STATE OF TENNESSEE
OFFICE OF THE ATTORNEY GENERAL

February 9, 2016

Opinion No. 16-05

Licensing and taxation of hotels selling alcohol for consumption on the premises

Question 1

For purposes of the license required under Tenn. Code Ann. § 57-4-301(b)(1)(T) for the sale by a hotel of alcoholic beverages sold for consumption on the premises, is the hotel owner or the hotel management company hired by the hotel owner the appropriate licensee?

Opinion 1

When the owner of a hotel has granted a franchise to a management company to operate the food and beverage services in the hotel, the management company may be the licensee for purposes of Tenn. Code Ann. § 57-4-201(b)(1).

Question 2

Although not the licensee, is the hotel owner liable for any delinquent taxes imposed under Tenn. Code Ann. § 57-4-301(c) that the management company fails to collect and remit with respect to sales of alcoholic beverages at the hotel owner's establishment?

Opinion 2

No.

Question 3

If the hotel management company is the licensee and ceases managing the hotel for whatever reason, has the management company "quit the business" within the meaning of Tenn. Code Ann. § 57-4-303 (2013) so that it must file a final return and remit all taxes due pursuant to that statute?

Opinion 3

Yes.

Question 4

If the hotel management company ceases managing the hotel for whatever reason, is the hotel owner (in the event the owner commences direct operation of the hotel) or the new hotel

management company (in the event the hotel owner contracts with a new management company) considered the "successor or assign" of the business, so that the hotel owner or new management company may be held liable for any unpaid tax, interest, or penalty under Tenn. Code Ann. § 57-4-303? If so, what constitutes "purchase money" for purposes of determining whether the hotel owner or new management company withheld sufficient amounts to cover all unpaid taxes, interest, and penalty that are due?

Opinion 4

Whether the hotel owner or a new management company would be liable for taxes, interest, or penalty that had not been paid by the former management company depends on the circumstances in which a new licensee assumes operation of the hotel. Any money paid to the former management company for its license or its stock of goods would be considered "purchase money" for purposes of Tenn. Code Ann. § 57-4-303.

Question 5

If the hotel management company is considered to be engaged in the business of selling alcoholic beverages at retail, such that it must obtain the license, is the hotel management company jointly and severally liable along with the hotel owner for Tennessee sales and use taxes due with respect to retail sales of alcoholic beverages sold for consumption on the hotel premises?

Opinion 5

No.

Question 6

If the hotel management company is considered to be engaged in the business of selling alcoholic beverages at retail, such that it must obtain the license, will the hotel management company be classified for Tennessee business tax purposes under Classification 2 as a retailer of prepared food and drinks, including alcoholic beverages (*see* Tenn. Code Ann. § 67-4-708(2)(G) (2013)) or under Classification 3 as a provider of management services (*see* Tenn. Code Ann. § 67-4-708(3)(C) (2013))?

Opinion 6

As provided in Tenn. Code Ann. § 67-4-708, the management company would be classified "according to the dominant business activity," which would depend in this case on whether sales of prepared food and drinks or fees received for management of the hotel constituted the "major and principal source of taxable gross sales of the business." Tenn. Code Ann. § 67-4-702(5).

ANALYSIS

1. "It is lawful to sell wine and other alcoholic beverages as defined in § 57-4-102, and beer as defined in § 57-6-102, to be consumed on the premises of, or within the boundaries of,

any . . . hotel." Tenn. Code Ann. § 57-4-101. But a "person, firm or corporation owning any hotel . . . desiring to sell wine or other alcoholic beverages for consumption on its premises where food may be served" is required to obtain a license or permit from the Tennessee Alcoholic Beverage Commission to do so. Tenn. Code Ann. § 57-4-201(b)(1).

A "hotel" is, with certain limiting qualifications, a building or structure that is "kept, used, maintained, advertised and held out to the public to be a place where food is actually served and consumed and sleeping accommodations are offered for adequate pay" to guests. Tenn. Code Ann. § 57-4-102(20)(A). Thus, a hotel is by statutory definition a particular kind of commercial enterprise that offers various services and products and that is conducted within a building or a structure and its premises, all of which "are a part of the hotel operation." *Id.* For purposes of construing § 57-4-201(b)(1) and the taxing provisions of Part 3 of Title 57, Chapter 2, therefore, the "person, firm or corporation owning" a "hotel" is the owner of that commercial enterprise or business.

The operation of a restaurant on the premises of a hotel may be granted by franchise to another person or entity, "and the holder of such franchise shall be included in the definition of 'hotel'" under the statute. Tenn. Code Ann. § 57-4-102(20)(A). A "franchise" is commonly understood to mean an authorization to carry out special commercial activities, like selling goods or providing services. *New Oxford American Dictionary*. Thus, the hotel enterprise can authorize some other person or entity to operate the hotel's dining facilities where liquor is sold or provide management services for those facilities on behalf of the hotel and, if that authority is granted, then the franchisee is also a "hotel" within the meaning of the statute. It follows, then, that the owner of the franchisee is also the owner of a hotel within the meaning of Tenn. Code Ann. § 57-4-201(b)(1) and can apply for and obtain the required license to sell alcoholic beverages for consumption in the hotel.

The licensing requirements of Tenn. Code Ann. § 57-4-201(d) in fact contemplate that such a franchisee may apply for and hold the required permit to sell alcoholic beverages for consumption in the hotel. When an applicant applies for a license, that applicant has to disclose its name, "the location of the hotel," "the true owner thereof," and has to swear that "the manager and/or operator of the hotel . . . seeking such permit is of good moral character." Tenn. Code Ann. § 57-4-201(d). This only makes sense if the applicant for the license may be different from the owner of the hotel and only if the applicant/licensee in fact may be the manager/operator of the hotel.

In practice, owners of hotels that qualify for licensing under Tenn. Code Ann. § 57-4-102 do sometimes contract with management companies to manage or operate the business, including the sale of alcoholic beverages, and the Tennessee Alcoholic Beverage Commission has a longstanding practice of granting the licenses required by Tenn. Code Ann. § 57-4-201(b)(1) to such management companies. This practice is particularly necessary in the case of establishments owned by municipal corporations since they themselves are not allowed to obtain licenses for the on-premises sale of alcoholic beverages and must obtain licenses through third parties. *See* Tenn. Att'y Gen. Op. No. 14-03 (Jan. 9, 2014). Tennessee Code Ann. § 57-4-201 and other Code provisions pertaining to intoxicating liquors have been amended numerous times over the years without any attempt or intent to alter the Commission's longstanding interpretation and application

of the licensing requirements with respect to hotel management companies. This administrative interpretation is accorded substantial weight, because, as the Tennessee Supreme Court has stated, the "construction of a statute . . . adopted by the legislative or executive departments of the State, and long accepted by the various agencies of government and the people, will usually be accepted as correct by the courts." *State v. Nashville Baseball Club*, 127 Tenn. 292, 154 S.W.1151, 1154 (Tenn. 1913), quoted in *New England Mut. Life Ins. Co. v. Reece*, 83 S.W.2d 238, 241 (Tenn. 1935).

In sum, the owner of a hotel enterprise may apply for and hold the license required under Tenn. Code Ann. § 57-4-301(b)(1)(T) for the sale by a hotel of alcoholic beverages sold for consumption on the premises. If the hotel enterprise grants a franchise to a management company for the operation of the food and beverage portion of the hotel business, the franchisee becomes a "hotel" and, therefore, the owner of the franchisee may—but does not have to—become the applicant for and holder of the license. In that situation, the terms of the franchise grant or management agreement may speak to and govern who applies for a license.

2. Title 57, Chapter 4, Part 3 provides for the taxation of sales of alcohol for on-premises consumption at establishments licensed under the authority granted in Parts 1 and 2. "[E]very person is exercising a taxable privilege who engages in the business of selling at retail in this state alcoholic beverages for consumption on the premises." Tennessee Code Ann. § 57-4-301(a). The applicant for an on-premises consumption license is required to pay the ABC a "one-time, non-refundable fee . . . when the application is submitted for review." Tenn. Code Ann. § 57-4-301(b)(1). The licensee must then pay taxes, as required by Tenn. Code Ann. § 57-4-301(b) and (c).

These taxes are collected by the Commissioner of Revenue and "shall be collected by the retailer from the consumer insofar as it can be done." Tenn. Code Ann. § 57-4-302. Each licensee is required to post and maintain an indemnity bond with the Commissioner of Revenue for the greater of $1000 or quadruple its average monthly tax liability as determined by the Commissioner. *Id.*

In sum, it is the licensee that is liable for the payment of these fees and taxes. Thus, if a management company obtains a license under Tenn. Code Ann. § 57-4-201(b)(1), the one-time fee is imposed on that company when it applies for a license. The management company is then also the retailer and is charged with collecting the tax from consumers and remitting it to the Commissioner of Revenue. The owner of the hotel enterprise is not the licensee and, therefore, is not charged with collecting the tax.

3. If "any licensee liable for any tax, interest or penalty" under Title 57, Chapter 4, Part 3 sells the business or stock of goods, or "quit[s] the business, *the licensee shall* make a final return and payment" of any taxes, interest, and penalty due. Tenn. Code Ann. § 57-4-303 (emphasis added). Thus, if a hotel management company is the licensee and if its franchise is terminated or it ceases its management operations for any reason, it must timely make a final return and payment of all taxes, interest, and penalties due under the statute.

4. Whether the owner of a hotel enterprise or a management company assuming operation of a hotel would be liable for unpaid taxes owed by a management company that quits the business would depend on the circumstances in which the new licensee assumes operation of the hotel. *See* Tenn. Code Ann. § 57-4-303. Any consideration paid to the former management company for its license or its stock of goods would be deemed "purchase money" for purposes of Tenn. Code Ann. § 57-4-303.

5. A management company holding a license for the sale of alcoholic beverages for on-premises consumption would be liable for collecting and remitting the taxes on those sales as both the licensee under Tenn. Code Ann. § 57-4-201(b)(1) and the seller under Tenn. Code Ann. §§ 57-4-301(c) and 57-4-302. Although the hotel owner would be entitled to obtain a license and make sales without the services of a management company, there is no provision in the law for a licensee to be liable for taxes jointly with another person who is not a licensee.

6. As provided in Tenn. Code Ann. § 67-4-708, the management company would be classified "according to the dominant business activity," which would depend on whether sales of prepared food and drinks or fees received for management of the hotel constituted the "major and principal source of taxable gross sales of the business." Tenn. Code Ann. § 67-4-702(5). This determination would depend, in turn, on whether the management company receives the food and drink revenues directly or instead receives a fee for its management services. If the "major and principal" portion of its gross sales comes directly from the sale of prepared food and drinks, the management company would fall under Classification 2 and be taxed accordingly. Tenn. Code Ann. § 67-4-708(2)(G) ("sales of . . . [p]repared food and drinks, including alcoholic beverages, for consumption on and/or off the premises"). If the "major and principal" portion of its gross sales comes from fees for managing the hotel, however, the management company would be subject to the business tax under § 67-4-708(3)(C), which imposes the business tax on persons "making sales of services or engaging in the business of furnishing or rendering services."

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