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

IN THE MATTER OF THE PROTEST OF
**QUALITY INN;** I.D. No. 02-071104-00 2 No. 96-30
ASSESSMENT NO. 1900351

## DECISION AND ORDER

This matter came on for formal hearing before Gerald B. Richardson, Hearing Officer, on December 18, 1996. The Quality Inn, hereinafter, "Taxpayer," was represented by Mr. Duane Gray, its general manager. The Taxation and Revenue Department, hereinafter, "Department," was represented by Margaret B. Alcock, Special Assistant Attorney General. Based upon the evidence and the arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

## FINDINGS OF FACT

1. The Taxpayer operates a motel in Santa Fe, New Mexico under a franchise agreement with Quality Inn.

2. As part of its agreement with Quality Inn, the Taxpayer is required to have a restaurant on the premises.

3. On January 15, 1990 the Taxpayer entered into a lease agreement with Santa Fe Cantina, Inc., a New Mexico corporation, (hereinafter, the "tenant") for the lease of the restaurant portion of the Quality Inn. The lease was for a term of five years, commencing February 1, 1990. Included in the property leased was Liquor License No. 94, issued by the state of New Mexico. The lease called for monthly rental payments of $500 per month for the first two years of the lease, with rent to increase to 6% of the gross income of the tenant, or $1,800 per month, whichever is greater, for the remaining term of the lease.

4. After a little more than a year into the lease, the tenant stopped making its monthly rental payments. In the process of working with the tenant to resolve the back rent issue, the

Taxpayer also found out that the tenant owed various other creditors, about $10,000. Among those creditors were the liquor distributors who supplied alcoholic beverages to the tenant for sale and the companies supplying utilities, such as electricity and gas, to the tenant.

5. The Taxpayer, as owner of the liquor license, was financially responsible for the unpaid bills owing to the liquor distributors.

6. Since the utilities for the restaurant were in the Taxpayer's name and not the tenant's, the Taxpayer was also financially responsible for the unpaid utility bills.

7. In August of 1991, the Taxpayer and the tenant agreed to modify the terms of the lease agreement whereby the $500 monthly rental payment to the Taxpayer would be waived and the monies would be applied to paying off the tenant's other obligations, such as those to the liquor distributors and the utility companies.

8. Under this arrangement, the tenant's creditors were paid off over time and the Taxpayer monitored the tenant's activities so as to ensure that further indebtedness would not be accumulated for which the Taxpayer would become liable.

9. Eventually, in November of 1994, the tenant agreed to vacate the leased premises because it was not able to make a financial go of its restaurant and lounge operations.

10. In November of 1994, the Taxpayer entered into a new lease arrangement with a new tenant for the lease of the restaurant premises and liquor license. Under the terms of this agreement, the tenant pays a monthly rental of $1.00 per month.

11. In the process of applying for a tax clearance from the Department for Liquor License No. 94 to be leased to another person, the Department learned from the Taxpayer that because it was not receiving any rental payments from its tenant under its lease agreement, that the Taxpayer had not reported and paid any gross receipts taxes on the value of leasing its liquor license and restaurant premises.

12. The fair market value for leasing a liquor license in Santa Fe during the time period at

issue was at least $1,000 per month.

13. Based upon the information the Department received from the Taxpayer, on February 13, 1995 the Department issued Assessment No. 1900351 to the Taxpayer, assessing $1,045.56 in gross receipts taxes, and $240.80 in interest for the reporting periods of January, 1992 through December, 1994. The Department's assessment was based upon an imputed value of $500 per month for the lease of the liquor license.

14. On February 14, 1995 the Taxpayer filed a written protest with the Department to Assessment No. 1900351.

## DISCUSSION

The issue to be determined herein is the propriety of the Department's assessment of gross receipts tax upon an imputed value to the Taxpayer of gross receipts from the rental of its liquor license.

Mr. Gray, the Taxpayer's general manager, has diligently and honestly paid gross receipts taxes with respect to actual money received from the operation of the Quality Inn in Santa Fe, but he disputes that there was any benefit to the Taxpayer or any value gained by the Taxpayer upon which gross receipts tax is due with respect to its lease of its liquor license, where no rental payments were received from his tenant.

The gross receipts tax is imposed, pursuant to NMSA 1978, § 7-9-4(A) (1995 Repl. Pamp.), which provides:

> For the privilege of engaging in business, an excise tax equal to five percent of *gross receipts* is imposed on any person engaging in business in New Mexico. (emphasis added)

"Gross receipts" is defined at NMSA 1978, § 7-9-3(F) in pertinent part 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. *In an exchange in which the money or other consideration received does not represent the value of the property or service exchanged, "gross receipts" means the reasonable value of the property or service exchanged. . .* (emphasis added)

The Department bases its assessment of gross receipts tax on the basis that the actual money exchanged for the lease of the liquor license, in this case, nothing, does not represent the reasonable value of the lease of a liquor license. It has attempted to arrive at what it considered to be a reasonable value for the lease of the liquor license between the tenant and the Taxpayer, and imputed a value as gross receipts to the Taxpayer. Essentially, the issues presented for resolution are whether the Department may assess gross receipts tax on a basis other than actual money exchanged and whether the value determined by the Department as the value of the liquor license lease is reasonable as a value upon which to assess gross receipts tax.

The answer to the first issue presented is clear from the language of Section 7-9-3(F) which authorizes the Department to treat as "gross receipts" not only any money exchanged, but also "the value of other consideration" received. "Consideration" is defined in the regulations issued by the Department interpreting the gross receipts tax statutes at 3 NMAC 2.1.7.2 as follows:

> "Consideration" is any benefit, interest, gain or advantage to one party, usually the seller, or any detriment, forbearance, prejudice, inconvenience, disadvantage, loss of responsibility, act or service given, suffered, or undertaken by the other party, usually the buyer.

In this case, the Department argues that although the Taxpayer did not receive any money in consideration of its lease of the liquor license, it has received a benefit, which qualifies as consideration. It argues that the Taxpayer benefitted in several respects by allowing its tenant to continue to lease the Taxpayer's liquor license. It received the benefit of having the tenant pay off its liquor distributor and utility creditors. If those liabilities had not been satisfied by the tenant, the Taxpayer would have been responsible for payment of those liabilities. The Department argues that the Taxpayer also benefitted by having someone else operate the restaurant, relieving the Taxpayer of that responsibility, which it would have otherwise had to shoulder in order to fulfill its obligations under its franchise agreement with Quality Inn.

I have no doubt that the Taxpayer did receive some benefit from allowing the tenant to continue to have the use of the Taxpayer's liquor license. Clearly, having the liabilities for which it

could be held responsible satisfied, was a benefit to the Taxpayer. The Taxpayer was also benefitted by having the tenant operate the restaurant. The Taxpayer needs to have a restaurant on its premises to fulfill its franchise agreement with Quality Inn. Mr. Gray also admitted that potential customers of the motel also regularly inquire whether the motel has a restaurant on premises. Thus, the presence of the restaurant is of benefit to the Taxpayer's overall motel business. In response to this argument, the Taxpayer argued that it wasn't really benefitted, because it could have chosen to operate the restaurant itself. While the Taxpayer could have done so, it chose not to do so, presumably for some good reason. It certainly would have involved some more management responsibility to oversee not only the operation of the motel, but also to operate the restaurant. Thus, there was at least some administrative convenience to having an outside party take responsibility for operating the restaurant.

The Department is also clearly authorized to impute a value as gross receipts by the language in Section 7-9-3(F) quoted above which provides that gross receipts means the "reasonable value of the property or service exchanged" when the money or other consideration exchanged does not represent the value of the property or service exchanged. Thus, the remaining issue to be determined is whether the Department's determination of a value of $500 per month is reasonable. The Department has a regulation and an example which illustrate the operation of this provision of Section 7-9-3(F). Regulation 3 NMAC 2.1.14.4 provides as follows:

> In a transaction where the actual consideration received does not represent the fair market value of the property sold or leased or of the service sold, the fair market value shall be included in the gross receipts of the seller or lessor. Fair market value is the value which the property or service can command in an arms length transaction between two independent parties in an open market.

The example given to illustrate the application of Section 7-9-3(F) with respect to consideration less than fair market value follows:

> Example: X, a land and cattle company, is a corporation which is affiliated with Y, an equipment company. Because of their affiliation, X leases a $30,000 tractor from Y for $1.00 a month. Y reports that its gross receipts from this transaction are $1.00. Y's gross receipts are the market value of a monthly lease of a $30,000 tractor. Y must pay gross receipts tax on the adjusted amount.

The Department presented the testimony of Mr. David Fergeson, an Assistant Bureau Chief who is responsible for issuing liquor license tax clearances for the Department. Mr. Fergeson testified that he consulted with Mr. Hill Davidson, a broker for liquor licenses, as to the going rate in Santa Fe during the assessment period to lease a liquor license. Mr. Davidson said that it was at least $1,000 per month. Mr. Fergeson testified that he also took the lease agreement between the Taxpayer and its tenant into consideration in setting the value for purposes of the Department's assessment and to be on the safe side, and to give the Taxpayer the benefit of the doubt, he used the $500 per month amount.

Mr. Gray presented no evidence to dispute the figures testified to by Mr. Fergeson other than that he did not receive the $500 a month and that he presently leases the license and the premises for $1.00 per month. While this evidence is some evidence of value, it fails to prove that Mr. Davidson's figure was erroneous for the Santa Fe market and it fails to take into consideration the well known fact that liquor licenses in New Mexico are a highly valuable commodity. Additionally, it fails to account for the other benefit which the Taxpayer received by its forbearance from collecting its lease revenues, the payment of the liquor distributor and utility liabilities which it could be held responsible for. Taxpayer's Exhibit 2 established that at the time the Taxpayer and the Tenant arrived at their agreement to waive the cash rental, the liquor distributor creditors were owed approximately $4,700. The utility bills were mentioned in the exhibit but the amounts owed were not noted. The Taxpayer did not present any quantification of those amounts other than to note his general recollection that about $10,000 was owed by the tenant to its various creditors at the time the agreement to waive the monthly rental was made.

NMSA 1978, § 7-1-17(C) provides that there is a presumption of correctness to an assessment of taxes by the Department. This means that a taxpayer disputing the assessment bears the burden of proving that the assessment is incorrect. In this case, the Department presented evidence to support the reasonableness of its determination of value for the lease of the Taxpayer's liquor license. The

Taxpayer has failed to present sufficient evidence to dispute the value determined by the Department and to overcome the presumption of correctness. Based upon the evidence presented, the $500 per month of imputed value appears to be a very reasonable, if not low, estimate of the value of the liquor license leased by the Taxpayer.

## CONCLUSIONS OF LAW

1. The Taxpayer filed a timely, written protest to Assessment No. 1900351, pursuant to NMSA 1978, § 7-1-24 and jurisdiction lies over both the parties and the subject matter of this protest.

2. When the money exchanged in a transaction does not represent the reasonable value of the good or service exchanged, the Department is authorized to determine a reasonable value as consideration for the transaction and to impose gross receipts tax on such value.

3. The Department's determination that the reasonable value of the Taxpayer's gross receipts from the lease of its liquor license is $500 per month is supported by substantial evidence which the Taxpayer has failed to sufficiently rebut.

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

DONE, this 30th day of December, 1996.