STATE OF FLORIDA
DIVISION OF ADMINISTRATIVE HEARINGS

BEACHSIDE INN DESTIN, INC.,	)	
	)	
Petitioner,	)	
	)	
vs.	)	Case Nos. 05-1262
	)	05-1263
DEPARTMENT OF REVENUE,	)	05-2261
	)	
Respondent.	)	
______________________________	)	

SUMMARY RECOMMENDED ORDER

This case was scheduled for hearing July 5 and 6, 2006. On July 3, 2006, the parties filed Motions for Summary Recommended Order and filed stipulated facts and exhibits. On July 5, 2006, the undersigned entered an Order Canceling Hearing and advised the parties that a Recommended Order would be prepared based on the stipulated facts and exhibits and written submissions of the parties. The authority for conducting the proceeding is set forth in Sections 120.569 and 120.57(1), Florida Statutes. The case was considered by Lisa Shearer Nelson, Administrative Law Judge.

APPEARANCES

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For Respondent: James O. Jett, Esquire
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STATEMENT OF THE ISSUE

Whether the Petitioners are liable for sales tax, penalties and interest as assessed by the Department of Revenue (the Department) and if so, in what amount?

PRELIMINARY STATEMENT

This proceeding involves three cases which have been consolidated because they deal with a parent company and its subsidiaries. In Case No. 05-1262, on February 8, 2005, the Department issued to Petitioner Beachside Inn Destin, Inc., a Notice of Decision pursuant to Section 212.031, Florida Statutes, sustaining a sales tax assessment of $78,353.56, with $60,481.54 (plus interest which continues to accrue) remaining due. Petitioner timely filed a Petition for a Chapter 120 Administrative Hearing and the matter was forwarded to the Division of Administrative Hearings (Division) for the assignment of an administrative law judge to conduct a formal hearing to resolve the dispute.

The case was originally set for hearing June 7, 2005, and was continued at the request of the Respondent. The parties were ordered to submit a Joint Status Report no later than June 17, 2005.

In Case No. 05-1263, the Department issued to Legendary Restaurant Associates, Inc., a Notice of Decision sustaining a sales tax assessment pursuant to Section 212.031, Florida Statutes, in the amount of $38,411.43, with $30,909.95 (plus interest which continues to accrue) remaining due for sales tax due. Petitioner timely filed a Petition for Chapter 120 Administrative Hearing and the matter was forward to the Division for hearing.

The case was originally set for hearing June 8, 2005, and was also continued at the request of the Respondent, with the parties ordered to submit a Joint Status report no later than June 17, 2005.

In Case No. 04-1585, on January 27, 2004, the Department filed a Notice of Proposed Assessment sustaining an assessment for sales tax pursuant to Section 212.031, Florida Statutes, in the amount of $110,501.72, with $99,548.10 (plus interest which continues to accrue) remaining due. Petitioner timely filed a Petition for Chapter 120 Administrative Hearing and the Department forwarded the case to the Division. The case was originally set for hearing June 29, 2004; however, at the request of the parties, the hearing was cancelled and the Division file was closed without prejudice for the parties to re-open the case at a later date.

On June 23, 2005, Case No. 04-1585 was re-opened and designated as DOAH Case No. 05-2261. All three cases were consolidated and the matter was set for hearing October 17 and 18, 2005. Both parties requested continuances and the case was set for hearing January 12 and 13, 2006, March 8 and 9, 2006, and then July 6 and 7, 2006.

On June 30, 2006, the Department filed a Motion for Summary Recommended Order. On July 3, 2006, Petitioners filed a Motion for Summary Recommended Order and Petitioners' Proposed Recommended Order. That same day the Department also filed Respondent's Motion to Cancel Final Hearing, stating that the parties had stipulated to the facts and had agreed to submit Motions for Summary Recommended Orders in lieu of having a live final hearing. As a result, the undersigned entered an Order Canceling Hearing on July 5, 2006, and this case has been decided based on the written submissions and stipulated exhibits filed by the parties. The submissions of both parties have been considered in the preparation of this Summary Recommended Order.

FINDINGS OF FACT

1. The parties have stipulated to the facts stated in paragraphs 2-59.[1/]

2. The Department of Revenue is an agency of the State of Florida, pursuant to Section 20.21, Florida Statutes, and

is authorized to administer the tax laws of the state, pursuant to Section 213.05, Florida Statutes. The Department was authorized to conduct an audit of each of the Petitioners and to request information to determine their liability for taxes pursuant to Chapter 212, Florida Statutes.

3. Legendary Holding, Inc. (Holding) is a corporation organized under the laws of Florida effective October 23, 1996, and was so organized from 1999-2003. Holding's corporate address is 4100 Legendary Drive, Suite 200, Destin, Florida 32541.

4. Holding was subject to the Internal Revenue Code of 1986 as amended and in effect (IRC) during 1999-2003 and for federal income tax purposes, Holding was a subchapter "s" corporation during this time.

5. Holding was also subject to Chapter 212, Florida Statutes, during 1999-2003.

6. Petitioner Harry T's, Inc. (Harry T's), is a corporation organized under the laws of Florida effective November 9, 1998, and was so organized during Harry T's Audit Period, defined as December 1, 1999 through March 31, 2003. Harry T's was a wholly-owned subsidiary of Holding.

7. During its Audit Period, Harry T's corporate address was 4460 Legendary Drive, Suite 400, Destin, Florida. Harry T's was subject to the IRC and for federal income tax purposes

was a qualified subchapter S subsidiary of the s-corporation parent, Holding.

8. Petitioner Beachside Inn Destin, Inc. (Beachside) was a corporation organized under the laws of Florida effective March 6, 2000, and was so organized during the Beachside Audit Period, defined as May 1, 2000, through May 31, 2003. Beachside, a wholly-owned subsidiary of Holding, was administratively dissolved on October 14, 2004, for failure to file an annual report.

9. During the Audit Period, Beachside's principle place of business was 2931 Scenic Highway 98, Destin, Florida, 32541. Its corporate address was 4460 Legendary Drive, Suite 400, Destin Florida.

10. Beachside was subject to the IRC and for federal income tax purposes was a qualified subchapter S subsidiary of the s-corporation parent, Holding, during the Beachside Audit Period.

11. Petitioner Legendary Restaurant Associates, Inc. (Restaurant) is a corporation organized under the laws of Florida effective October 7, 1999, and was so organized during Restaurant's Audit Period, defined as December 1, 1999, through March 31, 2003. During this time Restaurant was a wholly owned subsidiary of Holding and Restaurant's corporate address was 4460 Legendary Drive Suite 400, Destin, Florida.

12. Restaurant was subject to the IRC and for federal income tax purposes was a wholly-owned, qualified subchapter S subsidiary of the s-corporation parent, Holding, during the Restaurant Audit Period.

13. Legendary, Inc. (Legendary) is a corporation organized under the laws of Florida during 1999-2003, and its corporate address was also 4460 Legendary Drive, Suite 400, Destin, Florida, during this time. Legendary was also a wholly-owned subsidiary of Holding. Legendary was subject to the IRC and for federal income tax purposes, was a qualified subchapter S subsidiary of the s-corporation parent, Holding.

14. Legendary Resorts, LLC (Resorts), is a limited liability company organized under the laws of Florida and was so organized during 2000-2003. Resorts, whose corporate address was also 4460 Legendary Drive, Suite 400, Destin, Florida, was administratively dissolved on September 16, 2005, for failure to file an annual report.

15. Legendary entered into a cooperative business agreement (CBA) with certain subsidiaries of Holding prior to or during 1999-2003. The terms of the CBA between Legendary and these subsidiaries were identical other than the name of the "manager" subsidiary and the percentage of compensation paid to Legendary and the formula for sharing profits varied from time to time.

16. Legendary also entered into a management agreement with certain other of Holding's subsidiaries, and the terms of these agreements were identical.

FACTS RELATED TO PETITIONER HARRY T'S AUDIT

17. Harry T's was a registered dealer who filed form DR-15 (Sales Tax Return) with the Department for each month of Harry T's Audit Period. Harry T's used the cash basis of accounting during its Audit Period.

18. The Department sent Harry T's a Notification of Intent to Audit Books and Records (Form DR-840) to conduct an audit of Harry T's books and records for this purpose.

19. The Department and Harry T's entered into an Audit Agreement agreeing that a sampling method is the most effective, expedient, and adequate method in which to conduct an audit of Harry T's books and records. Gina Imm, a Department tax auditor, examined and sampled the available books and records of Harry T's to determine whether it properly collected and remitted sales and use tax in compliance with Chapter 212, Florida Statutes.

20. Harry T's was the tenant party in a lease with Legendary for the property upon which Harry T's operated its business prior to January 1, 2000. Under the terms of the lease agreement between Harry T's and Legendary, Harry T's

paid rent equal to eight percent of the gross sales to Legendary. On January 1, 2000, the lease was terminated.

21. On January 1, 2000, Harry T's entered into a CBA with Legendary, which was effective throughout Harry T's Audit Period.

22. Harry T's operated a business on property owned by Holdings during Harry T's Audit Period. Accounting entries were made each month during the Audit Period to record the amount of CBA compensation that was accrued by Harry T's to Legendary under the CBA. However, no rent was recorded on the income tax or accounting books of either Harry T's or Legendary during the Audit Period. Further, no amount of money labeled as CBA compensation was transferred from Harry T's to Legendary during Harry T's Audit Period and no payments labeled as "rent" were transferred from Harry T's to Legendary.

23. Based upon the business decisions of the Chief Financial Officer of Legendary, cash was transferred periodically from Harry T's to Legendary during the Audit Period. Based upon the business decisions of the Chief Financial Officer of Legendary, cash was also transferred from Legendary to Harry T's.

24. During Harry T's Audit Period cash was also transferred from Legendary to Holdings. These amounts were

reflected as dividend distributions and varied in amount and time from (a) Holdings insurance and mortgage indebtedness obligations associated with the property used by Harry Ts and owned by Holding, and (b) the amounts accrued under the CBA's. Any amounts collected by Harry T's and not paid directly to third parties were distributed periodically to Holdings as corporate dividends.

25. The Department determined that the transfers of cash from Harry T's to Legendary reflected rental consideration paid as CBA compensation, and directed the Department's auditor to assess sales tax against the amounts recorded as CBA compensation accounting entries.

26. Harry T's paid ad valorem taxes due on the property on which Harry T's operated during each year of Harry T's Audit Period. The Department auditor assessed sales tax on the amounts of ad valorem taxes paid by Harry T's on behalf of Holding.

27. The Department determined that Harry T's owed $58,844.02 in additional sales tax for the CBA compensation and ad valorem taxes paid, plus statutory interest and penalties. On September 5, 2003, the Department issued to Harry T's a Notice of Intent to Make Audit Changes (form DR-1215) for Audit No. A0233016246, stating that Harry T's owed $69,249.79 in taxes, $29,422.03 in penalties, and $6,612.44 in

interest for a total of $94,330.64, and that interest continued to accrue on the unpaid assessment.

28. By letter dated October 9, 2003, Harry T's agreed to the portions of the assessment related to food and beverage, but objected to the assessment for all other amounts including the CBA fees. Harry T's paid $10,953.62 for the uncontested assessment amounts.

29. The Department issued its Notice of Proposed Assessment (NOPA) for audit number A0233016246 on January 27, 2004. The NOPA stated that the total owed by Harry T's was $69,249.79 in taxes, $29,422.03 in penalties, and $11,831.88 for a total of $110,501.72. The NOPA reflected a payment of $10,953.62 paid for the uncontested amounts of the audit assessment, and showed a balance due of $99,548.10 as of the date of the NOPA.

30. The Department received Harry T's formal written protest on April 23, 2004.

FACTS RELATED TO RESTAURANT'S AUDIT

31. Petitioner Restaurant was a registered dealer who filed form DR-15 (Sales and Use Tax Return) with the Department for each month of the Restaurant Audit Period. Restaurant used the cash basis of accounting.

32. The Department sent Restaurant a Notification of Intent to Audit Books and Records (Form DR-840) to conduct an

audit of Restaurant's books and records for the purposes of Chapter 212, Florida Statutes. The Department and Restaurant entered into an Audit Agreement stipulating that a sampling method is the most effective, expedient, and adequate method by which to conduct an audit of Restaurant's books and records. Gina Imm examined and sampled the available books and records of Restaurant to determine whether Restaurant properly collected and remitted sales and use tax in compliance with Chapter 212, Florida Statutes.

33. Restaurant was the tenant party in leases for the property upon which Restaurant operated its business prior to January 1, 2000. On January 1, 2000, Restaurant terminated its leases for these properties.

34. Restaurant entered a CBA with Legendary prior to the beginning of Restaurant's Audit Period, December 1, 1999 through March 31, 2003. The CBA between Restaurant and Legendary was effective throughout the Restaurant Audit Period.

35. Restaurant operated the "Crystal Beach Coffee Company" and "Tony's By the Sea" on property owned by Floridian Homes of Crystal Beach, Inc. (FHCB), an unrelated third party, during the Restaurant Audit Period.

36. Restaurant operated "Blues" on property owned by an individual, Mr. Peter H. Bos, during the Restaurant Audit

Period. 37. Restaurant operated "Rutherford's 465" on property owned by Regatta Bay Investor, Ltd., a Florida limited partnership, during the Restaurant Audit Period.

38. Accounting entries were made each month during the Restaurant Audit Period to record the amount of CBA compensation that was accrued by Restaurant to Legendary under the CBA; however, no rent was recorded on the income tax or accounting books of either Restaurant or Legendary during the Restaurant Audit Period. No amount of money labeled as CBA compensation was transferred from Restaurant to Legendary and no payments labeled as "rent" were transferred from Restaurant to Legendary.

39. Based upon the business decisions of the Chief Financial Officer of Legendary, cash was transferred periodically from Restaurant to Legendary, and cash was also transferred from Legendary to Restaurant during the Restaurant Audit Period. Any amounts collected by Restaurant during the Restaurant Audit Period and not paid directly to third parties were distributed periodically to Holdings as corporate dividends.

40. The Department determined that the transfers of cash from Restaurant to Legendary reflected rental consideration paid as CBA compensation, and directed the Department's

auditor to assess sales tax against the amounts recorded as CBA compensation accounting entries.

41. Restaurant paid ad valorem taxes due on the property on which Restaurant operated during each year of the Restaurant Audit period. The Department assessed sales tax on the amounts of ad valorem taxes paid by Restaurant on behalf of Holding.

42. The Department determined that Restaurant owed $17,880.71 in additional sales tax for the CBA compensation and ad valorem taxes paid, plus statutory interest and penalties.

43. On September 5, 2003, the Department issued the Restaurant a Notice of Intent to Make Audit Changes (Form DR-1215) for audit number A0231102584, stating that Restaurant owed $26,092.10 in taxes, $8,940.31 in penalties, and $1.808.87 in interest for a total of $36,841.28. The Department noted Restaurant's payment of $8,745.53 for the portions of the assessment related to food and beverage sales, leaving a balance due as of that date of $28,095.75. The Department informed Petitioner Restaurant that interest continued to accrue on the unpaid assessment.

44. The Department issued its NOPA for audit number A0231102584 on March 17, 2004, to Restaurant. The total owed by Restaurant as stated in the NOPA was $26,092.10 in taxes,

$8,940.34 in penalties, and $3,378.99 in interest for a total of $38,411.43, less the $8,745.53 already paid, for a total balance due on that date of $29,665.90. Restaurant protested the NOPA, and the Department referred the matter to the Department's Technical Assistance and Dispute Resolution Section.

45. On March 28, 2005, the Department issued its Notice of Decision upholding the assessment of tax for the CBA fees and ad valorem taxes paid by Restaurant, and on April 6, 2005, the Department received the Restaurant's formal written protest.

FACTS RELATED TO BEACHSIDE'S AUDIT

46. Petitioner Beachside Inn Destin, Inc. (Beachside) was a registered dealer who filed form DR-15 (Sales and Use Tax Return) with the Department for each month during the Beachside Audit period, May 1, 2000, through May 31, 2003. Beachside used the cash basis of accounting during the Beachside Audit Period.

47. Beachside and the Department entered into an Audit Agreement stipulating that a sampling method is the most effective, expedient, and adequate method by which to conduct an audit of Beachside's books and records. Gina Imm, a Tax Auditor for the Department, examined and sampled the available books and records of Beachside to determine whether Beachside

properly collected and remitted sales and use tax during the Audit Period in compliance with the requirements of Chapter 212, Florida Statutes.

48. Legendary Resorts, LLC (Resorts) entered into an Asset Purchase Agreement with FHCB and Lester J. Butler, Timothy Fulmer and Mitt Fulmer, three of Resorts' shareholders (the Shareholders), in April 2000, for the acquisition of the Beachside Inn assets by Resorts. Subsequent to the execution of the Asset Purchase Agreement, the parties discovered that a condition precedent to the agreement, i.e., the assumption by Resorts of the major indebtedness of FHCB could not be accomplished as contemplated because it would cause the existing lender to violate its loan consideration limits with respect to the Legendary Group.

49. After discovering this problem, Resorts entered into a Triple-net Lease dated March 1, 2000, with the Shareholders for a beachfront lot and entered into a Triple-net Lease dated March 1, 2000, with FHCB for the Beachside Inn assets that were originally the subject of the Asset Purchase Agreement. These Triple-net Leases were designed to transfer control, and the benefits and burdens of ownership, of the Beachside Inn assets to Resorts pending resolution of the financing contingency and the closing under the Asset Purchase Agreement.

50. Beachside entered into a CBA with Legendary prior to the beginning of the Beachside Audit Period, which was effective throughout the Beachside Audit Period.

51. Although Resorts was the party entitled to all rights, and subject to all obligations, under the Triple-net Leases and Asset Purchase Agreement, the financial accounting and cash management functions and activities during the terms of the Leases were handled by and recorded in Beachside because these leases were designed to permit the Legendary Group to take over the operations of the Beachside Inn assets pending closing and because the Legendary Group intended to place the assets in Beachside under the Asset Purchase Agreement upon the closing of the asset purchase.

52. Resorts and Beachside operated the Beachside Inn assets on property owned by FHCB and the Shareholders during the Beachside Audit Period. Accounting entries were made each month to record the amount of CBA compensation that was accrued by Beachside to Legendary under the CBA but no rent was recorded on the income tax or accounting books of either Beachside or Legendary during the Beachside Audit Period. No money labeled as CBA compensation was transferred from Beachside or Resorts to Legendary and no payments labeled as "rent" were transferred from Beachside or Resorts to Legendary.

53. Based on the business decisions of the Chief Financial Officer of Legendary, cash was transferred periodically from Resorts and/or Beachside to Legendary and from Legendary to Resorts and/or Beachside during the Beachside Audit Period.

54. After Resorts and Beachside operated the Beachside Inn assets for a period of time at a material loss, Resorts was not able to arrange for suitable substitute financing to close on the purchase of the Beachside Inn assets under the Asset Purchase Agreement. Resorts, FHCB and the Shareholders reached an agreement on or about August 15, 2003 (the Termination Date), whereby Resorts terminated its rights under the Asset Purchase Agreement and the two leases. In exchange, the Shareholders transferred ownership of the beachfront lot to Resorts.

55. Federal income tax returns for calendar years 2000, 2001, and 2002 were filed by Resorts which reflected the results of operating the Beachside Inn assets. Following the Termination Date, all of the historic accounting entries made by Beachside reflecting the operation of the Beachside Inn assets were moved from its books and records to the books and records of Resorts for administrative reasons and consistency with the legal documents.

56. Beachside and Resorts made insurance payments on behalf of the owners of the property upon which Resorts operated its business for each year of the Beachside Audit Period. They also made payments for loans on behalf of the owners of the property and paid ad valorem taxes due on the property upon which Resorts operated for each year of the Beachside Audit Period.

57. The Department assessed Beachside sales tax on the amounts of ad valorem taxes, insurance payments and loan payments paid by Beachside on behalf of FHCB and the Shareholders. On October 27, 2003, the Department issued Beachside a Notice of Intent to Make Audit Changes (form DR-1215) for audit number A030582778, stating that Beachside owed $69,436.01 in taxes, $30,606.77, and $7,635.33 for a total of $107,678.11. The Department noted Beachside's payment of $8,936.01 for the portions of the assessment related to sales of good and beverage, and reflected a balance due after payment of $98,742.10, with interest continuing to accrue.[2/]

58. Beachside made an additional payment of $8,936.01 toward the balance due on the uncontested amount of the assessment. On February 19, 2004, the Department issued its Notice of Proposed Assessment for audit number A030582778, stating that the total amount owed by Beachside was $69,436.01 in taxes, $30,606.77 in penalties and $8,917.55 in interest

for a total of $108,960.33, less $17,872.02 previously paid by Beachside, for a balance as of that date of $91,088.31.

59. On April 16, 2004, Beachside protested the NOPA, and the Department referred the matter to the Department's Technical Assistance and Dispute Resolution Section. On March 28, 2005, the Department issued its Notice of Decision upholding the assessment of tax for the payment of ad valorem taxes, insurance and loans by Beachside on behalf of Holding. On April 6, 2005, the Department received the Beachside's formal written protest of audit number A030582778.

ADDITIONAL FACTS

60. In addition to the Stipulated Facts submitted by the parties, the undersigned makes the following findings based upon the stipulated exhibits submitted.

61. With respect to the CBAs, the documents provided "the Co-Operator and Manager have agreed to enter into this Agreement for each to provide certain assets to the Business and for Manager to provide, on a cost effective basis, Management Services as required from time to time by the Business." The Agreements state that "each have various assets including fixtures, employees, contractual relationships, knowhow and real estate which they wish to combine to operate a restaurant and bar (the Business)."

62. The CBAs do not name a physical location and do not have provisions for care and repair of the premises; for rights of access and inspection; for eminent domain or condemnation; for default; for provision of utilities or for subletting, all provisions typically seen in a commercial lease. By contrast, the Triple-Net Lease for the Beachside Inn Assets (Stipulated Exhibit 10) contains all of these provisions.

63. The CBAs provide for payment of management services, expenses of the business, and all services and assets necessary for the operations of the business. They are clearly not limited to provision of a location.

64. With respect to the Beachside Assets, the Triple-Net Lease (the Beachside lease) was entered after the Asset Purchase Agreement and expressly acknowledges the existence of that document. However, the Beachside lease by its terms does not provide a right of purchase at a nominal sum at the end of the lease. It provides options to extend the term of the three-year lease for five additional terms of three years each, governed by the same terms and provisions. It also provides a right to purchase the premises at any time during the term of the lease and up to six months after any extensions of the lease which shall be exercised by affecting a closing under the Asset Purchase Agreement.

65. The Beachside Lease for the Beachside Inn assets has other provisions that are relevant to these proceedings. For example, the Beachside Inn lease defines the term "rent" as including the base rent ($100 per month) plus any state sales tax imposed "upon any and all rents or other payments provided in this lease." It provides for surrender of the premises at the expiration of the lease, including terms for removal of any trade fixtures, personal property and signs. Most importantly, the Beachside Inn lease expressly states the following:

> 26. a. The Lease does not create the relationship of principal and agent or of partnership or of joint venture or of any association between Landlord and Tenant, <u>the sole relationship between the parties hereto being that of Landlord and Tenant.</u>
>
> * * *
>
> c. This Lease and the Exhibits, if any, attached hereto and forming a part hereof, constitute the entire agreement between Landlord and Tenant affecting the Premises and there are no other agreements, either oral or written, between them other than are herein set forth. . . .

CONCLUSIONS OF LAW

66. The Division of Administrative Hearings has jurisdiction over the subject matter and the parties to this action in accordance with Sections 120.569 and 120.57(1), Florida Statutes.

67. The Department must demonstrate 1) that an

assessment has been made against the taxpayer and 2) the factual and legal grounds for making the assessment. Once the Department meets this initial burden of proof, the burden shifts to the Petitioner to show by a preponderance of the evidence that the assessment is incorrect. Section 120.80(14)(b)(2), Florida Statutes; <u>IPC Sports, Inc. v. Department of Revenue</u>, 829 So. 2d 330 (Fla. 3d DCA 2002). In determining whether the assessment is correct, the undersigned is required to honor the settled principle that tax laws are to be strongly construed in favor of the taxpayer and against the government. <u>Maas Brothers, Inc. v. Dickinson</u>, 195 So. 2d 193, 198 (Fla. 1967); <u>Leadership Housing, Inc. v. Department of Revenue</u>, 336 So. 2d 1239 (Fla. 4th DCA 1976).

68. The sales tax indebtedness for all three entities is governed by Section 212.031, Florida Statutes, and Florida Administrative Code Rule 12A-1.070(4),(12)&(19). Section 212.031 provides:

> (1)(a) It is declared to be the legislative intent that every person is exercising a taxable privilege who engages in the business of renting, leasing, or granting a license for the use of any real property . . . .
>
> * * *
>
> (c) For the exercise of such privilege, a tax is levied in an amount equal to 6 percent of an on the total rent or license fee charged for such real property by the person charging or collecting the rental or

> license fee. The total rent or license fee charged for such real property shall include payments for the granting or a privilege to use or occupy real property for any purpose and shall include base rent, percentage rents, or similar charges. Such charges shall be included in the total rent or license fee subject to tax under this section whether or not they can be attributed to the ability of the lessor's or licensor's property as used or operated to attract customers. . . .
>
> * * *
>
> (3) The tax imposed by this section shall be in addition to the total amount of the rental or license fee, shall be charged by the lessor or person <u>receiving the rent or payment</u> in and by a rental or license fee arrangement with the lessee or person paying the rental or license fee, <u>and shall be due and payable at the time of the receipt of such rental or license fee payment by the lessor or other person who receives the rental or payment</u>. . . .

69. The relevant portions of Florida Administrative Code Rule 12A-1.070 provide:

> (4)(a) The tenant or person actually occupying, using or entitled to use any real property from which rental or license fee is subject to taxation under Section 212.031, F.S., shall pay the tax to his immediate landlord or other person granting the right to such tenant or person to occupy or use such real property.
>
> (b) The tax shall be paid at the rate of 5 percent prior to February 1, 1988, and 6 percent on or after February 1, 1988, on all considerations due and payable by the tenant or other person actually occupying, using, or entitled to use any real property to his landlord or other person for the privilege of use, occupancy, or the right

to use or occupy any real property for any purpose.

(c) Ad valorem taxes paid by the tenant or other person actually occupying, using, or entitled to use any property to the lessor or any other person on behalf of the lessor, including transactions between affiliated entities, are taxable.

* * *

(12) When a tenant or other person pays insurance for his own protection, the premium is not regarded as rental or licensee fee consideration, even though the landlord or other person granting the right to occupy or use such real property is also protected by the coverage. However, any portion of the premium which secures the protection of the landlord or person granting the right to occupy or use such real property and which is separately stated or itemized is regarded as rental or license fee consideration and is taxable.

* * *

(19)(a) The lease or rental of real property or a license fee arrangement to use or occupy real property between related "persons" as defined in Section 212.02(12), F.S., in the capacity of lessor/lessee, is subject to tax.

(b) The total consideration, whether direct or indirect, payments or credits, or other consideration in kind, furnished by the lessee to the lessor is subject to tax despite any relationship between the lessor and lessee.

(c) The total consideration furnished by the lessee to a related lessor for the occupation of real property, for the use or entitlement to the use of real property owned by the related lessor is subject to tax, even though the amount of the

> consideration is equal to the amount of the consideration legally necessary to amortize a debt owned by the related lessor and secured by the real property, or used, and even though the consideration is ultimately used to pay that debt.

THE ASSESSMENT AGAINST HARRY T'S

70. With respect to Harry T's, there are two issues requiring resolution: 1) whether Harry's T's payment of ad valorem taxes on behalf of the property owner are taxable under Chapter 212.031, Florida Statutes; and 2) whether payments of cash denominated as dividends transferred from Harry T's to a related business entity are taxable as rent where the parties have entered into a "Cooperative Business Agreement."

71. The first issue requires little discussion. Rule 12A-1.070(4)(c) makes it clear ad valorem taxes paid by the tenant "or other person actually occupying, using, or entitled to use any real property" on behalf of the lessor, including transactions between affiliated entities, are taxable. Harry T's makes no argument to the contrary. Accordingly, to the extent that the audit finds that Harry T's must pay sales tax on the amount of ad valorem taxes paid, the Department has demonstrated both a factual and legal basis for making the assessment, and the Petitioner has not demonstrated that the assessment is incorrect.

72. The second issue is less straightforward. There is

no question that the parties entered a cooperative business agreement by which they agree to pool their resources to operate a restaurant and bar. The parties have stipulated that Harry T's operated on property owned by its parent company, Holdings, and that while there were accounting entries reflecting CBA compensation accrued by Harry T's to Legendary, there were no payments actually made and labeled as either CBA compensation or as rent.

73. Cash was transferred between subsidiaries based upon the business decisions of the Chief Financial Officer of Legendary. However, as he testified via deposition, these transfers were accomplished to facilitate the needs of the individual companies. They were not tied to the accounting entries reflected as CBA compensation.

74. More importantly, the cash distributions labeled as corporate dividends appear to bear no correlation to the CBA compensation book entries. The records reflecting the actual transfers have not been included in the stipulated exhibits. Instead, the parties have stipulated that these amounts reflect "any amounts collected by Harry T's . . . and not paid directly to third parties."

75. Section 212.031(3) provides that sales tax on leases is due and payable "at the time of the receipt of such rental or license fee payment by the lessor or other person who

receives the rental or payment." Simply put, in order for there to be a tax due and owing, there must be a payment of rent. See Department of Revenue, 406 So. 2d 1299 (Fla. 1st DCA 1981); see also St. Johns Trading Co. v. Department of Revenue, DOAH Case No. 84-1652 (DOR Final Order 1985). Here, there is no such payment. Transfer of cash between related entities with no correlation to an agreed amount or percentage for payment of rent is not sufficient to demonstrate that the Petitioner was paying rent for the use of the property. To the extent that the audit assesses taxes for the amount listed as CBA compensation in Harry T's bookkeeping entries, Petitioner has demonstrated that the assessment is incorrect and sales tax should not be assessed for those amounts.

THE ASSESSMENT AGAINST RESTAURANT

76. Petitioner Legendary Restaurant Associates, Inc., challenges the Department audit on the same basis, i.e., 1) whether Restaurant's payment of ad valorem taxes on behalf of the property owner are taxes under Chapter 212.031, Florida Statutes; and 2) whether payments of case denominated as dividends transferred from Restaurant to a related business entity are taxable as rent where the parties have entered into a "Cooperative Business Agreement."

77. For the same reasons outlined with respect to Harry T's, the assessment of additional sales tax on the ad valorem

taxes paid by Restaurant on behalf of Holding during the audit period is sustained. However, the additional taxes on the bookkeeping entries labeled as CBA compensation cannot be sustained as no payment for rent was actually made.

THE ASSESSMENT AGAINST BEACHSIDE

78. With respect to Beachside, the Department has assessed additional taxes for the ad valorem taxes, insurance payments and loan payments paid by Beachside on behalf of FHCB and the Shareholders. All of these items are specified as payments that would trigger sales tax pursuant to Rule 12A-1.070. See specifically Florida Administrative Code Rule 12A-1.070(4)(c), (12) and (19)(b) and (c).

79. Petitioner contends that these amounts are not subject to assessment because there was a shift in the beneficial ownership of the Beachside Inn assets during the Audit Period. Petitioner states:

> Since Resorts both owned the Beachside Inn assets for tax purposes and operated on them, there can be no lease (since a lease between owner of real property and itself as the tenant effects a merger under Florida law) and no sales or use tax should be due here in connection therewith.

80. Beachside operated under the terms of the Beachside lease during the entire Audit Period. While the parties have stipulated that the intent of the leases was to transfer control of the assets, as well as the benefits and burdens of

ownership to Resorts, the language of the lease must determine whether Resorts became the equitable owner of the property.

81. In order to have all the benefits and burdens of ownership so as to qualify as an equitable owner of the property, there must be the ability to purchase the property at a nominal sum. Robbins v. Mt. Sinai Medical Center, Inc., 748 So. 2d 349 (Fla. 3d DCA 1999); Metropolitan Dade County v. Brothers of the Good Shepherd, Inc., 714 So. 2d 573 (Fla. 3d DCA 1998). Here, the option to purchase required Resorts to affect a closing under the Asset Purchase Agreement. The Asset Purchase Agreement did not allow for purchase of the property at a nominal sum, but instead required a note for payment of $880,000. Under these circumstances, Resorts cannot be considered the equitable owner of the property.

82. If Resorts is not the equitable owner of the property, Beachside clearly cannot claim the benefits of ownership. Under these circumstances, Resorts and Beachside were paying the ad valorem taxes, insurance premiums and loan payments in their capacities as tenants, as contemplated by the Beachside Inn lease, for the benefit of the property owner. Accordingly, the Department has sustained its burden regarding the taxes assessed against Beachside, and Petitioner has not demonstrated that the assessment is incorrect.

RECOMMENDATION

Upon consideration of the facts found and conclusions of law reached, it is

RECOMMENDED:

That the Department of Revenue enter a final order finding that:

1. The Department's assessment for additional sales tax, penalties and interest against Petitioner Harry T's is sustained for the portion attributable to payment of ad valorem taxes only;

2. The Department's assessment for additional sales tax, penalties and interest against Petitioner Legendary Restaurant Associates, Inc., is sustained for the portion attributable to payment of ad valorem taxes only; and

3. The Department's assessment for additional sales tax penalties and interest against Petitioner Beachside Inn, Inc., be sustained in its entirety.

DONE AND ENTERED this 27th day of July, 2006, in Tallahassee, Leon County, Florida.

____
LISA SHEARER NELSON
Administrative Law Judge
Division of Administrative Hearings
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Filed with the Clerk of the
Division of Administrative Hearings
this 27th day of July, 2006.

ENDNOTES

1/ For reasons that are not explained, several of the Stipulated Facts submitted by the parties read "intentionally omitted." Moreover, not all of the Stipulated Facts agreed to by the parties are reflected in the Proposed Recommended Order submitted by Petitioners. Accordingly, the numbering of the Stipulated Facts herein does not correspond to the numbering in the parties' submissions.

2/ The amounts in the stipulated facts submitted appear to be, for the most part, the amounts listed in the Notice of Intent to Make Audit Changes issues September 26, 2003, as opposed to those listed in the Notice issued October 27, 2003. See Exhibit 14. The undersigned has used the numbers actually identified in the Notice issued October 27, 2003.

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NOTICE OF RIGHT TO SUBMIT EXCEPTIONS

All parties have the right to submit written exceptions within 15 days from the date of this recommended order. Any exceptions to this recommended order should be filed with the agency that will issue the final order in this case.