

**STATE OF NEW MEXICO
ADMINISTRATIVE HEARINGS OFFICE
TAX ADMINISTRATION ACT**

**IN THE MATTER OF THE PROTEST OF
MOUNTAIN LIQUORS LLC AS SUCCESSOR TO
TRAIL HOUSE ENTERPRISES LLC
TO ASSESSMENT ISSUED UNDER LETTER
ID NO. L1155313712**

No. 16-15

DECISION AND ORDER

A protest hearing occurred on the above captioned matter on December 28, 2015 before Brian VanDenzen, Esq., Chief Hearing Officer, in Santa Fe. At the hearing, Jeremy Peck appeared *pro se* for Mountain Liquors, LLC (“Taxpayer”). Staff Attorney Gabrielle Dorian appeared representing the State of New Mexico Taxation and Revenue Department (“TRD”). Protest Auditor Veronica Galewaler appeared as a witness for TRD. TRD Staff Attorney Marek Grabowski also appeared as an observer. Taxpayer Exhibits #1-6 were admitted into the record. Taxpayer Ex. #6 is a sealed record involving another taxpayer’s confidential information. TRD Exhibits A1, A2, C, D & E were admitted into the record (TRD Ex. C was resubmitted on May 11, 2016 minus the handwritten notations that Taxpayer had objected to at hearing). All exhibits are more thoroughly described in the Administrative Exhibit Coversheet. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. On September 9, 2015, under letter id. no. L1155313712, TRD assessed Taxpayer as a successor in business to Trail House Enterprise LLC for \$5,513.39 in tax, \$1,183.26 in penalty, and \$151.30 in interest for a total assessment of \$6,847.95.

2. TRD included with the assessment a detailed spreadsheet listing the tax, penalty and interest for each tax reporting period.
3. On September 22, 2015, Taxpayer protested TRD's assessment.
4. On September 29, 2015, TRD's protest office acknowledged receipt of a valid protest.
5. On November 5, 2015, TRD filed a request for hearing in this matter with the Administrative Hearings Office (a separate agency from TRD under the Administrative Hearings Office Act, NMSA 1978, Section 7-1B *et seq* (2015)).
6. On November 6, 2015, the Administrative Hearings Office sent Notice of Administrative Hearing, scheduling this matter for a merits hearing on December 28, 2016, within 90-days of TRD's acknowledgment of receipt of a valid protest.
7. Taxpayer is a limited liability company operated by its sole member Jeremy Peck.
8. Mr. Peck is also the sole member of Trail House, LLC, an entity also owning an interest in the commercial property described in finding of fact #9. [Taxpayer Ex. #3].
9. Taxpayer, in conjunction with Trail House LLC, owns commercial property at 10902 Highway 4, Jemez Pueblo, New Mexico, 87024.
10. Taxpayer also possessed a liquor license used at that property.
11. Taxpayer, apparently in conjunction with Trail House LLC, operated a grocery store, liquor store, and deli at that property it owned during the first eight of the eleven years that Taxpayer owned the property.
12. Trail House Enterprise, LLC (a separate entity from Trail House, LLC) is a New Mexico limited liability company operated by Nick and Ilie Spilca.

13. On February 22, 2012, Taxpayer entered into a lease agreement with Trail House Enterprise LLC whereby Taxpayer leased its commercial property in Jemez to Trail House Enterprise LLC. [Taxpayer Ex. #3].

14. Under the property lease agreement, Trail House Enterprise LLC was liable for the payment of all federal, state, and local tax. Failure to timely pay these taxes was a grounds for default under the agreement.

15. Nick and Ilie Spilca executed a personal guarantee to Taxpayer for any debt of Trail House Enterprise LLC under the lease agreement with Taxpayer. This guarantee also granted Taxpayer a security hold against any of Nick and Ilie Spilca assets against a debt under the lease. [Taxpayer Ex. #1].

16. Taxpayer leased its liquor license to Trail House Enterprise LLC. [Taxpayer Ex. #2].

17. Under the liquor license lease, Trail House Enterprise LLC was liable for the payment of all federal, state, and local tax, including penalty and interest. Failure to pay such taxes was grounds to default the liquor license lease.

18. After entering into the various leases in 2012, Trail House Enterprise LLC took over the operation of the grocery store, liquor store, and deli commercial business located in Jemez.

19. With the assistance of Taxpayer, Trail House Enterprise LLC made or attempted to make improvements to the store, liquor store and deli. Taxpayer would provide credit against rent for some of these improvements, although in retrospect Trail House Enterprise LLC did not always fully complete the improvement projects.

20. Trail House Enterprise LLC fell significantly behind on the payment of its gross receipts tax obligations (Taxpayer was seven reporting periods behind) from the commercial businesses operated at the rented property and the liquor excise tax associated with the liquor license it was renting from Taxpayer.

21. Trail House Enterprise LLC also fell significantly behind on the payments under the leases to Taxpayer.

22. Sometime on or before February 16, 2015, Taxpayer met with Nick and Ilie Spilca of Trail House Enterprise LLC about the rental payment delinquencies. At the time, Nick and Ilie Spilca informed Mr. Peck that they had fallen behind financially and wished to voluntarily terminate the lease agreements.

23. At that meeting, Taxpayer provided Nick and Ilie Spilca with three-days notice of eviction based on their default under the lease.

24. On February 16, 2015, Illie Spilca of Trail House Enterprise LLC informed in writing Taxpayer that it was breaking the lease with Taxpayer. [Taxpayer Ex. #4].

25. As part of the termination of the lease agreements, Taxpayer and Trail House Enterprise LLC agreed to conduct a full inventory of all merchandise at the property.

26. The inventory of the all of Trail House Enterprise LLC's inventory contained on the property revealed a total wholesale value of the inventory of \$20,153.71. [TRD Ex. A-1].

27. About 46% of the inventory amounted to liquor and beer of the on-site liquor store while about 53% was general merchandise attributable to on-site grocery store. [TRD Ex. C].

28. It originally cost Taxpayer over \$200,000.00 for the liquor license it leased to Trail House Enterprise LLC, and Taxpayer rented that liquor license out for \$2,000.00 per month.

29. Upon termination of the leases, Taxpayer took possession of its property in Jemez, the liquor license that Trail House Enterprise LLC had previously leased, and Trail House Enterprise LLC's inventory at the property.

30. Taxpayer paid Trail House Enterprise LLC \$4,000.00 for the inventory. This inventory total included grocery items transferred to Trail House LLC, and liquor items that transferred to Mountain Liquors, LLC. [TRD Ex. A-1].

31. This transfer of inventory did not occur in the regular course of Taxpayer's business, but rather as a mechanism for Taxpayer to preserve the value of the commercial businesses located at the property and to collect on some of Trail House Enterprise LLC's debts Taxpayer.

32. Using Trail House Enterprises LLC's inventory and the liquor license obtained upon the termination of the leases, Taxpayer operated the established grocery store, liquor store, and deli located on Taxpayer's commercial property for at least ten-months.

33. Taxpayer used some of the same signage as when Trail House Enterprises LLC's operated the business. [TRD Ex. E & D].

34. In order to protect the value of the businesses, Taxpayer paid off some of Trail House Enterprise LLC's outstanding liabilities to National Distributing, Windstream, and TRD. [TRD Ex. A-1].

35. Taxpayer retook possession of its liquor license as part of the default under the lease. In order to preserve the liquor license and in order to continue operating, Taxpayer paid off

the outstanding Liquor Excise Tax liability that Trail House Enterprise LLC had accrued with TRD.

36. Although Mr. Peck asserted at hearing that when Taxpayer paid off the outstanding Liquor Excise Tax liability associated with the liquor license it was informed that extinguished all liability, there is no evidence that a TRD employee in fact told Mr. Peck that the outstanding tax liability was extinguished when Taxpayer paid the outstanding liquor excise tax to clear the liquor license. [Taxpayer Ex. #5].

37. Because there was no clean copy of TRD Ex. C in the administrative file without the handwritten notes that Taxpayer objected to, on May 6, 2016 AHO's legal assistant emailed both Taxpayer's representative Mr. Peck and TRD's Representative Ms. Dorian directing that the exhibit be resubmitted. With no objection noted, on May 11, 2016, TRD provided a clean copy of TRD Ex. C.

DISCUSSION

The issue in this case is whether Taxpayer was a successor in business of Trail House Enterprises LLC and thus liable for the assessed successor in business tax. Although TRD assessed penalty and interest and continued to argue that penalty and interest was appropriate in this matter, such argument is not consistent with the recent clear holding by the Court of Appeals in *Hi-Country Buick GMC, Inc. v. Taxation and Revenue Dep't*, 2016-NMCA-027, ¶20, *cert denied*, March 15, 2016, No. S-1-SC-35647, 2016 N.M. Lexis 67. As such, as a threshold matter, the protest of penalty and interest in this matter is granted and that portion of the assessment is abated.

Presumption of Correctness.

Under NMSA 1978, Section 7-1-17 (C) (2007), the assessment issued in this case is presumed correct. Consequently, Taxpayer has the burden to overcome the assessment. *See Archuleta v. O'Cheskey*, 1972-NMCA-165, ¶11, 84 N.M. 428. Accordingly, it is Taxpayer's burden to present some countervailing evidence or legal argument to show that it is entitled to abatement, in full or in part, of the assessment issued against it. *See N.M. Taxation & Revenue Dep't v. Casias Trucking*, 2014-NMCA-099, ¶8. "Unsubstantiated statements that the assessment is incorrect cannot overcome the presumption of correctness." *See MPC Ltd. v. N.M. Taxation & Revenue Dep't*, 2003 NMCA 21, ¶13, 133 N.M. 217; *See also* Regulation 3.1.6.12 NMAC. When a taxpayer presents sufficient evidence to rebut the presumption, the burden shifts to TRD to show that the assessment is correct. *See MPC Ltd.*, 2003 NMCA 21, ¶13.

Successor in Business.

NMSA 1978, Section 7-1-61 (B) (1997) establishes that the "tangible and intangible property used in any business remains subject to liability for payment of the tax due on account of that business to the extent stated herein, even though the business changes hands." Section 7-1-61 (C) requires the successor to place into a trust account sufficient money to cover the outstanding tax liability until TRD either issues a clearance certificate or makes a demand or assessment for the outstanding liability. Under Section 7-1-63 (C), the successor can "discharge as assessment made... by paying to the Department the full value of the transferred tangible and intangible property."

Regulation 3.1.10.16 NMAC (1/15/01) addresses what constitutes a successor in business for the purposes of the TAA. *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). Regulation 3.1.10.16 (A) NMAC establishes eight indicia in determining whether a business is a successor:

- (1) Has a sale and purchase of a major part of the materials, supplies, equipment, merchandise or other inventory of a business enterprise occurred between a transferor and a transferee in a single or limited number of transactions?
- (2) Was a transfer not in the ordinary course of the transferor's business?
- (3) Was a substantial part of both equipment and inventories transferred?
- (4) Was a substantial portion of the business enterprise that had been conducted by the transferor continued by the transferee?
- (5) By express or implied agreement did the transferor's goodwill follow the transfer of the business properties?
- (6) Were uncompleted sales, service or lease contracts of the transferor honored by the transferee?
- (7) Was unpaid indebtedness to suppliers, utility companies, service contractors, landlords or employees of the transferor paid by the transferee?
- (8) Was there an agreement precluding the transferor from engaging in a competing business to that which was transferred?

If any of these eight indicia are present, then TRD “may presume that ownership of a business enterprise has transferred to a successor in business.” *See* Regulation 3.1.10.16 (B) NMAC.

In this case, at least four of the factors under Regulation 3.1.10.16 (B) NMAC are met. A substantial portion of the grocery and liquor inventory of Trail House Enterprises, LLC transferred to Taxpayer when the leases were terminated. Taxpayer needed that inventory to try to keep the businesses afloat and pay off outstanding liabilities accrued by Trail House Enterprises, LLC. The transfer did not occur in the regular course of Taxpayer’s business but as part of a default on the various lease agreements. Taxpayer continued the grocery, liquor store, and deli operation at the same location in Jemez. Taxpayer paid the unpaid indebtedness of Trail House Enterprises LLC to suppliers and TRD. Thus, for the purposes of the Tax Administration Act, Taxpayer was presumed to be a successor in business of Trail House Enterprises LLC.

The purpose of the successor in business statute is “to make tangible and intangible property security for payment of the tax.” *Sterling Title Co. v. Comm'r of Revenue*, 1973-NMCA-086, ¶23, 85 N.M. 279. In other words, the tax liability of the predecessor business follows the tangible and intangible assets to the successor business. According to Judge Sutin’s concurring opinion in *Sterling Title Co.*, ¶28, under the successor in business statutory scheme, “[t]he burden is placed on the purchaser, at the time of the purchase of tangible and intangible property used in a business, to determine whether a gross receipts tax is due and payable by the seller.” Although Mr. Peck was understandably frustrated and questioned why the state pursued him rather than the Spilcas who collected the tax but failed to remit it to the state, the answer to that complaint is found in the structure and purpose of the statute: the state follows the assets of the defunct business to collect on the outstanding liability.

Taxpayer argued that he was simply perfecting a credit interest on the seized inventory and thus was not a successor pursuant to Regulation 3.1.10.16(F)(2) NMAC. Under Regulation 3.1.10.16 (F) (2) NMAC, a successor means “any transfer of a business or property of a business, except to the extent it would be materially inconsistent with the rights of secured creditors that have perfected security interests or perfected liens on the business or property of the business.” Excluded from the definition of a successor in business under Regulation 3.1.10.16 (F) (2) NMAC is “a disinterested third party who purchases property at a commercially reasonable foreclosure sale, a bank or other financial institution or government that acquires and operates a business for a limited period of time in order to protect its collateral for eventual resale in a commercially reasonable manner...” Taxpayer is not bank, other financial institution, or government, and thus this provision does not appear to apply to the facts of this case. *See Hi-Country Buick GMC, Inc.*, 2016-NMCA-027, ¶17. Nor was Taxpayer a disinterested third party,

as Taxpayer had operated the businesses at the commercial property for eight years before Trail House Enterprises LLC took over the property and businesses under the leases. Although Mr. Peck expressed an interest in eventually selling the property, at the time of the hearing Taxpayer had already been operating the commercial businesses at the property for ten-months. Considering he had previously operated these businesses for eight years, this subsequent operation of the businesses is not consistent with the type of disinterested party mentioned in Regulation 3.1.10.16 (F) (2) NMAC or the purpose of that regulation. *See id.*

In this case, Taxpayer cited numerous agreements that required Trail House Enterprises, LLC to pay the tax obligations of the business. However, while Taxpayer is certainly free to pursue a contractual legal action against Trail House Enterprises, LLC, agreements between third parties regarding taxes do not prohibit TRD from pursuing a tax liability under the Tax Administration Act. As discussed above, under the structure and purpose of the successor in business provision of the Tax Administrative Act, TRD follows the assets of a business, which in this case it is undisputed that the assets transferred to Taxpayer. But that does not preclude Taxpayer from subsequently enforcing its own legal rights against Trail House Enterprises, LLC and/or the Spilcas.

The final issue raised after closing argument was whether TRD issued the assessment to the correct successor entity: Taxpayer or the other entity that Mr. Peck is a member of, Trail House LLC. While initially there was some argument about this point, the record clearly established that Taxpayer took control of the liquor and beer inventory and the liquor license from Trail House Enterprises, LLC and used these assets to continue to operate the liquor store. The successor factors under Regulation 3.1.10.16 (A) NMAC were equally present for the liquor portion of the business. The transferred liquor and beer assets amounted to approximately 46%

percent of the \$20,153.71 in inventory that Taxpayer took possession of in this case. That value of the inventory exceeds the assessed successor tax liability. While Taxpayer had to pay TRD the outstanding Liquor Excise Tax liability to maintain the liquor license, that is a distinct tax different separate from the assessed successor tax liability associated with the unpaid gross receipts tax. While Mr. Peck argued that he was told paying the Liquor Excise Tax would extinguish his liability, the emails exchanges he had with Department employees in Taxpayer Ex. #5 do not support that assertion. *See MPC Ltd. v. N.M. Taxation & Revenue Dep't*, 2003 NMCA 21, ¶13 (“Unsubstantiated statements that the assessment is incorrect cannot overcome the presumption of correctness.”). Taxpayer did not overcome the presumption of correctness that attached to the assessment with regard to the successor liability tax. Thus, with the exception of penalty and interest, TRD’s assessment was appropriate.

CONCLUSIONS OF LAW

A. Taxpayer filed a timely, written protest to TRD’s assessment, and jurisdiction lies over the parties and the subject matter of this protest.

B. The hearing was timely set and held within 90-days of protest under NMSA 1978, Section 7-1B-8 (2015).

C. The assessment of penalty and interest against Taxpayer as a successor in business of Trail House Enterprises LLC is not legally supported in light of the clear contrary holding of *Hi-Country Buick GMC, Inc. v. Taxation and Revenue Dep’t*, 2016-NMCA-027, ¶20, *cert denied*, March 15, 2016, No. S-1-SC-35647, 2016 N.M. Lexis 67. Therefore, Trail House Enterprises LLC’s penalty and interest assessed against Taxpayer must be abated.

D. The liability of a defunct business follows the tangible and intangible assets transferred to a different business. *Sterling Title Co. v. Comm'r of Revenue*, 1973-NMCA-086, ¶23, 85 N.M. 279.

E. Because four of the eight factors articulated under Regulation 3.1.10.16 (A) NMAC were present, it was presumed under that regulation that Taxpayer was a successor in business under NMSA 1978, Sections 7-1-61 through 63 up to the value of the transferred assets.

F. Taxpayer did not overcome the presumption of correctness under the assessment. *See* NMSA 1978, Section 7-1-17 (C) (2007) and *Archuleta v. O'Cheskey*, 1972-NMCA-165, ¶11, 84 N.M. 428.

G. Taxpayer was not a bank, a financial institution, or a government institution, and thus not excluded from the definition of successor in business under Regulation 3.1.10.16 (C) (2) NMAC. *See Hi-Country Buick GMC, Inc.*, 2016-NMCA-027, ¶17.

For the foregoing reasons, the Taxpayers' protest **IS PARTIALLY GRANTED AND IS PARTIALLY DENIED. IT IS ORDERED** that TRD abate the assessed penalty and interest totaling \$1,334.56 pursuant to the holding in *Hi-Country*. **IT IS ORDERED** that the Taxpayer is liable for the remaining successor in business tax liability of \$5,513.39.

DATED: May 11, 2016.

Brian VanDenzen
Chief Hearing Officer
Administrative Hearings Office
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