

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

**IN THE MATTER OF THE PROTEST OF
GREG L. AND KIMBERLY HAYES
ID NO. 03-005938-00 0, TO ASSESSMENT
ISSUED UNDER LETTER ID L1737907200**

No. 07-21

DECISION AND ORDER

An administrative hearing on the above-referenced protest was held on November 28, 2007, before Margaret B. Alcock, Hearing Officer. The Taxation and Revenue Department (“Department”) was represented by Jeffrey W. Loubet, Special Assistant Attorney General. Greg L. and Kimberly Hayes were represented by Thomas Smidt, II, with Tax, Estate & Business Law, N.A., LLC. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. During the audit period at issue, Greg Hayes (“the Taxpayer”) was the owner of GLH Enterprises, Inc., a corporation that performed services as an independent sales representative for President Homes, Inc., a manufacturer of home packages.
2. Customers who purchased a home package received the plans and all construction materials necessary to build the home, except for finish work such as floor coverings and paint. GLH Enterprises, Inc. then guided the customer through the building process, including assistance in obtaining financing, required permits, and subcontract labor.
3. In order to promote the sale of home packages and better compete with builders of finished homes, the Taxpayer decided to build a model home as an example of the final product that customers could expect when they purchased a home package.

4. Toward the end of 2000, the Taxpayer obtained an owner/builder permit and began construction of a home using the same construction materials used in packages sold by President Homes.

5. The Taxpayer did not qualify to give nontaxable transaction certificates (NTTCs) to his vendors because he did not have a contractor's license, nor was he building the home for resale. As a result, the Taxpayer's vendors included the gross receipts tax they were required to pay the state as part of the sales price they charged to the Taxpayer.

6. The amount of gross receipts tax included in the price the Taxpayer paid for labor and materials used to build his first model home was \$7,850.

7. The Taxpayer completed construction in May 2001, and for over a year he used the finished home as an office for his corporation and a model to promote the sale of home packages manufactured by President Homes.

8. The Taxpayer did not represent the model home as being for sale, display a for-sale sign on the property, or engage the services of a realtor. As a marketing tool for his home packages, he did enter the home in the local home builders' "Parade of Homes."

9. After construction of the model home was completed, the Taxpayer decided to apply for a contractor's license.

10. In September 2001, the Taxpayer was certified as a qualifying party under the Construction Industries Licensing Act, and a contractor's license was issued to his corporation, GLH Enterprises, Inc.

11. In the summer of 2002, a couple toured the Taxpayer's model home and asked if they could buy the model itself, rather than purchasing a home package and building their own home.

12. In August 2002, the Taxpayer sold the model home for \$238,000, netting a profit of approximately \$57,000.

13. The Taxpayer reported his gain from the sale of the home on his 2002 federal income tax return, but did not report New Mexico gross receipts tax on the sale proceeds.

14. After the sale of his first model home, the Taxpayer built a second model home, using his corporation's contractor's license to obtain the building permit.

15. Although GLH Enterprises, Inc. could have obtained NTTCs to use in purchasing construction materials and labor, the Taxpayer was unfamiliar with New Mexico's tax laws and did not apply to the Department to execute NTTCs. Instead, the Taxpayer paid the passed-on gross receipts tax charged by his suppliers.

16. The amount of gross receipts tax included in the price the Taxpayer paid for labor and materials used to build the second model home was \$11,870.

17. The Taxpayer did not advertise his second model home for sale, but again entered it in the "Parade of Homes" and received an offer on the home within a short time after its completion.

18. In February 2003, six months after the sale of the first model home, the Taxpayer sold his second model home for \$315,000, netting a profit of approximately \$66,600.

19. The Taxpayer reported his gain from the second model home on his 2003 federal income tax return, but did not report New Mexico gross receipts tax on the sale proceeds.

20. During the next three years, the Taxpayer built and sold two more homes under his contractor's license and intends to continue in the business of residential construction.

21. After completing his second model home, the Taxpayer learned about the deduction from gross receipts available to vendors of construction materials and labor who receive an NTTC from a licensed contractor.

22. When constructing his third and subsequent homes, the Taxpayer provided NTTCs to the vendors from whom he purchased construction materials and labor and reported gross receipts tax on the sales price of the completed construction projects.

23. In 2004, the Taxpayer was audited by the Department.

24. The auditor concluded that the Taxpayer was in the construction business and should have paid gross receipts tax on his receipts from the sale of his first two model homes, less the value of the underlying land.

25. On August 4, 2004, the Department assessed the Taxpayer for \$26,990.46 of gross receipts tax, plus interest, for reporting periods July 2001 through June 2004.

26. The Taxpayer received a 60-day extension of time to protest the assessment and filed his protest on November 2, 2004.

DISCUSSION

The Taxpayer raises the following arguments in support of his protest: (1) the sale of the two model homes at issue were isolated or occasional transactions entitled to the exemption provided in NMSA 1978, § 7-9-28; and (2) if the sales do not qualify as isolated and occasional, the Taxpayer should be given credit for the gross receipts tax his vendors included as part of the sales price of construction materials and labor the Taxpayer purchased to build his model homes.

Exemption for Isolated or Occasional Sales. The Taxpayer argues that his receipts from the sale of the first two model homes he constructed are exempt from tax under NMSA 1978, § 7-9-28, which states:

Exempted from the gross receipts tax are the receipts from the isolated or occasional sale of or leasing of property or a service by a person who is neither regularly engaged nor holding himself out as engaged in the business of selling or leasing the same or similar property or service.

Based on the facts presented, the Taxpayer qualifies for this exemption on the sale of his first model home, but not on the second.

Construction and Sale of First Model Home. The Taxpayer constructed his first model home to promote the sale of home packages by his wholly-owned corporation, GLH Enterprises, Inc. The Taxpayer believed that he could better compete with builders of finished homes by giving potential customers a tangible example of the final product they could expect when purchasing a home package. In late 2000, the Taxpayer obtained a permit as an owner/builder and began construction using the same materials used in home packages sold by President Homes. The Taxpayer did not have a contractor's license and did not intend to sell the completed home. Instead, the Taxpayer intended to use—and did use—the home as an office for his corporation and a model to promote the corporation's sale of home packages. More than a year after construction was completed, the Taxpayer was approached by a couple who wanted to purchase the model instead of building a similar home from a package. Given these facts, the Taxpayer's sale of his first model home in August 2002 qualifies as an isolated sale by a person who was not regularly engaged in the business of selling finished homes.

Construction and Sale of Second Model Home. After the sale of the first model home, the Taxpayer proceeded to build a second home. The Taxpayer maintains that at the time the second home was built, his business was still limited to the sale of home packages rather than the sale of finished homes. In fact, the Taxpayer was engaged in both of these businesses. In *Besser Co. v. Bureau of Revenue*, 74 N.M. 377, 383, 394 P.2d 141, 146 (1964), the New Mexico Supreme Court held that the number of transactions entered into does not control whether those transactions are isolated and occasional. Instead, the “real question is whether the sale or lease is in line with the business for which the seller or lessor was organized and in which it engages.” *Id.* In *Continental Inn of Albuquerque, Inc. v. New Mexico Taxation and Revenue Department*, 113 N.M. 588, 590, 829

P.2d 946, 948 (Ct. App. 1992), the court of appeals held that a taxpayer who held a contractor's license and constructed a hotel in New Mexico was "engaged in the construction business" even though the taxpayer intended to own and operate—rather than sell—the completed structure. *See also*, Department Regulation 3.2.116.9 NMAC (taxpayer may not claim the exemption for isolated and occasional sales if the taxpayer is licensed to sell property or carry on services that are the same or similar to those being sold).

In this case, the Taxpayer built his first model home under an owner/builder permit. By the time he began construction of the second home, the Taxpayer had taken the exam to be certified as a qualifying party under the Construction Industries Licensing Act. He then used his position as a qualifying party to obtain a contractor's license for his wholly-owned corporation, and the corporation applied for the permit to build the second model home. Upon completion, the Taxpayer did not actively advertise the home for sale. He did, however, enter it in the "Parade of Homes" and testified that he was open to selling if the price was right. Unlike his first home, which was used as an office and demonstration model for well over a year before it was sold, the Taxpayer's second home was sold in February 2003, just a few months after construction began in August 2002. During the next three years, the Taxpayer used his contractor's license to build and sell two more homes and has acknowledged that he intends to build more homes in the future.

The Taxpayer's contention that he built his first model home for the sole purpose of providing an office for his corporation and a model for potential customers of home packages is plausible and conforms to the facts presented. His testimony that this was the only motivation for constructing the second home is less persuasive. The Taxpayer's decision to obtain a contractor's license, together with his successive construction and sale of three additional homes, support the conclusion that the unplanned—but profitable—sale of his first model home led the Taxpayer to

enter the residential construction business. The fact that he continued his business of selling home packages on behalf of President Homes does not affect this conclusion. *See, Kewanee Industries, Inc. v. Reese*, 114 N.M. 784, 792, 845 P.2d 1238, 1246 (1993) (rejecting Kewanee's argument that its leasing of draglines was isolated and occasional because it was not typical of its regular oil and gas business). Because he was a licensed contractor engaged in constructing residential homes, the Taxpayer is liable for gross receipts tax on the February 2003 sale of his second model home.

Credit for Gross Receipts Tax Charged by Suppliers. When the Taxpayer purchased construction materials and labor to build his first two model homes, the vendors included the gross receipts tax they were required to pay on each transaction as part of the sales price. After the Taxpayer obtained his contractor's license, he had the option of providing his vendors with NTTCs to avoid the cost of the passed-on gross receipts tax. *See, NMSA 1978, §§ 7-9-51 and 7-9-52* (allowing sellers of construction materials and services to deduct receipts from sales to a person engaged in the construction business, provided that person delivers an NTTC to the seller). Unfortunately, the Taxpayer was unfamiliar with New Mexico's tax laws and never filed an application for NTTCs with the Department. As a result, his suppliers were not eligible for the deductions provided in §§ 7-9-51 and 7-9-52.

The Taxpayer maintains that he is entitled to a credit for the gross receipts tax his vendors paid to the state when the Taxpayer failed to provide them with NTTCs. The Taxpayer argues that the New Mexico Legislature did not intend construction materials and labor to be taxed both at the time they are purchased and at the time they are sold as part of a completed structure. The Taxpayer believes that taxing him on his receipts from the sale of his second model home without giving him credit for the taxes his suppliers paid and passed on to him results in double taxation.

The Taxpayer's arguments reflect a misunderstanding of New Mexico's gross receipts tax. More than 30 years ago, the New Mexico Court of Appeals rejected the argument that taxing the receipts of different taxpayers in successive transactions constitutes double taxation or violates New Mexico's tax laws or constitution. *House of Carpets, Inc. v. Bureau of Revenue*, 84 N.M. 747, 507 P.2d 1078 (Ct. App. 1973). See also, *New Mexico Sheriffs and Police Association v. Bureau of Revenue*, 85 N.M. 565, 514 P.2d 616 (Ct. App. 1973); *New Mexico Enterprises, Inc. v. Bureau of Revenue*, 86 N.M. 799, 528 P.2d 212 (Ct. App. 1974). In this case, the Taxpayer and his vendors are separate taxpayers, each of which is engaged in business in New Mexico. The gross receipts tax is imposed—once—on a vendor's receipts from selling construction materials or services to the Taxpayer. The gross receipts tax is also imposed—once—on the Taxpayer's receipts from selling the completed construction project. Under these facts, there is no double taxation.

The issue of legislative intent was addressed in Judge Hendley's specially concurring opinion in *House of Carpets, supra*:

It is taxpayer's contention that it is the legislative intent, as manifested by the provisions permitting the deduction of receipts from sales for resale, that the tax "... be assessed but once." Assuming, without deciding, that taxpayer's statement of the legislative purpose is correct, taxpayer still cannot prevail. As we said in *Reed v. Jones*, 81 N.M. 481, 468 P.2d 882 (Ct.App.1970):

"... The burden is on the taxpayer to establish clearly his right to the deduction...."

In the present case the Legislature has provided the means for the tax to be assessed but once, namely, by using nontaxable transaction certificates. Not having availed himself of the means for avoiding the tax in question, taxpayer is left with the presumption of taxability.

84 N.M. at 752, 507 P.2d at 1083. Judge Hendley's conclusion is supported by a long line of cases holding 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 taxpayer. *Wing Pawn Shop v. Taxation and Revenue Department*, 111 N.M. 735, 740, 809 P.2d 649, 654 (Ct. App. 1991); *Security Escrow Corp. v. Taxation and Revenue Department*, 107 N.M. 540, 543, 760 P.2d 1306, 1309 (Ct. App. 1988). Taxation is the rule and the claimant for an exemption must show that his demand is within the letter as well as the spirit of the law. *Id.*

The Gross Receipts and Compensating Tax Act provides a deduction for receipts from selling construction materials and services to a buyer who delivers an NTTC to the seller. The requirements for claiming the deduction are clear and unambiguous. The deduction is available to the seller—not the buyer—and is predicated on the seller’s receipt of an NTTC. No provision of New Mexico law supports the Taxpayer’s claim to a credit for gross receipts tax paid by his vendors in the absence of required NTTCs.

CONCLUSIONS OF LAW

A. The Taxpayer filed a timely, written protest to the assessment issued under Letter ID L1737907200, and jurisdiction lies over the parties and the subject matter of this protest.

B. The Taxpayer’s August 2002 sale of his first model home was an isolated or occasional transaction, and the receipts from that sale qualify for the deduction provided in NMSA 1978, § 7-9-28.

C. Once the Taxpayer acquired a contractor’s license and began construction of his second model home, he was engaged in the residential construction business and his receipts from the February 2003 sale of the second home does not qualify for the deduction provided in NMSA 1978, § 7-9-28.

D. The Taxpayer is not entitled to a credit for the gross receipts tax his vendors were required to pay to the state and included as part of the sales price of construction materials and labor the Taxpayer purchased to build his model homes.

For the foregoing reasons, the Taxpayer's protest IS GRANTED IN PART AND DENIED IN PART. The Department is ordered to abate the gross receipts tax and related interest assessed on the Taxpayer's receipts from selling his first model home in August 2002. The Taxpayer remains liable for the gross receipts tax and accrued interest assessed on his receipts from the sale of his second model home in February 2003.

Dated December 5, 2007.