer argues that it provides three types of services to its New Mexico students: educational services, financial aid services and job placement services. It argues that its educational services may be further broken down into three components, the sale of tangible personal property (books and other educational materials), the provision of instruction, and the preparation of curriculum. The Taxpayer presented evidence that its curriculum preparation, and a portion of its job placement and financial aid services are performed at its corporate headquarters and the Taxpayer presented evidence in support of its contention that these services represent 37% of the services it provides its Albuquerque students. Accordingly, the Taxpayer has requested an apportionment of the tax assessed to reflect an abatement of 37% of the tax, with a corresponding abatement of the penalty and interest to reflect an apportionment of the Taxpayer's receipts between its taxable in-state activities and its non-taxable out-of-state activities.

The Department does not dispute that it is without authority to impose tax on the performance of services which occurs out-of-state, but it disputes the Taxpayer's characterization that the tuition payments it receives from its students represent compensation for the performance of job placement, financial aid or curriculum development services which are separable from the overall educational services which it provides to its New Mexico students. The Department contends that all of the Taxpayer's tuition receipts are receipts from performing educational services in New Mexico and they are thus subject to tax in New Mexico.

The gross receipts tax is imposed, pursuant to NMSA 1978, § 7-9-4, which imposes the tax "for the privilege of engaging in business" upon gross receipts. "Gross receipts" is defined, in pertinent part, at NMSA 1978, § 7-9-3(F) (1995 Repl. Pamp.) as follows:

> "gross receipts" means the total amount of money or the value of other consideration received from selling property in New Mexico, from leasing property 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*. (Emphasis added.)

This definition includes in gross receipts the receipts of taxpayers not only from performing services in New Mexico, but from performing services out-of-state, if the product of the services is initially used in New Mexico. Arguably, this portion of the definition would appear to cover the services the Taxpayer attempts to exclude from taxation in this case, curriculum development, financial aid services and placement services. This part of the definition, however, was enacted by Laws 1989, ch. 262, § 1, effective July 1, 1989, so it would not cover the first six months of the audit period. Additionally, at the same time that this amendment to the definition of gross receipts was enacted, the legislature also enacted NMSA 1978, § 7-9-13.1 which exempts from gross receipts tax the receipts from selling services performed outside New Mexico the product of which is initially used in New Mexico. *See,* Laws 1989, ch. 262, § 4. This exemption from gross receipts tax covers all but a narrow group of research and development services which are not relevant to this inquiry. *See*, NMSA 1978, § 7-9-13.1 (B) (1995 Repl. Pamp.). Because the Department argues that the services the Taxpayer performs are performed in New Mexico and thus fall under the portion of the definition of gross receipts which covers receipts from performing services in New Mexico, and since the first six months of the audit period would not be affected by the amendment to the definition of gross receipts, it will still need to be determined whether all of the Taxpayer's tuition receipts from its New Mexico students can properly be characterized as receipts from the performance of services in New Mexico. Thus, the determination of this matter will still turn upon how the Taxpayer's tuition receipts are characterized. The Taxpayer has also argued that it is performing educational services in interstate commerce and that the Commerce Clause also requires apportionment of its gross receipts to reflect an apportionment between its in-state and its out-of-state activities. As with the first issue, the characterization of the Taxpayer's activities and the location of those activities is critical to the analysis of taxability under the Commerce Clause.

Both parties rely upon the Supreme Court decision in ***Advance Schools, Inc. v. Bureau of Revenue***, 89 N.M. 79, 547 P.2d 562 (1976). In that case, the taxpayer, Advance Schools, Inc.

("ASI") was a vocational correspondence school based in Chicago, Illinois. It maintained two offices in New Mexico with two to six sales representatives who contacted prospective students and assisted them with filling out application forms and retail installment contracts to pay for tuition. After the students were accepted into ASI's program, virtually all contact between ASI and the New Mexico student was conducted by mail or telephone from the taxpayer's offices in Illinois. ASI mailed each student course materials. Exams were mailed to students and mailed back to ASI for grading. ASI monitored the time each student took to complete each course segment and handled problems by correspondence or telephone. Students received counselling by phone from Illinois. After course completion, ASI assisted the students with job placement by recommending them to employers from its Chicago offices. The tuition paid by the students covered the course materials and all of the services related to ASI's correspondence courses the student signed up for.

ASI paid gross receipts tax to the Department on the value of its course materials. The Department assessed ASI gross receipts tax on the entire tuition paid, on the theory that the entire tuition payments represented gross receipts from the sale of tangible personal property in New Mexico. The Commissioner of Revenue and the Court of Appeals upheld the Department's assessment on the basis that the primary activity of ASI was selling educational materials to students within the state and that the services provided were merely incidental to the sale of property in New Mexico. ***Advance Schools, Inc. v. Bureau of Revenue***, 89 N.M. 133, 548 P.2d 95 (Ct. App. 1975). The Supreme Court reversed that decision, ruling that the Commissioner's Decision and Order was not supported by substantial evidence because the court determined that ASI was primarily performing a service, virtually all of which was performed out-of-state.

The Taxpayer relies upon ***Advance Schools***, claiming that its provision of educational services is little different than the provision of educational services by ASI, and citing it for evidence of the apportionability of receipts from providing educational services. Taxpayer Brief in Chief, P. 6. As the Department correctly points out, however, the facts in this case are readily distinguishable

from the manner in which ASI delivered its educational services. ASI had no schools and no teachers in New Mexico and it handled virtually all aspects concerning the delivery of its educational services, including grading papers, monitoring student progress, correction of homework, counseling of students, etc., from its Chicago offices. In this case, the Taxpayer's school and teachers are located in New Mexico, the classes and laboratories are taught here, student progress is monitored here, students are counselled here, and homework and tests are graded here. Although the curriculum is developed out-of-state, it is delivered and taught to the Taxpayer's students in New Mexico.

Additionally, I do not find the Supreme Court decision in ***Advance Schools*** to support the apportionment of tuition receipts for educational services. ASI itself had apportioned its tuition receipts by paying gross receipts tax on the value of the materials it sold to its students in New Mexico, thus apportioning its tuition between the in-state sale of property and the performance of educational services out-of-state. This determination was not at issue in the case.[1] The Supreme Court, however, did not make any attempt to apportion the remaining tuition receipts to reflect an apportionment for ASI's in-state activities, such as the assistance given students in New Mexico by ASI employees with applying for admission, and filling out installment contracts. While the Court's decision provides no guidance as to why apportionment was not considered for these in-state activities, it appears that the Court did not consider that ASI had receipts from providing application and school financing assistance, but rather, that its tuition receipts reflected payment for the educational services being provided by ASI. The other possibility is that the court believed the in-state assistance rendered to be merely incidental to the educational services ASI provided out-of-state. In any event, ***Advance Schools*** supports the Department's position in this case that the Taxpayer's tuition receipts are not subject to apportionment on the basis that there are receipts for services which the Taxpayer performs out-of-state.

[1] Similarly, in this case, the Taxpayer has paid gross receipts tax on its receipts from selling books and tool kits to its students, although those materials are bought separately and are not included in the cost of tuition charged by the Taxpayer.

Also instructive is the decision in ***Mountain States Advertising, Inc. v. Bureau of Revenue***, 89 N.M. 331, 552 P.2d 233 (Ct. App.), *cert. denied* 90 N.M. 8, 558 P.2d 620 (1976). In that case, a Colorado corporation had receipts from displaying advertising messages on billboards it erected and maintained in New Mexico. The sign face was constructed in Colorado and brought to New Mexico for erection. The taxpayer argued that it had no offices, warehouses, salesmen, storage yards, construction facilities or telephone listing in New Mexico and that only ten percent of its cost of doing business was attributable to sign maintenance. It therefore requested an apportionment of ninety percent of its receipts as exempt from gross receipts tax on the basis that this represented receipts for services performed out-of-state. The Court of Appeals denied any apportionment on the basis that the entire service of displaying the advertising was performed in New Mexico. No consideration was given for the work done out-of-state which facilitated or enabled the activity for which the taxpayer charged its customers. In this case, the court focused upon what service was being sold, and where the sale occurred. Undoubtedly, it was of little consequence to the advertisers who sought to have their messages displayed to New Mexico residents that the billboards were fabricated elsewhere than New Mexico. The service being sold was the display of advertising in New Mexico, and that sale took place where the service was performed.

A similar line of reasoning, which focuses on the service contracted for and where it is performed has been developed with respect to the treatment of general and administrative expenses incurred with respect to performing services in New Mexico. In ***United States v. New Mexico***, 581 F.2d 803 (10th Cir. 1978), the United States challenged New Mexico's imposition of gross receipts tax upon Lockheed Electronics Company and RCA Service Company who had cost-plus contracts with the United States for the performance of research and development services at White Sands Missile Range in New Mexico. The primary issue in the case was whether the imposition of New Mexico's tax fell impermissibly upon the United States, in violation of the federal government's immunity from state taxation. The court ruled that the legal incidence of the gross receipts tax was upon the

contractors, and not the United States, and upheld the tax even though the United States bore the economic burden of the tax because it became a reimbursable expense under its contracts. Because the tax was upheld, the United States attempted to shield itself from a portion of cost of the gross receipts tax, contending that a portion of the contract payments were for reimbursement of its contractors' general and administrative ("G&A") expenses which were incurred at Lockheed's headquarters in Arizona or at RCA's headquarters in New Jersey. The United States made the identical argument being made in this case, that there must be an apportionment of gross receipts tax to prevent the imposition of tax upon the portion of the contractors' gross receipts for services which they performed out-of-state. The contracts recognized G&A expenses as a separately reimbursable item and G&A was separately stated on the invoices to the government. The G&A costs were reimbursable under a contract "pool" ratio formula, the reimbursement representing a percentage of the direct reimbursement for work performed in New Mexico. The parties stipulated that the allowable G&A expenses were "the cost of services or items such as management, personnel, financial, marketing, contracting, industrial relations, legal, accounting, payroll, computer and administration." ***Id***. at 805. The Tenth Circuit rejected the government's argument. It held that:

> In this case, the United States has not demonstrated that the G&A reimbursements are for services performed for the United States out-of-state. On the contrary, G&A expenses appear merely to be a component of the price for services performed under the contracts in New Mexico.

Id. at 811.

In arriving at this determination, the Tenth Circuit relied upon the ***Mountain States Advertising*** decision of the Court of Appeals, and it found ***Advance Schools*** to be distinguishable. The Tenth Circuit also found ***Dravo Contracting v. James***, 114 F.2d 242 (4th Cir. 1940), *cert. denied,* 312 U.S. 678, 61 S.Ct 450, 85 L.Ed. 1117 (1941) to be particularly persuasive, quoting from it for the proposition that:

> Only where income arising from a contract performed within the state accrues *upon a separable out-of-state transaction* should it be excluded, as not being income arising from contracting within the state. (Emphasis added.)

Id. 114 F.2d at 247. In the ***Dravo Contracting*** case, the taxpayer was an engineering and contracting firm based in Pennsylvania. It had contracts with the federal government for construction of locks and dams in West Virginia. The taxpayer argued that West Virginia's tax must be apportioned to take into account that it did much work in Pennsylvania, fabricating parts and preparing structural steel and other materials for incorporation into the locks and dams. In rejecting the taxpayer's argument, the court stated:

> The fact that the contractor may have prepared materials in other states for use under the contract is immaterial, if they were used in the performance of the contract in West Virginia and payments made the contractor were dependent upon such use.

Id. 114 F.2d at 246. This language strongly supports the argument made by the Department with respect to the Taxpayer's curriculum development activities which occur at its home office. The Department has argued that the Taxpayer's concept of where a service is provided is fundamentally flawed because if fails to distinguish between the actual provision of the service, which is the activity being taxed, and the activities which are merely preparatory or in support of the provision of the service. The Department argues that curriculum development is merely preparatory to the delivery of educational services in New Mexico. It offers the analogy of a renowned scholar from out-of-state who is paid an honorarium to speak at a university in New Mexico. Even though the scholar may have spent years of study at Harvard gathering the knowledge and information from which her speech was drawn, and even though she may have thought about the contents of her speech during her airline flight to New Mexico, New Mexico is imposing its tax upon the performance of her services in New Mexico, which is the delivery of the speech in New Mexico.

The Department has also promulgated a regulation, which embodies the concepts endorsed in the ***United States v. New Mexico*** and ***Mountain States Advertising*** decisions, Regulation 3(F):65. It provides as follows:

> General administrative and overhead expenses incurred outside New Mexico and allocated to operations in this state for bookkeeping purposes, costs of travel outside New Mexico which travel was an incidental expense of performing services in New Mexico,

> employee benefits, such as retirement, hospitalization insurance, life insurance and the like, paid to insurers or others doing business outside New Mexico for employees working in New Mexico, *and other expenses incurred outside New Mexico which are incidental to performing services in New Mexico*, all constitute the taxpayer's expenses of performing services in New Mexico.
>
> No provision of the Gross Receipts and Compensating Tax Act allows a deduction for expenses incurred in performing services to determine gross receipts subject to tax. Therefore, the total amount of money or reasonable value of other consideration derived from performing services in New Mexico is subject to the gross receipts tax. (Emphasis added.)

As the emphasized language indicates, although the regulation speaks of general and administrative expenses, it is not limited to just expenses which can be so characterized. Any expenses which are incidental to the performance of services in New Mexico are not deductible.

The Taxpayer has strenuously argued that this regulation and the reasoning of ***United States v. New Mexico*** does not apply because it asserts that the services for which is requests apportionment are not general and administrative expenses. It also argues that its curriculum development, job placement and financial aid services are separate and non-incidental services which are being performed out-of-state. Taxpayer's Reply Brief, p.10. I do not agree. Regardless of whether they are examined under the criteria which looks at whether they are incidental to the service upon which tax is being imposed, or whether they are examined under the criteria of being a separable out-of-state transaction, they cannot be sufficiently separated from the Taxpayer's service of providing educational services in New Mexico to require apportionment. The services at issue will each be examined.

The Taxpayer has requested an apportionment of twenty-five percent of its tuition receipts as attributable to its curriculum development activities, which unquestionably occur out-of-state. The Taxpayer supported its percentage allocation by the testimony of its Comptroller, Mr. Gene Baugh, who based that allocation upon his estimate of what other similar institutions charge to sell or franchise their curriculum to others. The Taxpayer does not sell its tuition to any other institutions, it does not sell its curriculum separately to any students and it and does not earmark or differentiate any portion of the tuition it charges for its curriculum development services. Thus, the valuation is

somewhat speculative. The Department points out that the Taxpayer's cost of curriculum development for its Albuquerque campus is only about $10,000 per year, based upon the Taxpayer's estimate of $1 million a year for curriculum development and updating and the fact that only about one percent of the Taxpayer's students are in New Mexico. While I agree with the Taxpayer that the apportioned cost is not necessarily an accurate indicator of the value of the curriculum to the Taxpayer's students, the cost of performing a service is an indicator of value which may be considered, along with other evidence of value. I also found the evidence of value presented by the Taxpayer to be somewhat speculative. There is no need to resolve this discrepancy, however, because I find that there is no separable out-of-state transaction whereby New Mexico is imposing a tax upon the Taxpayer's out-of-state curriculum development activities.[2] The service which the Taxpayer is performing in New Mexico in return for the payment by its students of tuition is the teaching of its curriculum. Although I have no doubt that the Taxpayer's curriculum is excellent and very current, it is but one component of the educational services being delivered by the Taxpayer to its students in New Mexico. For the students, it is doubtful that it is of any consequence where their curriculum was developed or maintained. What is of consequence to them is that it is available to them at the Taxpayer's Albuquerque campus, where it is taught by instructors who will personally deliver it in such a manner that they can understand it, who will grade their exams, oversee their laboratory work and otherwise monitor their learning process to ensure a meaningful educational experience. It is the teaching of its curriculum in New Mexico which is the service the Taxpayer's students are paying for, and which is the service being performed wholly in New Mexico upon which

[2] In this regard, it has been noted above that no portion of the tuition charged is earmarked or invoiced for curriculum development. This is indicative that it is incidental to or a component of the services the Taxpayer is delivering in New Mexico. Even if the Taxpayer were to charge separately for it, however, it would not change the reality of this transaction. In ***United States v. New Mexico***, the contractors also separately invoiced their charges for out-of-state G&A expenses. Nonetheless, the court looked at the reality of the transaction and concluded that these expenses were merely a component of or incidental to the performance of the research and development services which were being performed in New Mexico.

New Mexico imposes its tax. There is no prohibited taxation of services performed out-of-state by New Mexico.

The Taxpayer's job placement services are clearly incidental to its teaching activities with respect to its New Mexico students. The students spend four hours a day, five days a week, for either eighteen months or two years being taught at the Taxpayer's Albuquerque campus, receiving training for their prospective jobs. The Taxpayer's job placement services represent a small fraction of the time and resources committed to their students, teaching them the curriculum. Additionally, the performance of these services are not a separable out-of-state transaction. The amount of tuition the student pays is not dependent upon whether the student uses the services, or uses the services only to locate an in-state job which may have taken little or no involvement of the staff at the Taxpayer's headquarters. While I have no doubt of the benefit which the Taxpayer's job placement services represent, it is a benefit which inures to both the Taxpayer and the student. Not only does the student benefit by the link provided to potential employers, but the success of the Taxpayer's job placement services make it a powerful recruitment tool in attracting students to its program. In this regard, it can be likened to a general and administrative expense which is important to the overall success of the Taxpayer's nationwide business. As such, however, it is merely incidental to the service the Taxpayer is performing for its New Mexico students at its Albuquerque campus, which is teaching them and preparing them for the work force.

The same can be said for the financial aid services rendered by the Taxpayer for its students. Even the Taxpayer's allocation of two percent of its tuition revenues[3] serves as an acknowledgement of how incidental these services are to the overall educational services it is providing. In view of the rather minimal amount of time spent at corporate headquarters handling each student's financial aid transactions when compared to the amount of time teaching the Taxpayer's curriculum to each

[3] I believe even this two percent allocation to be grossly overstated when one compares the time and resources committed to teaching the curriculum as opposed to processing financial aid applications.

student, this service is indeed incidental to the overall educational services being provided students in New Mexico. As with the placement services the Taxpayer provides, the financial aid services also benefit both the student and the Taxpayer. Nearly ninety percent of the Taxpayer's students receive financial aid to enable them to attend ITT Tech. Not only do the students benefit from the financial aid, but the Taxpayer assures itself of a much larger number of students, and since it handles the collection and disbursement of financial aid, it ensures the Taxpayer timely and dependable payment of tuition. In this sense, these activities are also in the nature of a general and administrative expense which, while it is important to the overall functioning of the Taxpayer's business, is incidental to the provision of educational services to the Taxpayer's New Mexico students. Additionally, there is no separable taxable event represented by the provision of these services. The ten percent of students who do not receive financial aid receive no break on their tuition because they do not use these services and the Taxpayer does not offer these services to any persons other than its students. This service is simply included in the overall educational services the Taxpayer provides to its students.

The Taxpayer argues that failure to recognize its curriculum development, job placement and financial aid services as separable and apportionable activities would be contrary to the Department's own treatment of the provision of legal services in Revenue Ruling 410-90-2. This ruling concerned an attorney whose place of business was in Texas and who was licensed to practice law in both New Mexico and Texas. The attorney had recently begun taking cases on contingency fee in New Mexico and in those cases, some work was performed in New Mexico and some in Texas. The Department's ruling was that the attorney was liable for gross receipts tax on the services performed in New Mexico and was exempt for the services performed in Texas. It required the attorney to keep records of the actual time spent on each case and to apportion his receipts to New Mexico based on the actual hours in which service was performed in New Mexico as a percentage of the total hours spent in the performance of legal services on each case.

This ruling is distinguishable from the facts of this case. The service being provided by the

attorney is legal services, which were performed both in Texas and in New Mexico, and were properly apportionable. In this case, the service being provided by the Taxpayer is the teaching of its curriculum in New Mexico. As noted above, it is the delivery of the education to the student in New Mexico which is the service the student contemplates when paying tuition. All of this occurs in New Mexico and is subject to tax by New Mexico.

The Taxpayer has also cited to the definition of service in support of its argument that its services must be apportioned to reflect those performed out-of-state. Specifically, the Taxpayer relies upon the broad and inclusive definition of service:

> ***"Service"*** means ***all activities*** engaged in for other persons for a consideration, which ***activities*** involve predominantly the performance of a service as distinguished from selling of leasing property.... (Emphasis added.)

NMSA 1978, § 7-9-3(K) (Repl. Pamp. 1995) for the proposition that in identifying services, the performance of which are subject to gross receipts tax, each aspect or component of a service must be identified as to what was performed and where it was performed. Taxpayer's Reply Brief, pp. 2-5. The Taxpayer has cited to no authority which supports this interpretation and I have found none. Since enactment, the Gross Receipts and Compensating Tax Act has defined service in this inclusive manner. Service was initially defined, in pertinent part as follows:

> "Service" means all activities engaged in for other persons for a consideration, which activities involve primarily the performance of a service as distinguished from selling property....

Laws 1966, ch. 47, § 3, compiled at NMSA 1953, § 72-16A-3(J). This, or a similarly indistinguishable definition of service was in place when the ***Advance Schools, Mountain States Advertising and U.S. v. New Mexico*** cases were decided and none of those decisions adopted the analysis the Taxpayer urges today. This argument is simply without merit.

The final issue to be determined is whether the application of an unapportioned gross receipts tax to the Taxpayer's tuition receipts runs afoul of the Commerce Clause of the United States Constitution, art. I, § 8, cl. 3. A tax imposed on an activity in interstate commerce will be sustained

if it can pass the four part test announced by the Supreme Court in ***Complete Auto Transit v. Brady***, 430 U.S. 274, 97 S.Ct. 1076, 51 L.Ed.2d 326 (1977), which requires that the tax be applied to an activity with a substantial nexus with the taxing state, be fairly apportioned, not discriminate against interstate commerce and be fairly related to the services provided by the state.

The Taxpayer argues that New Mexico's tax fails the second prong of the ***Complete Auto Transit*** test because New Mexico has failed to apportion it between the Taxpayer's in-state and out-of-state activities. The purpose for the requirement that taxes be fairly apportioned is to ensure that each state taxes only its fair share of an interstate transaction so as to prevent the possibility that a transaction or activity will be subjected to multiple taxation by the various states. A tax satisfies the requirement of fair apportionment if it meets standards of both internal and external consistency. ***Container Corp. of America v. Franchise Tax Board***, 463 U.S. 159, 168, 103 S.Ct 2933, 2942 (1983); ***Goldberg v. Sweet***, 488 U.S. 252, 261, 109 S.Ct. 582, 589 (1989).

Internal consistency is met if an identically structured tax imposed by every state on the same taxable event will result in no multiple taxation. ***Container Corp***., 463 U.S at 169, 103 S.Ct. at 2942; ***Goldberg***, 488 U.S. at 261, 109 S.Ct. at 589. New Mexico's tax meets the test of internal consistency. It is taxing the Taxpayer's receipts from its New Mexico students for the performance of educational services within New Mexico. No other state may impose this same tax. They may tax the Taxpayer's receipts from students in their own state for services performed within their state, but they cannot tax the Taxpayer's receipts from its New Mexico students. Nor may Indiana impose a tax upon the Taxpayer's receipts from its New Mexico students. There is no sale of educational services which occurs in Indiana. These services are sold in New Mexico when the students pay their tuition in order to be taught in New Mexico. The teaching occurs in New Mexico and this is the only place where it may be taxed. There is simply no possibility of double taxation and the taxpayer has failed to demonstrate that such may occur.

External consistency requires that each state tax only that portion of the revenues which

"reasonably reflects the in-state component of the activity being taxed." ***Goldberg***, 488 U.S. at 262, 109 S.Ct. at 589. External consistency is met in this case because New Mexico is taxing the Taxpayer's receipts from its New Mexico students which they pay in order to be taught at the Taxpayer's Albuquerque facility. All of the teaching occurs in New Mexico and, appropriately, all of it may be taxed by New Mexico.

Particularly instructive with respect to meeting the requirements for external consistency is the Supreme Court's recent decision in ***Oklahoma Tax Commission v. Jefferson Lines, Inc***., 115 S.Ct 1331 (1995). The issue in that case was whether Oklahoma would be allowed to impose its tax on 100 percent of the taxpayer's revenues from selling bus tickets in Oklahoma for travel to out-of state destinations. The taxpayer had argued that such a tax must be apportioned in proportion to the in-state versus out-of-state mileage of the travel to satisfy the fair apportionment requirement of the Commerce Clause. The Court, however, did not require a segregation of the tax to differentiate the in-state component of the bus line's services from the out-of-state component and it found Oklahoma's tax to be externally consistent. The Court found that the tax was imposed on the purchase of transportation services and the purchase transaction occurred wholly in Oklahoma. The fact that no other state could impose a tax on the same transaction satisfied the court that apportionment was not required.

In this case, the Department is taxing the Taxpayer's receipts from the performance of educational services in New Mexico. These services are performed wholly in New Mexico when the Taxpayer teaches its curriculum to its New Mexico students at its Albuquerque facility. This is what the New Mexico students are paying for and this is what is delivered in return for such payment. The development of curriculum is not separable from the delivery of that curriculum when it is taught, and that teaching occurs in New Mexico. The placement services and financial aid services represent an insignificant part of the total educational services which the Taxpayer provides to its students at its New Mexico campus and are incidental to the provision of an excellent education, which is what the

Taxpayer's students are paying their tuition for. The imposition of New Mexico's gross receipts tax on all of the Taxpayer's tuition receipts is upheld.

CONCLUSIONS OF LAW

1. The Taxpayer filed a timely, written protest to Assessment No. 1940766 and jurisdiction lies over both the parties and the subject matter of this protest.

2. New Mexico's gross receipts tax applies to receipts from services performed in New Mexico.

3. The services which the Taxpayer provides to its students in return for the payment of tuition at its Albuquerque campus is the teaching of its curriculum. These services are provided entirely in New Mexico and are subject to gross receipts tax.

4. The development of the Taxpayer's curriculum is but a component of and is not a separable transaction from the teaching of that curriculum to the Taxpayer's students in New Mexico.

5. The job placement services and financial aid services provided by the Taxpayer to its New Mexico students are merely incidental to and in support of the educational services the Taxpayer provides when it teaches its curriculum in New Mexico.

6. The imposition of New Mexico's gross receipts tax upon 100% of the taxpayer's tuition receipts from its New Mexico students does not violate the Commerce Clause of the United States Constitution.

For the foregoing reasons, the Taxpayer's protest IS HEREBY DENIED.

DONE, this 15th day of January, 1997.