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

IN THE MATTER OF THE PROTEST OF
SANTA FE TOW **No. 15-21**
TO ASSESSMENT ISSUED UNDER
LETTER ID NO. L1332888896

and

IN THE MATTER OF THE PROTEST OF
EMERGENCY LOCK & KEY
TO ASSESSMENT ISSUED UNDER
LETTER ID NO. L0837170496

DECISION AND ORDER

A formal hearing on the above-referenced protest was held on May 18, 2015, before Monica Ontiveros, Hearing Officer. Santa Fe Tow and Emergency Lock & Key (collectively known as "Taxpayers") were represented by Clinton W. Marrs, Esq. and Patrick Griebel, Esq. of the Marrs Griebel Law, LTD law firm. Taxpayers share a common owner, Mr. Armando Beltran. The tax protests were consolidated on April 1, 2014. Mr. Beltran appeared and testified along with his wife, Fabiola Beltran. Mr. Chad McKinney, CPA from McKinney & Associates LLC also appeared and testified on behalf of Taxpayers. The Taxation and Revenue Department ("Department") was represented by Peter Breen, attorney for the Department. Mr. Danny Pogan, protest auditor, appeared and testified as a witness for the Department. Taxpayers filed Protestant's Post-Hearing Brief on May 26, 2015 and the Department filed Santa Fe Tow Post-Hearing Brief on June 5, 2015. This Decision is being issued within 30 days from the date of the last Brief filed in this matter.

The Department's Exhibits C-I were stipulated to by Taxpayers and Taxpayers' Exhibits 1-

21 were stipulated to by the Department. The Department did not object to Taxpayers' Exhibits 22 and 23. The aforementioned Exhibits were introduced into the record and are part of the administrative file.

In addition to the pleadings and filings referred to in the Findings, the record contains the following: Notice of Telephonic Scheduling Conference issued on March 12, 2014 to each separate taxpayer; Scheduling Order and Notice Administrative Hearing issued on April 1, 2014 (the protests were consolidated as part of the Order); Department's Preliminary Exhibit and Witness List filed on June 13, 2014; Taxpayers' Preliminary Exhibit and Witness List filed on June 16, 2014; Protestant Emergency Lock & Key's First Interrogatories filed on December 10, 2014; Protestant Santa Fe Tow's First Interrogatories filed on December 10, 2014; Taxpayers' Requests for Production of Documents filed on December 10, 2014; Taxpayers' Certificate of Service filed on December 10, 2014; Department's Certificate of Mailing filed on January 9, 2015 (two Certificates); Taxpayers' Unopposed Motion for Postponement of Formal Hearing filed on March 13, 2015; Joint Pre-Hearing Statement filed on March 20, 2015; Continuance Order, Notice of Reassignment, Amended Scheduling Order and Amended Notice of Administrative Hearing issued on March 23, 2015. It should be noted that the attorneys for both parties conducted themselves in an extremely courteous manner and Taxpayers' Brief was especially interesting and helpful. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. On September 12, 2012, the Department assessed Emergency Lock & Key in gross receipts tax in the amount of $68,849.00 in principal; $13,769.89 in penalty; and $9,358.92 in interest for tax period June 30, 2007 – October 31, 2011. Letter Id No. L0837170496.

2. On September 12, 2012, the Department assessed Santa Fe Tow in gross receipts tax in the amount of $196,731.00 in principal; $39,346.20 in penalty; and $22,853.32 in interest for tax period January 31, 2007 – October 31, 2011. Letter Id No. L1332888896.

3. On October 10, 2012, Taxpayers filed protests to the assessments.

4. On October 26, 2012, the Department acknowledged the protests. Letter Id Nos. L0273995072 and L1543130432.

5. On March 11, 2014, the Department requested a hearing in both protests.

6. The Hearings Bureau initially set the consolidated cases for hearing on April 7, 2015. The consolidated cases were continued to May 18, 2015.

7. Armando Beltran is the owner of both Taxpayers.

8. Emergency Lock & Key is a limited liability company. **[Exhibit G, page AN1.1].**

9. Santa Fe Tow is owned as sole proprietorship. **[Exhibit F, page AN1.1].**

10. During the tax periods at issue, Emergency Lock & Key engaged in the business of providing mobile emergency lock and key services such as installing locks, rekeying and making keys for auto, residential, and commercial locks. **[Exhibit G, page AN1.2].**

11. Santa Fe Tow engaged in the business of providing automobile towing services, twenty-four hours a day, seven days a week with a quick response. **[Exhibit F, page AN1.1].**

12. During the audit period at issue, Taxpayers filed their monthly gross receipts tax returns on a timely basis; however, Taxpayers deducted all the receipts received from the AAA New Mexico, LLC, ("AAA"), the New Mexico affiliate of the American Automobile Association. **[Exhibit G, page AN1.2; Exhibit F, page AN1.3].**

13. Taxpayers filed their gross receipts returns in a timely manner.

14. Taxpayers hired a competent certified public accountant, Chad McKinney, sometime in 2005 to prepare the gross receipts returns. **[CD 05-18-15 1:03].**

15. Mr. McKinney has been licensed as a certified public accountant since 2003. **[CD 05-18-15 2:17].**

16. Mr. McKinney credibly testified at the hearing that he believed all the receipts received from AAA were nontaxable, which is why he advised Taxpayers to deduct all of the AAA receipts. **[CD 05-18-15 2:27-2:29].**

17. In preparation for filing their monthly gross receipts returns, Mr. Beltran provided Mr. McKinney with his monthly bank statements and a listing of expenses. Mr. McKinney prepared the gross receipts returns based on the bank statements provided by Mr. Beltran. **[CD 05-18-15 2:27; Exhibit G, page AN1.3; Exhibit F, page AN1.2].**

18. Mr. Beltran had complete trust and faith in Mr. McKinney and Mr. Beltran is not a certified public accountant. **[CD 05-18-15 1:07-1:08].**

19. The Department's auditor, Irene Jaramillo, conducted a field audit of Taxpayers records from December 7, 2011 through July 31, 2012. [**Exhibit G, page AN1.1; Exhibit F, page AN1.1].**

20. Ms. Jaramillo used the bank deposit method to determine Taxpayers' total receipts, which is to say that she took all of the receipts deposited into Taxpayers' bank accounts and considered them to be receipts.

21. Ms. Jaramillo found Taxpayers' "internal controls were solid." **[Exhibit G, page AN1.2; Exhibit F, page AN1.2].**

22. Ms. Jaramillo also noted in her audit that "taxpayer's representative was able to provide the auditor with proper backup documentation." **[Exhibit G, page AN1.; Exhibit F, page AN1.2].**

23. There was no issue raised during the audit that Taxpayers' records were inadequate.

24. The exceptions or findings made by Ms. Jaramillo were that Taxpayers either underreported or over-reported their gross receipts and took deductions without nontaxable transaction certificates to support the deductions.

25. Ms. Jaramillo compared Taxpayers' bank deposits from January 1, 2009 through October 31, 2011 against the receipts reported to the Department to determine whether Taxpayers had over-reported or underreported their gross receipts. **[Exhibit G, page AN1.3].**

26. The underreporting or over-reporting amounts were reconciled to arrive at an amount without tax and this amount was incorporated into the total amount of gross receipts taxable. **[Exhibit G, page AN1.3 and Exhibit F, page AN1.3].**

27. Emergency Lock & Key had two reporting periods where there was either an underreporting or over-reporting of gross receipts. **[Exhibit G, pages C2.1 and C2.2].**

28. Santa Fe Tow had 13 reporting periods where there was either an underreporting or over-reporting of gross receipts. **[Exhibit F, pages C2.1 and C2.2].**

29. Santa Fe Tow provided services to the Albuquerque Police Department, AAA and 5% to other customers. **[CD 05-18-15 0:44].**

30. Emergency Lock & Key provided services to AAA and 5% to other customers. **[CD 05-18-15 0:45].**

31. Emergency Lock & Key received nontaxable transaction certificates from Knittles Towing, Inc. and Haven House, Inc. **[Exhibit G, page C3.8].**

32. Santa Fe Tow received nontaxable transaction certificates from Trucks West, Inc., Albuq. Motor Co., Inc., Knittles Towing, Inc., Lujan's Paint & Body, Inc., R & C Bodyworks, Inc., Crown Coachworks, LTD, Co. and Crown Coach Works. **[Exhibit F, page C3.11].**

33. AAA did not execute any nontaxable transaction certificates to Taxpayers and the Department acknowledged that because AAA holds a Certificate of Authority for insurance purposes, its member receipts are not subject to gross receipts tax and the Department would not have been able to issue a non taxable transaction certificate to AAA. **[Exhibit 17 (Answer to Interrogatory No. 3) and Exhibit 18 (Answer to Interrogatory No. 3)].**

34. The nontaxable transaction certificates were provided to Ms. Jaramillo, but she made no adjustments for these deductions.

35. Ms. Jaramillo stated in both of her audits that the "taxpayer's representative told the auditor that the only deductions the taxpayer was taking is for one customer." **[Exhibit G, page AN1.4; Exhibit F, page AN1.4].**

36. Based on this alleged statement, Ms. Jaramillo disallowed all the deductions including the deductions for both Emergency Lock & Key and Santa Fe Tow. **[Exhibit G, page AN1.4; Exhibit F, page AN1.4].**

37. Ms. Jaramillo disallowed all the deductions Taxpayers reported. **[Exhibit G, pages C3.3-C3.4; Exhibit F, pages C3.3-C3.4].**

38. In the Department's responses to the Interrogatories propounded by Taxpayers, the Department's employees, Ms. Jaramillo and Mr. Pogan, stated that only the deductions from AAA were disallowed. **[Exhibit 16, pages 16.2].**

39. No explanation was provided by the Department as to the inconsistency between Ms. Jaramillo's statement in the audit and her response to the Interrogatories (Response No. 3).

40. There was also no explanation given by the Department as to why Ms. Jaramillo disallowed all of the deductions if some of the receipts were deducted based on the nontaxable transaction certificates presented to her.

41. In two places in the audit for Santa Fe Tow, Ms. Jaramillo made references to Emergency Lock & Key and stated that "(t)he taxpayer is in the business of selling lock and key emergency services and was under/over reported for gross receipts. **[Exhibit G, pages AN1.3 and AN1.4].** This is an obvious error since the audit was for Santa Fe Tow and not Emergency Lock & Key.

42. Ms. Irene Jaramillo did not testify for the Department.

43. Mr. Beltran relocated his business to New Mexico from California at the behest of AAA. **[CD 05-18-15 0:45-0:46].**

44. Mr. Beltran had 25 to 27 trucks operating under the name of Santa Fe Tow. **[CD 05-18-15 0:43].**

45. Mr. Beltran had two trucks or vans operating under the name of Emergency Lock & Key. **[CD 05-18-15 0:43].**

46. Mr. Beltran has worked as an independent contractor for the American Automobile Association for 25 years. **[CD 05-18-15 0:45].**

47. During the audit period, AAA contracted with Taxpayers to provide emergency road services upon AAA's request, 24-hours a day, seven days a week. **[Exhibits 3, 4 and 5].**

48. AAA required Taxpayers to adhere to its standards of quality, to maintain insurance coverages that named AAA as a loss payee, and to prominently display AAA's service marks and other branding on Taxpayers' service vehicles, tow trucks, and the uniforms of Taxpayers' drivers. **[Exhibits 9, 10, 13, 14, and 20].**

49. Taxpayers' trucks and vans always displayed AAA's service marks and other branding. **[Exhibit 14].**

50. Taxpayers' trucks and vans always displayed Santa Fe Tow's marks. **[Exhibit 14, pages 14.1, 14.4 and 14.5].**

51. Taxpayers' drivers always wore uniforms with AAA's brand even if responding to any other calls. **[Exhibit 20, pages 20.1, 20.2, 20.3 and 20.4].**

52. Taxpayers' drivers always wore uniforms with Santa Fe Tow's brand. **[Exhibit 20, pages 20.1 and 20.3].**

53. AAA required Taxpayers to comply with the policies, rules and standards established by its "Highway Heroes Have H.E.A.R.T." ("HEART") and "Orientation for Independent Contract Stations" ("Orientation") manuals (collectively known as "manuals"). **[Exhibits 6 and 7].**

54. The contract between AAA and Taxpayers does not mention or require Taxpayers to adhere to the manuals. **[Exhibits 3, 4, and 5].**

55. The Orientation manual is a AAA document which is a training manual for Taxpayers' drivers. **[Exhibit 7, page 7.3].**

56. The Orientation manual is extremely specific in the manner in which Taxpayers' employees are to perform services for Taxpayers. **[Exhibit 7].**

57. The Orientation manual instructed Taxpayers' drivers to think of themselves as "stand[ing] for the quality service and reputation of AAA-New Mexico and the American Automobile Association (AAA)." **[Exhibit 7, page 7.12].**

58. The HEART manual was provided to Taxpayers, and Taxpayers' drivers were instructed by the Manual to view themselves as the "savior" of AAA's members and characterized

Taxpayers' employees as "one of the most important persons in the process of providing service to AAA members." **[Exhibit 6, page 6.3].**

59. The HEART manual set out the standards on the appearance of Taxpayers' service vehicles and tow trucks and the appearance of Taxpayers' employees. **[Exhibit 6, pages 6.9-6.18].**

60. The HEART manual states that the driver's adherence to standards is necessary "to project credibility and professionalism in this industry, and for the member to associate you with AAA." **[Exhibit 6, page 6.11].**

61. The HEART manual required drivers to keep in their vehicles a plastic laminated set of instructions for addressing its members as they rendered roadside service to the members. **[Exhibit 11].**

62. AAA also provided Taxpayers with a checklist of items each tow truck or service driver was required to perform in responding to a call from a member from AAA. **[Exhibit 11].**

63. A tow truck or service driver was required to greet each member by using their surname and offering the member a bottle of water bearing the mark of AAA, verify the member's identity and membership number. **[Exhibit 11, page 11.1; Exhibit 21, page 21.1].**

64. The Orientation manual instructed employees on how to interpret and understand the member's identification numbers. **[Exhibit 7, pages 7.22-7.23].**

65. AAA members received services by calling AAA at the 1-800 number on the back of the members' cards. **[CD 05-18-15 1:09; Exhibit 15.1].**

66. AAA utilized a software system that Taxpayers were required to use that would then select the closest driver. Using the AAA software system, Taxpayers would then dispatch the driver using a specially configured cell phone that would alert the driver with information about

the service call. **[CD 05-18-15 1:09-1:10; CD 05-18-15 1:57-2:12; Exhibit 22, page 22.1 and Exhibit 23, pages 23.1 and 23.2].**

67. Once a driver was dispatched to respond to a AAA member's request for service, Taxpayers role was to monitor the progress of the call on the computer system, the progress of the driver's response, and the amount of time elapsed. **[CD 05-18-15 1:57-2:12].**

68. Taxpayers' dispatchers updated the system by including comments on the progress of the service and they would call AAA members to notify them of the progress of the driver. **[CD 05-18-15 2:12].**[1]

69. The contract between Taxpayers and AAA provided that Taxpayers would receive payment from AAA according to a fixed rate schedule. **[Exhibit 4, page 4.2].**

70. Taxpayers did not receive any reimbursement from AAA members but instead AAA members paid AAA a membership fee.

71. Nothing within the contract provided that Taxpayers were responsible for any gross receipts tax. **[Exhibits 3, 4 and 5].**[2]

72. The contract provided that it was the express intention of both Taxpayers and AAA that Taxpayers were not "agents" of AAA and prohibited Taxpayers from representing that they were agents of AAA. **[Exhibit 3, page 3.4, Exhibit 4 page 4.4 and Exhibit 5, page 5.5].**

73. The contract between Taxpayers and AAA provided that Taxpayers were independent contractors and that Taxpayers retained "exclusive direction and control" of

[1] There were no changes or amendments to the contract during the audit period.

[2] The Department alleged in its Post-Hearing Brief that the contract between Taxpayers and AAA provided that Taxpayers were "responsible for payment of all taxes." The Department cited to the audio file at 16:52 (16 minutes and 52 seconds) and the contract. The audio file at 16:52 does not support Mr. Breen's statement that Taxpayers were responsible for payment of all taxes. In fact, the citation to the audio file has nothing to do with the terms of the contract. In addition, the contract only provides that Taxpayers were responsible for "withholding for social security, income tax and unemployment compensation, as well as providing workers' compensation insurance." [Exhibit 3, page 3.4].

Taxpayers' employees. **[Exhibit 3, page 3.4, Exhibit 4 page 4.4 and Exhibit 5, page 5.5].**

74. Prior to hiring employees and as a condition to allow Taxpayers' drivers to provide services to AAA members, Taxpayers were instructed that all prospective and current employees be vetted through HireRight, a company that performed on-line background checks. **[CD 05-18-15 1:23-1:25].**

75. AAA instructed Taxpayers which employees did not "meet the requirements" (pass the background check) and Mr. Beltran believed that his contract would be terminated if he did not terminate any employee who did not pass the background check. **[CD 05-18-15 1:25].**

76. At least three of Taxpayers' employees were terminated because they either failed the background check or they did not follow the quality standards of AAA. **[CD 05-18-15 1:26-1:27].**

77. AAA told Taxpayers that a driver with a DWI could not service AAA members and Taxpayers terminated that employee. **[CD 05-18-15 1:26-1:28].**

78. AAA directly paid all expenses to HireRight. **[CD 05-18-15 1:24-1:25].**

79. Taxpayers's net revenue after expenses incurred as a result of its contract with AAA was:

Emergency Lock & Key

2007	2008	2009	2010	2011
$36,721.32	$126,724.40	$58,010.33	$87,392.93	$25,500.95

[Exhibit 19].

Santa Fe Tow

2007	2008	2009	2010	2011
$180,688.71	$214,844.99	$119,789.16	$206,171.05	$101,486.68

[Exhibit 18].

80. For Taxpayers' employees, Taxpayers were required to provide "withholding for social security, income tax and unemployment compensation, as well as providing workers' compensation insurance." **[Exhibit 3, page 3.4].**

81. Under the terms of the contract, Taxpayers were required to maintain liability insurance in the amounts determined by AAA. **[Exhibit 3, page 3.5].**

82. There was no written contract between the AAA and any of the employees working for Taxpayers.

83. In the contract, Taxpayers agreed to indemnify AAA from any and all claims, suits, demands, actions, or proceedings of every nature and description committed by Taxpayers' employees. **[Exhibit 13, page 3.4-3.5].**

DISCUSSION

The central issue in this case is whether Taxpayers' receipts were received from AAA in a disclosed agency relationship. Taxpayers argued that even though the contract between AAA and Taxpayers did not expressly give Taxpayers the authority to bind AAA in contract, Taxpayers had apparent authority to act on AAA's behalf, so therefore, Taxpayers were a disclosed agent for AAA.

Burden of Proof and Standard of Review.

Section 7-1-17(C) provides that any assessment of taxes made by the Department is presumed to be correct. NMSA 1978, §7-1-17(C) (2007). Accordingly, it is taxpayer's burden to present evidence and legal argument to show that it is entitled to an abatement, in full or in part, of the assessment issued against it. *See, TPL, Inc. v. Taxation and Revenue Dep't.*, 2000-NMCA-083, ¶8, 129 N.M. 539, *rev'd on other grounds*, 2003-NMSC-7, 133 N.M. 447. When a taxpayer presents sufficient evidence to rebut the presumption, the burden shifts to the Department to show

that the assessment is correct. *See, MPC LTD. v. N.M. Taxation and Revenue Dep't.*, 2003-NMCA-021, ¶ 13, 133 N.M. 217; *Grogan v. N.M. Taxation and Revenue Dep't.*, 2003-NMCA-033, ¶11, 133 N.M. 354. Under NMSA 1978, Section 7-1-17(C) (2007), the assessment issued in this case is presumed to be correct.

Consequently, Taxpayers have the burden to show that the Department's assessment is incorrect and establish that they were entitled to the exemption. *See Archuleta v. O'Cheskey*, 1972-NMCA-165, ¶7, 84 N.M. 428. The courts have held that "where an exemption or deduction from tax is claimed, the statute must be construed strictly in favor of the taxing authority, the right to the exemption or deduction must be clearly and unambiguously expressed in the statute, and the right must be clearly established by the taxpayers." *Wing Pawn Shop v. Taxation and Revenue Department*, 1991-NMCA-024, ¶16, 111 N.M. 735.

Gross Receipts.

In New Mexico, the general rule is that services performed within the State of New Mexico are taxable. The term "gross receipts" is broadly defined in Section 7-9-3.5(A)(1):

> "gross receipts" means the total amount of money or the value of other consideration received from selling property in New Mexico, from leasing or licensing property employed in New Mexico, from granting a right to use a franchise 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 services exchanged, "gross receipts" means the reasonable value of the property or services exchanged;

NMSA 1978, §7-9-3.5(A) (1) (2003).

The Gross Receipts and Compensating Tax Act, Sections 7-9-1 through 114, defines "service" as "all activities … which activities involve predominately the performance of a service as distinguished from selling or leasing property. … In determining what a service is, the intended

use, principal objective or ultimate objective of the contracting parties shall not be controlling." NMSA 1978, §7-9-3(M) (2003). The Supreme Court in 1937 decided in *Comer v. State Tax Comm'n,* 1937-NMSC-032, ¶37, 41 N.M. 403 that gross receipts shall include "all activities or acts engaged in (personal, professional and corporate) or caused to be engaged in with the object of gain, benefit[,] or advantage either direct or indirect."

In addition thereto, it is presumed that "all receipts of a person engaging in business are subject to the gross receipts tax." NMSA 1978, §7-9-5 (2002). Therefore, the presumption is that Taxpayers' receipts from the services that Taxpayers provided to AAA which included providing emergency roadside services to AAA members are taxable. NMSA 1978, §7-9-5(A) (2002).

Disclosed Agent.

Business relationships have become more complex and they no longer fit neatly into one classification: agent/principal, employee/employer, or independent contractor/business. As these relationships have become more complicated and less predictable, the Department's statutes and regulations either have become more flexible or immutable, depending on whether you are the taxpayer or the Department.

Taxpayers argued that while the receipts that they received from AAA were gross receipts, the receipts were not taxable to Taxpayers because an exemption applied to the receipts or that Taxpayers received these receipts in a disclosed agency capacity for AAA pursuant to NMSA 1978, Section 7-9-3(F)(2)(f) (1994) (for periods before June 15, 2007) and NMSA 1978, Section 7-9-3.5(A)(3)(f)(2007) (for periods on or after June 15, 2007).[3] Section 7-9-3.5(A)(3)(f) states that excluded from gross receipts are "amounts received solely on behalf of another in a disclosed

[3] The Hearing Officer applied the statute and the regulation in place at the time the tax was due. *See, Kewanee Indus. Inc. v. Reese*, 1993-NMSC-006, 114 N.M. 784.

agency capacity." The Department defines what the test is to determine whether an agency relationship exists. Regulation 3.2.1.19(C) (1) NMAC provides that "(a)n agency relationship exists if a person has the power to bind a principal in a contract with a third party so that the third party can enforce the contractual obligation against the principal." Taxpayers argued that all of their receipts from AAA should be exempted because Taxpayers had apparent authority to act on behalf of AAA.

For Taxpayers to prevail on this issue, the Hearing Officer would have to find the contract between AAA and Taxpayers void and she would have to find that regulation 3.2.1.19(C) (1) allows for a disclosed agency relationship to exist if there is apparent authority. Taxpayers concede that Taxpayers did not have actual authority to act as an agent for AAA, but they argue Taxpayers had apparent authority to act on AAA's behalf. Taxpayers cited to *Diversified Dev. & Inv., Inc. v. Heil*, 1995-NMSC-005, 119 N.M. 290, 296 (apparent authority arises from manifestations by the principal to the third party and can be created by appointing a person to a position that carries with it generally recognized duties). Taxpayers urged the Hearing Officer to look only to words and acts of the principal. *Brown v. Cooley*, 1952-NMSC-083, 56 N.M. 630, 635 (whether an agency exists is a question of fact to be determined from the circumstances of each case). Taxpayers further argued that a principal's control over the agent is a key characteristic of an agency relationship, and if present may establish an apparent agency relationship. *Gallegos v. Citizens Ins. Agency*, 1989-NMSC-055,108 N.M. 722, 729.

Actual Agency Relationship.

Regulation 3.3.1.19(C)(1) makes it quite clear that to establish a disclosed agency relationship, there must be proof of an actual agency relationship. The Department's regulation provides that "(a)n agency relationship exists if a person has the power to bind a principal in a

contract with a third party so that the third party can enforce the contractual obligation against the principal." Regulation 3.2.1.19(C) (1) NMAC. The language in the regulation provides that the agent must be able to bind the principal in a contract with a third party. Because of the requirement that the agent must be able to bind the principal in contract with a third party, the regulation requires more than an oral contract between the principal to the agent. The terms of a contract between a third party and a principal can only be enforced if the contract is in writing. It is a general rule of law that one who is not a party to a contract cannot maintain suit upon it. *Staley v. New*, 1952-NMSC-102, 56 N.M. 756; *Fleet Mortg. Corp. v. Schuster*,1991-NMSC-046, 112 N.M. 48.

Thus the regulation requires a written contractual relationship between the agent and the principal, and an actual agency relationship must exist and not an apparent agency relationship. In this case, there is a written binding contract between AAA which specifically provides that it is the express intention of Taxpayers and AAA that Taxpayers are not "agents" of AAA and in fact prohibits Taxpayers from representing themselves as agents of AAA. **[Exhibit 3, page 3.4, Exhibit 4 page 4.4 and Exhibit 5, page 5.5].**

There was no evidence introduced contradicting the intention of the parties, or that the intention of AAA was to designate Taxpayers as its agent. This provision of the contract controls and Taxpayers are not agents of AAA.

While not directly on point, the Court of Appeals in *Western Elec. Co. v. N.M. Bureau of Rev.,* 1976-NMCA-047, 90 N.M. 164, in determining whether a party to a written contract owed compensating taxes for transportation charges, looked to the terms of the contract in deciding whether an agency relationship existed. The Court determined that because the contract between Western Electric Company and Mountain Bell required the taxpayer to pay the transportation

charges on materials sold and returned, Western Electric was acting as an agent for Mountain Bell. The court reiterated that an agent is defined as a person authorized by another to act on his behalf and under his control.

Apparent Authority.

Taxpayers argued that the regulation requiring a contract should be given a broad reading because agency relationships may be established by oral statements and by actions of the principal to third parties. Even if, as a matter of law, the regulation contemplated that a disclosed agent could be established by apparent authority, there is not enough evidence that the members (third parties) were told by AAA that Taxpayers actions were those of AAA. The key to determine whether an apparent agency relationship existed is to ascertain whether AAA manifested any acts or words to its members indicating that Taxpayers were its agent.

There is no doubt that AAA controlled many aspects of how Taxpayers' drivers performed their services to AAA members. However, only the branding and service marks displayed on both Taxpayers' vehicles and uniforms are the only manifestations to the members that Taxpayers could be agents for AAA. The evidence established that AAA required Taxpayers to prominently display AAA's service marks and other branding on Taxpayers' service vehicles, tow trucks, and the uniforms of Taxpayers' drivers. **[Exhibits 9, 10, 13, 14, and 20].** Taxpayers' trucks and vans always displayed AAA's service marks and other branding. Taxpayers' drivers always wore uniforms with AAA's brand even if responding to any other calls. **[Exhibit 20, pages 20.1, 20.2, 20.3 and 20.4].** However, in reviewing the pictures, the patches on the uniform state "AAA Roadside Assistance Provider" and "AAA New Mexico," but the uniform also displays a logo for "Santa Fe Tow." **[Exhibit 20, pages 20.1, 20.2, and 20.3].** The pictures of the vehicles also indicate that along with the "AAA" service mark is the "Santa Fe Tow" mark. **[Exhibit 14, page**

14.1, 14.4, and14.5]. In fact the phone number displayed on one tow truck, 344-3117, is the telephone number for Santa Fe Tow and not AAA. **[Exhibit 14, page 14.4].** And, most importantly, all of the branding and service marks on the vehicles and uniforms are acts on equipment owned by the agent and are not acts of the principal. To establish apparent authority, the relying party must base the relationship upon the words or acts of the principal. There is no evidence that the principal or AAA expressed to its members that Taxpayers were agents of AAA

Taxpayers argued that they acted as disclosed agents in the manner in which they delivered roadside services to AAA members. Taxpayers point out to many facts to support their position and the Hearing Officer acknowledges that AAA exerted control and cared about the quality and manner in which Taxpayers provided its services to AAA members. The facts supporting Taxpayers position are that AAA required Taxpayers to comply with the policies, rules and standards established by its manuals. **[Exhibits 6 and 7].** There is an Orientation manual that is a AAA document which is a training manual for Taxpayers' drivers. **[Exhibit 7, page 7.3].** The Orientation manual is extremely specific in the manner in which Taxpayers' employees are to perform services for Taxpayers. **[Exhibit 7].** The Orientation manual instructed Taxpayers' drivers to think of themselves as "stand[ing] for the quality service and reputation of AAA-New Mexico and the American Automobile Association (AAA)." **[Exhibit 7, page 7.12].**

Then there is the HEART manual instructing Taxpayers' drivers to view themselves as the "savior" of AAA's members and characterized Taxpayers' employees as "one of the most important persons in the process of providing service to AAA members." **[Exhibit 6, page 6.3].** The HEART manual set out the standards on the appearance of Taxpayers' service vehicles and tow trucks and the appearance of Taxpayers' employees. **[Exhibit 6, pages 6.9-6.18].** The

manual states that the driver's adherence to standards is necessary "to project credibility and professionalism in this industry, and for the member to associate you with AAA." **[Exhibit 6, page 6.11].** It also requires the drivers to keep in their vehicles a plastic laminated set of instructions for addressing its members as they rendered roadside service to the members. **[Exhibit 11].** However, there is nothing in the contract between AAA and Taxpayers that mentions that Taxpayers are required to adhere to the manuals. **[Exhibits 3, 4, and 5].**

AAA controlled how Taxpayers' driver interacted with customers. AAA provided Taxpayers with a checklist of items each tow truck or service driver was required to perform in responding to a call from a member from AAA. **[Exhibit 11].** A tow truck or service driver was required to greet each member by using their surname and offering the member a bottle of water bearing the mark of AAA, verify the member's identity and membership number. **[Exhibit 11, page 11.1; Exhibit 21, page 21.1].**

AAA members did not call Taxpayers but received services by calling AAA at the 1-800 number on the bank of their cards. **[Exhibit 15.1].** AAA utilized a software system that Taxpayers were required to use that would then select the closest driver. Using the AAA software system, Taxpayers would then dispatch the driver using a specially configured cell phone that would alert the driver with information about the service call. **[CD 05-18-15 1:09-1:10; CD 05-18-15 1:57-2:12; Exhibit 22, page 22.1 and Exhibit 23, pages 23.1 and 23.2].** Once a driver was dispatched to respond to a AAA member's request for service, Taxpayers role was to monitor the progress of the call on the computer system, the progress of the driver's response, and the amount of time elapsed. **[CD 05-18-15 1:57-2:12].** Taxpayers' dispatchers updated the system by including comments on the progress of the service and they would call AAA members to notify them of the progress of the driver. **[CD 05-18-15 2:12].**

AAA had some control over who Taxpayers hired and retained, but only to the extent if an employee or driver did not pass a background check. Prior to hiring employees and as condition to allow Taxpayers' drivers to provide services to AAA members, Taxpayers were instructed that all prospective and current employees be vetted through HireRight, a company that performed on-line background checks. **[CD 05-18-15 1:23-1:25].** Mr. Beltran believed that his contract with AAA would be terminated if he did not hire or he did not terminate those employees who did not "meet the requirements" or pass a background check. **[CD 05-18-15 1:25].** At least three of Taxpayers' employees were terminated because they either failed to the background check or they did not follow the quality standards of AAA. **[CD 05-18-15 1:26-1:27].** However, it is interesting to note that AAA directly paid all expenses to HireRight and did not reimburse Taxpayers for this expense. **[CD 05-18-15 1:24-1:25].** These acts by the principal indicate that in dealing with a third party, HireRight, AAA dealt directly with the third party.

All of these facts clearly show that AAA had an interest in the quality and manner of work Taxpayers performed on behalf of its members. However, these manifestations of control over the quality and manner of work are not sufficient to void the terms of the contract which provide that Taxpayers retained "exclusive direction and control" of Taxpayers' employees. **[Exhibit 3, page 3.4].** In reviewing all of the cases cited to by Taxpayers, an apparent agency relationship was established when there was no written contract in effect. In this case, there is a contract between Taxpayers and AAA whose terms state that Taxpayers are not agents of AAA. In this case, the written contract provides that it is the express intention of Taxpayers and AAA that Taxpayers are not "agents" of AAA. **[Exhibit 3, page 3.4, Exhibit 4 page 4.4 and Exhibit 5, page 5.5].** The contract is not void and the terms of the contract controls.

In reviewing all the facts, the written contract controls that Taxpayers were not agents of AAA. Taxpayers' argument fails to prove that an agency relationship existed between AAA and Taxpayers because the contract provides that Taxpayers did not have actual authority or the power to bind a principal in a contract with a third party so that the third party can enforce the contractual obligation against the principal.

Employee Relationship.

As an aside, in some ways the relationship between AAA and Taxpayers is somewhat like that of an employer and employee where the employer has the right to exercise control over the means of accomplishing a result or only over the result. Regulation 3.2.105.7(A)(7) NMAC. The regulation establishing whether an independent contractor is an employee also requires that the presumed employer withhold taxes and make unemployment insurance contributions. Regulation 3.2.105.7(A)(2)(3)(4)(5) NMAC. AAA did not withhold any taxes or make unemployment insurance contributions on behalf of any of Taxpayers' employees. In fact, the contract requires Taxpayers to withhold "social security, income tax and unemployment compensation, as well as providing workers' compensation insurance" for its employees. **[Exhibit 3, page 3.4].**

Members' Receipts.

The other problem with Taxpayers' argument is that there was no financial relationship between the members and Taxpayers. The exemption under either Section 7-9-3(F)(2)(f) (1994) or NMSA 1978, Section 7-9-3.5(A)(3)(f)(2007) requires that the receipts received by the agent from the third party are really meant for the principal and not the agent. In this case, the members never remitted any fees to Taxpayers. There are no amounts received solely on behalf of another. If the exemption is to apply, the receipts received by the agent must be received "solely on behalf of another in a disclosed agency capacity." *Carlsberg Mgmt. Co. v. Taxation and Revenue*

Dep't.,1993-NMCA-121, 116 N.M. 247 (an agent for a disclosed principal is, therefore, not liable for sales-type taxes on amounts for which he is reimbursed by his principal.). Taxpayers did not receive any amount solely on behalf of another. Taxpayers received amounts from the principal on their own behalf. Therefore Taxpayers cannot be a disclosed agent for AAA.

Civil Penalty.

At the hearing, the hearing officer ordered that penalty be abated because Taxpayers provided more than sufficient evidence through the testimony of Mr. Beltran that he reasonably relied on a competent certified public accountant, Mr. McKinney, to provide him with advice that the receipts from AAA were received in a disclosed agency capacity. The Department argued in its Post-Hearing Brief that penalty should not be abated because the contract was clear that Taxpayers were not agents and had Mr. McKinney read the contract, he would not have given advice to Taxpayers that they were agents for AAA. The Department's counsel fails to understand the regulation which only requires that a taxpayer fully disclose the facts to a certified public accountant and then the taxpayer must reasonably rely on the advice of the competent certified public accountant. There is no requirement that the advice given to the taxpayer be correct.

Civil penalty is imposed when a taxpayer is "negligent" or disregards the Department's rules and regulations in not filing a return or paying tax when it is due. Section 7-1-69(A) states that:

> (e)xcept as provided in Subsection C of this section, in the case of failure due to negligence or disregard of department rules and regulations, but without intent to evade or defeat a tax, to pay when due the amount of tax required to be paid, to pay in accordance with the provisions of Section 7-1-13.1 NMSA 1978 when required to do so or to file by the date required a return regardless of whether a tax is due, there shall be added to the amount assessed a penalty in an amount equal to the greater of:

> (1) two percent per month or any fraction of a month from the date the tax was due multiplied by the amount of tax due but not paid, not to exceed twenty percent of the tax due but not paid;

(Emphasis added). NMSA 1978, §7-1-69 (A) (1) (2007). The Department's regulation provides that "negligence" includes "failure to exercise ordinary business care and prudence which reasonable taxpayers would exercise under like circumstances; inaction where action is required; inadvertence, indifference, thoughtlessness, carelessness, erroneous belief or inattention" for either failing to file a return on time or failing to make a payment on time. Regulation 3.1.11.10 NMAC. Inadvertent error is defined as "negligence." See *El Centro Villa Nursing Ctr. v. Taxation & Revenue Dep't.*, 1989-NMCA-070, ¶14, 108 N.M. 795. The regulations provide exceptions to the negligence definition. The applicable exception is found in regulation 3.1.11.11(D) which provides that:

> (t)he taxpayer proves that the failure to pay tax or to file a return was caused by reasonable reliance on the advice of competent tax counsel or accountant as to the taxpayer's liability after full disclosure of all relevant facts; failure to make a timely filing of a tax return, however, is not excused by taxpayer's reliance on an agent;

To meet this regulation, it requires Taxpayers to prove that they reasonably relied on the advice of a competent accountant and that the competent accountant provided incorrect tax advice. The term "reasonable reliance" is a factual determination made by the Hearing Officer. It requires evidence that the taxpayer acted reasonably or acted in a "(f)air, proper or moderate under the circumstances" and the person exercised reliance or a "(d)ependence or trust" on the advice of a competent accountant. Black's Law Dictionary, 1379, 1404 (9th ed. 2009). This indication, as with the other indications of nonnegligence, are in keeping with the holding in *El Centro Villa Nursing Ctr. v. Taxation & Revenue Dep't.*, where the court stated that "(u)nder the statutory definition of negligence, it is inappropriate to impose a penalty where the taxpayer as acted

reasonably in failing to report income or to pay taxes." *Id*. at ¶6. The court also held that a taxpayer is not relieved of his or her duty to ascertain the possible tax consequences of his action or inaction by abdicating this responsibility by merely appointing an accountant to act as an agent in tax matters. *Id*. at ¶14. Thus, in reading the regulation and *El Centro Villa,* the hiring of an accountant by itself is insufficient to prove that a taxpayer is nonnegligent. The taxpayer must act reasonably and he or she must have relied on the accountant's incorrect tax advice.

The Department has ruled in numerous cases that reasonable reliance on a CPA may be a reason for abatement of penalty especially when it seems clear from the evidence that the accountant provided "incorrect tax advice." See, Carlos Chavez Formerly dba Mayan Construction, Decision and Order No. 12-09 (the accountant failed to review the work of Taxpayer's employee and failed to properly advise Taxpayer of time deadlines), Jesus Hernandez, Decision and Order No. 11-16 (the accountant stated in a letter that he had provided taxpayer with incorrect advice), Wal-Mart, Decision and Order No. 06-07 (taxpayer relied on in-house tax accountants to form a subsidiary company to reduce state tax liability), Children's Orchard, Decision and Order No. 01-05 (taxpayer hired an accountant to give them advice to assist them in making sure their taxes were properly paid) and Eileen P. Cahoon, Decision and Order No. 98-38 (taxpayer relied on her accountant's advice in not providing a timely NTTC). But see, PPR Healthcare Staffing, Decision and Order No. 14-15 (no evidence introduced showing that the accountant had provided incorrect tax advice), and Marilyn Stock, Decision and Order No. 05-04 (taxpayer was not granted a refund of the penalty amount she paid even though she had relied on her CPA who used the wrong tax table in determining her tax liability).

In this case, Taxpayers were able to prove that Mr. McKinney was a certified public accountant and that he is competent. Mr. Beltran is not an attorney or a certified public

accountant. He believed and trusted Mr. McKinney's advice and acted on his advice. **[CD 05-18-15 1:07-1:08].** Mr. McKinney's advice was that the receipts were to be reported but that an exemption applied. **[CD 05-18-15 2:27-2:29].** The relationship between AAA and Taxpayers is unique and it was not unreasonable that Mr. McKinney believed that Taxpayers receipts were deductible. Taxpayers services are sold to AAA for which no nontaxable transaction certificate can be issued to AAA. AAA pays Taxpayers for services rendered based on a set payment schedule for each type of service for which no gross receipts tax can be added to each service rendered. Mr. McKinney attempted to reconcile all the facts and while his advice was incorrect, it was not entirely unreasonable. Therefore penalty is abated because Taxpayers met the requirements found within the exception for negligence.

CONCLUSIONS OF LAW

A. Taxpayers filed timely written protests on October 10, 2012, to the assessments issued under Letter Id Nos. L0837170496 and L1332888896 and jurisdiction lies over the parties and the subject matter of this protest.

B. The contract between AAA and Taxpayers provided that it was the express intention of Taxpayers and AAA that Taxpayers were not "agents" of AAA and prohibited Taxpayers from representing to third parties that Taxpayers were agents of AAA. **[Exhibit 3, page 3.4, Exhibit 4 page 4.4 and Exhibit 5, page 5.5].**

C. The contract between AAA and Taxpayers is not void and the terms of the contract control.

D. Taxpayers did not have apparent authority to bind AAA with third parties.

E. Taxpayers were not a disclosed agent for AAA and their receipts were not exempt.

F. AAA members did not reimburse Taxpayers for any expenses.

G. Taxpayers and their drivers were not employees of AAA.

H. Taxpayers did not present sufficient evidence to prove it was entitled to either an exemption or a deduction.

I. A certified public accountant provided advice to Taxpayers that the receipts from AAA were deductible.

J. Taxpayers reasonably relied on the advice.

K. Penalty is abated.

L. Interest is due and owing on the principal amount of tax due until the date the principal is paid.

M. Taxpayers owe gross receipts tax in the amount of $196,731.00 and $68,849.25 in principal for tax periods set out in the assessments.

For the foregoing reasons, the Taxpayers's protest **is DENIED**.

DATED: June 29, 2015.

Monica Ontiveros

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