

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

**IN THE MATTER OF THE PROTEST OF
SUNROOMS PLUS, INC.
TO ASSESSMENT ISSUED UNDER LETTER
ID NO. L2080690688**

No. 11-20

DECISION AND ORDER

A formal hearing on the above-referenced protest was held on May 11, 2010, before Monica Ontiveros, Hearing Officer. The Taxation and Revenue Department (“Department”) was represented by Ida M. Luján, attorney for the Department. On June 10, 2010, Sunrooms Plus, Inc. (“Taxpayer”) filed its closing argument. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. Taxpayer was a New Mexico corporation doing business in New Mexico from 1989 until sometime in 2004.
2. Larry A. Chavez, former president of Taxpayer, represented Taxpayer and testified on Taxpayer’s behalf. Mr. Chavez was the sole owner of Taxpayer.
3. The Department assessed Taxpayer on December 29, 2004, in gross receipts tax in the amount of \$536,614.78 in principal, \$54,228.97 in penalty and \$194,729.57 in interest for a total of \$785,573.32 for the tax period of January 31, 2001 through December 31, 2003. The Department also assessed Taxpayer in withholding tax in the amount of \$2,850.89 in principal, 285.10 in penalty and \$952.65 in interest.
4. On January 27, 2005, Taxpayer filed a request for an extension to file a written protest.

5. On January 31, 2005, the Department granted the extension to file a written protest.
6. On or about March 30, 2005, Taxpayer filed a written protest to the assessment, which was accepted by the Department under a retroactive extension of time granted pursuant to NMSA 1978, Section 7-1-24 (B)(2003).
7. On January 22, 2010, the Department requested a hearing in this matter.
8. On February 3, 2010, the Hearings Bureau mailed a Notice of Administrative Hearing in this matter setting the hearing for May 11, 2010.
9. Taxpayer was in the business of selling and installing of sunrooms, spas, saunas, gazebos and patio covers in New Mexico and in Arizona. Taxpayer also sold pool tables, dry and wet bars, outdoor kitchens, and spa chemical and accessories. Taxpayer sold its maintenance service on spas and gazebos. Taxpayer ceased operating its business sometime in 2004.
10. In August 2003, the Department contacted Taxpayer and spoke with Mr. Chavez. Mr. Chavez was informed that Taxpayer had been selected for audit by the Department. Exhibit L, page GN1. An audit start date of September 10, 2003 was selected by both Taxpayer and the Department. Exhibit L, page GN1.
11. Taxpayer requested an extension of the start date of the audit. A new start date of February 24, 2004 for the audit was selected by the Department. Exhibits A and B.
12. On February 16, 2004, the Department formally notified Taxpayer in writing that it had been selected for audit and that the start date of the audit would be February 24, 2004. Exhibit A, page B9.1.
13. The Department conducted an audit of Taxpayer. The audit period was from

January 31, 2001 through December 31, 2003.

14. The Department's original auditor spent quite a bit of time trying to get the Taxpayer to provide documentation.

15. Taxpayer was required to produce the documents by the audit start date. Exhibits A and B.

16. On February 24, 2004, the Department began the audit of Taxpayer. Exhibit B, page B8.1. On December 13, 2004, the audit of Taxpayer was completed. Exhibit F.

17. On May 18, 2004, Taxpayer was notified that it had not provided the requested records or books necessary to complete the audit. The letter also provided that Taxpayer had until August 16, 2004 to provide additional records or books. Exhibit C, page B6.1.

18. On August 16, 2004, the day the documents were due to the Department, Taxpayer requested an extension of time to present its documents and promised to present its documents by November 16, 2004. Exhibit D, pages B5.1 through B6.3.

19. On November 5, 2004, the Department subpoenaed Taxpayer's records and books. Exhibit E.

20. On December 13, 2004, the audit concluded that Taxpayer owed \$536,614.78 in principal gross receipts tax due, plus penalty and interest, and \$2,850.89 in principal withholding tax. Exhibit L, page 1. The gross receipts tax resulted from underreporting of gross receipts.

21. Taxpayer filed and reported gross receipts returns for the audit period. Taxpayer also paid gross receipts taxes on the amount that it filed and reported.

22. On August 11, 2009, the Department made an adjustment to the amount of gross

receipts principal tax in the amount of \$296,771.44. (Adjustment #1). Exhibit M, page P-B.0.

23. Ms. Sylvia Sena, senior protest auditor, testified that in August 2009, there were several errors that she corrected on the audit. Exhibit M, page P-B.0. She made adjustments to the principal amount of gross receipts tax due and prepared work papers to reflect the corrections or adjustments. The corrections or adjustments she made were to correct the March 2001 percentage not being included in the revised work papers and carried forward to other work papers. She also made an upward adjustment to the tax rate and she gave Taxpayer credit for the reported receipts for the months of September, October and November 2003. Exhibit M, page P-B.0.

24. After Adjustment #1 was made the remaining amount of gross receipts principal tax due and owing was \$239,843.34.

25. On or about May 6, 2010, Ms. Sena made a second adjustment (Adjustment #2) to Taxpayer's liability by reducing the amount of principal in gross receipts tax by \$13,481.87, leaving \$226,361.47 in principal in gross receipts tax. Exhibit O.

26. The amounts made in Adjustment #2 were for various receipts for 2003 that were erroneously included as New Mexico gross receipts. Exhibit O.

27. After Adjustment #2 was made, the remaining amount of gross receipts principal tax due and owing was \$226,361.47. Exhibit O.

28. On May 11, 2010, the day of the hearing, the Department and Taxpayer entered into a Stipulation whereby the Department agreed to abate \$5,523.72 in principal gross receipts tax, leaving \$220,837.75 (Adjustment #3) in principal gross tax due and owing. Exhibit Q.

29. During the audit period, Taxpayer conducted business in New Mexico and Arizona.
30. The audit used the bank deposit method to determine the underreported gross receipts derived from New Mexico.
31. The exceptions reported in the audit were based on the auditor's review of bank statements and accounts and Taxpayer's contracts at Taxpayer's office in Albuquerque. The auditor determined the amount of gross receipts that should have been reported by comparing the amounts deposited into the bank accounts with those amounts reported on the gross receipts returns. The differences between income and what was reported were treated as unreported gross receipts. Exhibit L, page C5.1 through C5.6.
32. The Department made adjustments to the principal gross receipts tax after the audit was completed based on information that either should have been provided by Taxpayer or errors made by the original auditor assigned to the audit.
33. The audit determined that all of the income deposited into Taxpayer's bank account at Wells Fargo Bank was gross receipts because Taxpayer failed to provide any contracts to support a credit.
34. Taxpayer did not dispute that it owed withholding tax in the amount of the assessment or \$2,850.89 in principal tax.
35. Taxpayer conceded at the hearing that it was not contesting the gross receipts liability for tax year 2003.
36. Taxpayer used accounting software in its business and provided certain documents to the Department at various times.

37. Taxpayer argued that further adjustments should have been made to tax years 2001 and 2002 based on the documents provided to the Department and the lists he had provided to the Department. Taxpayer hired a college student, Michael Katz, to prepare a listing of amounts or receipts that should be excluded from gross receipts. Exhibit 1.

38. At the hearing, Taxpayer conceded that the crossed out receipts on Exhibit #1 were New Mexico gross receipts (D.Horton Casa \$16,753.95 and Invoice 2862 \$1,927.88). Exhibit 1.

39. Mr. Chavez testified that all other receipts on Exhibit #1, except those in finding of fact #38, were not gross receipts and therefore not taxable. Exhibit 1.

40. Mr. Chavez testified that the receipts from Del Sol Mortgage and Bryan Handing were loan proceeds and therefore not taxable. Exhibit 1.

41. Mr. Chavez testified that the receipt of \$2,500 was insurance proceeds from an insurance company for a stolen jack hammer. Exhibit 1.

42. Mr. Chavez testified that Taxpayer's business has been defunct since December 2004. He also testified that a series of catastrophes, including the death of Taxpayer's comptroller in December 1999 and the embezzlement of Taxpayers' funds, caused the business to fail.

43. Mr. Chavez testified that it was normal business practice for Taxpayer to pay cobra insurance payments of former employees and then be reimbursed by that employee. The reimbursements were deposited into Taxpayer's bank accounts.

44. Mr. Chavez testified that he used bank statements to create a list of non-sufficient fund checks.

DISCUSSION

The issue to be determined is whether Taxpayer underreported its gross receipts in the amount of \$220,837.75 in principal gross receipts tax. There are no legal issues in dispute. The only issues in dispute are factual in nature and deal with whether certain gross receipts are taxable. Taxpayer argued that miscellaneous receipts in the amount of \$92,950.44 for tax years 2001 and 2002 should be excluded from gross receipts because these amounts were not gross receipts. Taxpayer also argued that certain returned checks should be excluded from gross receipts for each tax year because the Department excluded other returned checks. Thirdly, Taxpayer argued that a different audit methodology should have been used and a maximum audit adjustment should be made. Finally, Taxpayer argued that penalty should be abated because of the many extenuating circumstances that occurred.

Burden of Proof.

Section 7-1-17 provides that any assessment of taxes made by the Department is presumed to be correct. NMSA 1978, Section 7-1-17 (2007). 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). 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. When a taxpayer presents evidence sufficient 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, 62 P.3d 308.

Audit

There was testimony presented by Mr. Chavez in which he complained that the Department made significant mistakes in the audit, and therefore by implication, the audit was not reliable. The audit that was conducted on Taxpayer's business was based on the bank deposit method of auditing. Exhibit L, page GN3. In the audit, the original auditor stated that this was an "(a)udit to bring the taxpayer into compliance with New Mexico tax laws and focuses specifically on the taxpayer's failure to report and pay gross receipts tax and withholding tax." Exhibit L, page GN1. Taxpayer had an accounting system to maintain its books called Peachtree accounting system. Taxpayer provided certain documents to the Department, but failed to provide all of the documents requested by the Department. Exhibit L, page GN1.

In arriving at the amount of tax due, the original auditor reviewed all of the bank statements, contracts and other documents provided and compared the bank deposits with the receipts reported. Exhibit L. Since Taxpayer also had out of state receipts from Arizona in its bank deposits, credit was given if Taxpayer was able to show that the receipt was from an out of state sale in Arizona. Exhibit L. The original auditor allocated the gross receipts to certain tax locations by reviewing the contracts she was provided, and then listed the construction in the corresponding municipality. Exhibit L, page GN3. The exceptions reported in the audit were based on the auditor's review of bank statements and accounts and Taxpayer's contracts at Taxpayer's office in Albuquerque. The auditor determined the amount of gross receipts that

should have been reported by comparing the amounts deposited into the bank accounts with those amounts reported on the gross receipts returns. The differences between income and what was reported were treated as unreported gross receipts. Exhibit L, page C5.1-C5.6.

The Department countered Mr. Chavez' argument by arguing that Mr. Chavez failed to produce the documents requested or failed to produce the documents in a timely manner. While the original auditor did not testify in this matter, her narrative suggests that she spent quite a bit of time trying to get Taxpayer to provide the requested documents. Exhibit L. The Department followed all of its required auditing procedures to notify Taxpayer that it had been selected for audit. It notified Taxpayer when the audit would begin, and it notified Taxpayer what documents it was requesting. Exhibits B, C and D. After initially requesting the documents, the Department notified Taxpayer that if it did not provide the requested documents by August 16, 2004, the Department would issue an assessment based on the documents presented. Exhibit C, page B6.1. On the day the documents were required to be produced, Taxpayer requested an extension of time to present its documents and promised to present its documents by November 16, 2004. Exhibit D, pages B5.1 through B6.3. Some documents were produced by November 16, 2004. The original auditor called Mr. Chavez and informed him that the documents were incomplete and she would need additional documents. Exhibit L, pages GN2 and GN3. An assessment was finally issued on December 29, 2004 only after the Department made numerous attempts at obtaining the requested documents.

Mr. Chavez complained that he provided the original auditor with documents but she rejected the documents. The audit narrative states that Mr. Chavez produced a number of

documents for the Department, like the “Chart of Accounts, W2s, Accounts Payable invoices, limited contracts, limited Sales Invoices, and Bank Statements” to name a few. Exhibit L, page GN1. However, the audit narrative also states that Taxpayer failed to provide copies of all contracts to the auditor. Exhibit L, page GN3. There are letters introduced from the Department to Taxpayer requesting additional documents. There are no corresponding letters that are part of the audit or were introduced at the hearing, from Taxpayer to the auditor confirming which documents the Department rejected. It is unclear why the original auditor when conducting the audit would have rejected some of the documents provided unless the documents were received after the audit was completed. The Hearing Officer will not speculate as to which documents were rejected or the reason they were rejected.

The Department contended that Mr. Chavez was a poor record keeper and he was the cause for the number of adjustments that had to be made to the audit. The Department argued that perhaps other deductions could have been made but that Mr. Chavez failed to produce the required documents. Mr. Chavez argued that any argument that he somehow intentionally caused the audit to be delayed was an unfair characterization of the events. He agreed that he did not provide the documents in a timely manner to the original auditor but there were extenuating circumstances. He credibly testified that he wanted to pay the liability but that the liability was overstated and since the company was no longer in business and defunct it was unclear how he would pay such an overstated liability. Mr. Chavez also testified that his company was defunct because of many unforeseen events. While Mr. Chavez’ reasons for not presenting the documents, the death of his comptroller three years prior to the audit, an employee who may have embezzled money and the

theft of his customer list may all be extenuating circumstances, a taxpayer is still required to present the documents requested by an auditor, and in indeed, it is to the taxpayer's benefit to present those documents.

The Department argued that the extenuating circumstances were not relevant. In response to this argument, Mr. Chavez further charged that it was the Department through Ms. Sena who caused some of the delay. He argued that after he filed the protest, he received a letter dated April 1, 2005 from the Department indicating that Ms. Sena was assigned to his protest and that she would be contacting him. He testified that Ms. Sena did not contact him until September 13, 2006. He further testified that he provided Ms. Sena with the majority of documents sometime in August 2007 and the adjustments were not made until August 2009. Ms. Sena testified that the Taxpayer should have called her.

Generally, Taxpayers "shall maintain books of account or other records in a manner that will permit the accurate computation of state taxes or provide information required by the statute under which he is required to keep records." NMSA 1978, Section 7-1-10(A)(2001). The Department's regulations provide that "(t)he adequacy or inadequacy of taxpayer records is a matter of fact to be determined by the secretary or secretary's delegate. Taxpayers have a duty to provide the secretary or secretary's delegate, upon request, with books of account and other records upon which to establish a basis for taxation." Regulation 3.1.5.8(A) NMAC (2000). The regulation further provides that "(f)ailure of a taxpayer to keep adequate books of account or other records will cause the department to use alternative methods to determine or estimate taxes dues." Regulation 3.1.5.8(B) NMAC (2000). "Alternative methods which may be used by the

department include, but are not limited to: (1) bank deposit method.” Regulation 3.1.5.8(C)(1) NMAC (2000).

In this case, Taxpayer had an obligation to keep its business records in an orderly manner and the Department had a right to request those documents. Ideally, all tax documents should be presented during the audit. If the documents are not presented during the audit and they are presented during the protest, then naturally adjustments will be made. The Hearing Officer did note that in Ms. Sena’s narrative dated August 11, 2009, she stated under Protest Notes that a number of corrections were made to the audit. Exhibit M, page P-B.0. In reviewing the Protest Notes, the Hearing Officer finds the three errors that Ms. Sena corrected on the original audit to be minor and not fundamental errors in the audit itself. Exhibit M, page P-B.0. The Hearing Officer rejects Mr. Chavez’ argument that the audit was unreliable and despite whatever errors occurred in the audit, the Department provided Taxpayer numerous opportunities to correct the liability.

Miscellaneous Receipts

Mr. Chavez argued that for tax years 2001 and 2002 certain miscellaneous amounts should be removed from the total amount of gross receipts because they were not gross receipts pursuant to NMSA 1978, Section 7-9-3.5(A)(1) (2007) which states that “ “gross receipts” means the total amount of money or the value of other consideration received from selling property in New Mexico...” Mr. Chavez argued that the amounts listed on his Exhibit 1 were really loan proceeds, reimbursements or other types of amounts that a large business receives in its normal course of business. At the hearing Mr. Chavez conceded the amount of tax liability for tax year 2003.

The total amount of gross receipts that Taxpayer is requesting be adjusted from gross

receipts is \$92,950.44. Taxpayer's Letter filed June 10, 2010. However, in reviewing Taxpayer's Exhibit 1, the amount Taxpayer appears to be disputing is \$70,826.21 for tax year 2001 and \$38,878.09 for tax year 2002. The calculations used in Taxpayer's Letter do not correspond with the testimony and Exhibit 1 presented at the hearing. The reasons for this are that the total amount listed for tax year 2002 was scratched out and another figure was written over this figure. Exhibit 1, page 2. In addition some of the receipts Taxpayer was disputing have been abated. Exhibit M, page P7.3. On Exhibit 1, Mr. Chavez stated that the amount in dispute was \$70,826.21 for tax year 2001 and \$45,470.04 for tax year 2002.

First, in reviewing the list of miscellaneous receipts, many of the receipts Taxpayer is disputing, the Department agreed to abate in August 2009. The receipts that the Department argued to abate in August 2009 are: January 2002-\$206.75 and \$565.30; February 2002-\$151 and \$206.75; March 2002-\$647.49 and \$206.75; April 2002-\$206.75; May 2002-\$38 and \$206.75; June 2002-\$206.75 and \$661; July 2002-\$206.75; August \$206.75; September \$16.75; October 2002-\$206.75; and November 2002-\$206.75 and \$517.15. There were two receipts that the Department made an adjustment for \$5,122.05 and \$34.81 but were not on Taxpayer's Exhibit 1. The Hearing Officer only reviewed those amounts that were on Exhibit 1 that were not abated.

At the hearing, time was spent reviewing some of the receipts listed on Taxpayer's Exhibit 1. Mr. Chavez did not present any documents other than the list of receipts itself, detailing what the receipts were used for. Mr. Chavez testified that he hired a college student, Michael Katz, to prepare Exhibit 1, the listing of receipts that should be excluded from gross receipts, and that the college student had reviewed bank statements to compile the list. Exhibit 1. Mr. Chavez also

testified that if Mr. Katz needed clarification, that he assisted him with whatever information he needed.

Testimony was provided by Mr. Chavez as to the miscellaneous disputed amounts on Exhibit 1. Mr. Chavez testified that the amounts were mischaracterized by the Department and were really loan proceeds, reimbursements, and other miscellaneous deposits entered into his bank accounts, but in any event they were not gross receipts. Mr. Chavez testified that Taxpayer was a large business and as a large business it was customary to receive deposits into its bank accounts that were not gross receipts. For example, Mr. Chavez testified that Taxpayer borrowed money from Del Sol Mortgage Company and that the deposits listed under Del Sol Mortgage Company were loan proceeds to Taxpayer. He also testified that the receipt of \$2,500 was insurance proceeds from an insurance company for a stolen jack hammer. The Bryan Handing payments were loan reimbursements according to Mr. Chavez.

Ms. Sena testified that as to all the receipts listed on Exhibit 1 for tax year 2001, she could not make any adjustments because there was no back-up documentation presented. Mr. Chavez presented no evidence other than the list to support an adjustment. However, in reviewing the employee list of the audit in Exhibit L, page E3.1, and comparing the list of employees with the cobra reimbursement receipts of former employees on Exhibit 1, James Zunno or Jim Zunno is listed as an employee who was employed in 2001. Exhibit L, page E3.1. There are two cobra receipts (6/14/2001 and 7/18/2001) listed for Jim Zunno totaling \$1,079.64. Mr. Chavez testified that it was normal business practice to pay the cobra insurance payments of former employees and then be reimbursed by that employee. Since Mr. Zunno is on the Department's own work papers

as an employee in 2001, the Hearing Officer finds Mr. Chavez' testimony credible as to the receipts being cobra reimbursements and not gross receipts. Therefore the amount of \$1,079.64 should be abated.

On Exhibit 1, for tax year 2002, there were two receipts in the amount of \$206.75 (September and December) for reimbursements received from a former employee named Lovato for cobra payments. The Department did not make adjustments for these amounts because Ms. Sena testified that even though she made adjustments for all other reimbursements in this exact amount, she was not provided with back-up documentation for those two months indicating there was an employee named Lovato who had left employment with Taxpayer. Mr. Chavez testified that the receipts of \$206.75 in September and December were for amounts received from a former employee named Lovato for the reimbursement of cobra payments. Because these two receipts are in the exact amount of the other Lovato reimbursement amounts, the Hearing Officer finds Mr. Chavez' testimony credible and the amount of \$413.50 should be abated.

As for any other receipts listed in Exhibit 1, the Hearing Officer finds that Mr. Chavez failed to provide any documents to show that the receipts in question were not gross receipts other than his testimony and therefore failed to rebut the presumption of correctness. The testimony and the list are insufficient evidence that the receipts listed by Taxpayer should be excluded from gross receipts from the audit. While Mr. Chavez' testimony is reliable, without supporting documentation like an affidavit from Mr. Handing or some kind of documentation that Del Sol Mortgage Company loaned money to Taxpayer, the Hearing Officer is unwilling to order any adjustments made because there was insufficient evidence presented by Taxpayer.

Non-Sufficient Fund Checks

Taxpayer argued that the Department should have made additional adjustments in the amount of \$20,500.91 as listed on Exhibit 2 for amounts that had been received as income but were returned as non-sufficient fund checks (NSF checks). Some of the NSF checks listed on Exhibit 2 were adjusted from the gross receipts in August 2009. Exhibit L, page P7.4. Ms. Sena testified that NSF fund checks were not taxable as gross receipts.

Once again Taxpayer's requested adjustment, in this case of \$20,500.91 and the total figures on Exhibit 2 do not correspond with the testimony and the evidence introduced at the hearing. If Taxpayer's Exhibit 2 is used and the NSF checks Ms. Sena already provided an adjustment for are subtracted out, then the amount in dispute as to the NSF checks is \$27,512.81.

At the hearing, time was spent reviewing each of the receipts listed on Taxpayer's Exhibit 2. Mr. Chavez prepared Exhibit 2 from reviewing his bank statements. On Taxpayer's Exhibit 2, the NSF checks listed included amounts the Department abated in August 2009 are: 2/9/01-\$200; 3/15/01-\$598; 4/9/01-\$500; 4/12/01-\$100; 4/16/01-\$500; 4/19/01-\$1,975; 4/24/01-\$16,477; 4/25/01-\$332; 5/1/01-\$12,358; 8/17/01-\$100; 8/23/01-\$10,387.50; 8/31/01-\$1,682; 2/26/02-\$496; 3/4/02-\$600; 3/25/02-\$500; 8/26/02-\$4,769.60; 11/21/02-\$500; and 12/23/02-\$1,237.56. Exhibit M, page P7.4. On May 6, 2010, the Department agreed to abate: 7/25/02-\$9,000; 10/1/02-\$9,043. Exhibit O. On Exhibits M and O, there were additional adjusted amounts that were not included on Taxpayer's Exhibit 2. The Hearing Officer only reviewed those amounts that were on Exhibit 2 that were not abated.

Ms. Sena testified that she initially made an adjustment of \$60,325.36 in August 2009 and

an adjustment in the amount of \$18,043.00 in May 2010 for NSF checks. Exhibit M, P7.4 and Exhibit Q. Ms. Sena testified that she made adjustments for NSF checks if she could trace on the bank statement the amounts that were not re-deposited. Ms. Sena also testified that she did not make an adjustment if Mr. Chavez did not present an Arizona return. Ms. Sena testified that the reason it was necessary to review the Arizona returns was that she had provided Taxpayer with adjustments for out of state sales based on the amounts reported on Arizona returns. She testified that she wanted to cross reference with the Arizona receipts because she did not want to give a double adjustment—one adjustment for out of state sale and the other adjustment for NSF. In other words, the adjustment could be both an Arizona out of state adjustment and a NSF adjustment.

What is not clear from Ms. Sena's testimony is why she was not able to cross reference with other information in the audit, like the list of New Mexico customers found in Exhibit L (unnumbered pages-Contracts per location) or how she would have been able to cross reference if no Arizona return was ever provided. If an Arizona return was never provided, then theoretically she never provided a credit for amounts reported as out of state sales by Taxpayer. Taxpayer had the opportunity to question Ms. Sena on the audit methods used to make the determination of whether to accept or reject amounts listed as NSF checks.

Taxpayer argued that the Department never presented any evidence to refute his testimony that the NSF checks were indeed checks returned for nonsufficient funds, and therefore not gross receipts. The Department did refute Taxpayer's argument by presenting its methodology as to why it made certain adjustments. Ms. Sena testified that if she could trace the NSF check, she

made an adjustment to the assessment. Ms. Sena testified that she wanted to trace the NSF check to the Arizona returns for purposes of making sure that no double credit or adjustment was made. Mr. Chavez argued that it was unclear why Ms. Sena needed the Arizona returns to support a NSF check deposited into a bank statement. While her testimony was not entirely clear, Ms. Sena's objective of making sure a double credit or adjustment was not being made is a reasonable one. Mr. Chavez argued that if a NSF check was re-deposited, then when the check was re-deposited, the amount would be considered income either in New Mexico or in Arizona. Regardless, however, because Mr. Chavez failed to provide bank statements showing that the remaining amounts listed on Exhibit 2 were NSF checks, his testimony alone is not sufficient for the Hearing Officer to make the requested adjustments. Without the bank statements being introduced in the hearing, there is insufficient proof that the amounts remaining on Exhibit 2 are not gross receipts as defined by Section 7-9-3.5(A)(1).

Tabulation of Maximum Audit Adjustment

Mr. Chavez argued that the method that the Department should have used was one in which the Department took the gross receipts reported on Taxpayer's federal returns and then determined the underreported amount based on what was reported. Mr. Chavez submitted a worksheet that utilized this method. Exhibit 3. The regulations allow the Department to use federal returns and other governmental reports as an alternative method. Regulation 3.1.5.8(C)(3) NMAC (2000). However, as Taxpayer's own Exhibit 3 indicates there was no return available for tax year 2003 making it impossible to use this particular method. Exhibit 3.

Mr. Chavez argued that the bank deposit method overstated the gross receipts for tax years

2001 and 2002. If the method of looking at the sales reported on the federal returns, less receipts from Arizona, less receipts reported in New Mexico to arrive at a total amount of gross receipts was used, his receipts would not be overstated and perhaps he could pay the liability. The audit method used in this matter was verified and reliable and while the original auditor made some errors, these errors could have been attributed to Mr. Chavez failing to provide the proper documentation to the Department in a timely manner.

Mr. Chavez was fairly upset that Ms. Sena did not provide him with the work papers in Exhibit M, pages marked P8.1 through P8.182. Ms. Sena testified that the reason she did not provide Mr. Chavez with the work papers is that the work papers were based on copies of documents provided to the Department by Mr. Chavez. Ms. Sena testified that she provided Mr. Chavez with the opportunity to review the documents in Santa Fe but he did not avail himself of the opportunity.

The methodology used by the Department is valid and Taxpayer has not provided sufficient information or documents to prove that the methodology used by the Department was in error.

Civil Penalty.

Mr. Chavez argued that because of a series of catastrophes, he was nonnegligent in reporting and paying the correct amount of gross receipts tax. Mr. Chavez argued that the unexpected death of his accountant in December 1999, the embezzlement, and the replacement of the first accountant with one in which good accounting controls were not put into place, all contributed to his business' demise. There is no dispute by the Department that these events

occurred, and the Hearing Officer has no doubt that each event hindered or crippled Taxpayer's business. The Department's regulation defines negligence for purposes of assessing penalty as:

- 1) failure to exercise that degree of ordinary business care and prudence which reasonable taxpayers would exercise under like circumstances;
- 2) inaction by taxpayers where action is required;
- 3) inadvertence, indifference, thoughtlessness, carelessness, erroneous belief or inattention.

Regulation 3.1.11.10 NMAC (1996).

The Department argued that despite the events described by Mr. Chavez, Taxpayer was required to maintain its books and records. In reviewing the indicia of nonnegligence as set out in regulation 3.1.11.11 NMAC (2001), the regulation does not provide an exception for the sort of catastrophes described by Mr. Chavez. Only if a taxpayer's business records are destroyed or damaged or if the taxpayer is somehow injured, does the regulation contemplate the abatement or no assessment of penalty.

In this case, Taxpayer acted negligently by not reporting all of the gross receipts received from selling property in New Mexico.

Interest.

Interest "shall be paid" on taxes that are not paid on or before the date on which the tax is due. NMSA 1978, § 7-1-67 (A). The word "shall" indicates that the assessment of interest is mandatory, not discretionary. *See State v. Lujan*, 90 N.M. 103, 105, 560 P.2d 167, 169 (1977).

The assessment of interest is not designed to punish taxpayers, but to compensate the state for the

time value of unpaid revenues. Because the principal amount of gross receipts tax was not paid when it was due, interest was properly assessed.

CONCLUSIONS OF LAW

A. Sunrooms Plus, Inc. filed a timely written protest to the principal, penalty and interest assessed under Letter ID L2080690688, and jurisdiction lies over the parties and the subject matter of this protest.

B. The parties stipulated on May 11, 2010, that the tax due was based on the adjusted assessed amount of gross receipts of \$220,837.75 in principal tax, not including penalty and interest.

C. Taxpayer conceded that it owed the entire amount of the withholding principal tax of \$2,850.89, plus penalty and interest.

D. Taxpayer proved by a preponderance of the evidence that the amounts of \$413.50 and \$1,079.64 should be adjusted or abated from gross receipts because they were not gross receipts as defined by Section 7-9-3.5(A)(1).

E. Taxpayer was unable to either rebut the presumption or prove by a preponderance of the evidence that the gross receipts listed in Exhibits 1 and 2 were not taxable, except for the amounts of \$413.50 and \$1,079.64.

F. Taxpayer was negligent in underreporting its gross receipts. The proper amount of penalty should be calculated at no more than 10% of the principal amount of tax owed pursuant to NMSA 1978, Section 7-1-69 (2003).

G. Interest should be applied to the principal amount of tax due in accordance with

this Decision.

For the foregoing reasons, Sunrooms Plus, Inc.'s protest is GRANTED IN THE AMOUNT OF \$1,493.14 IN GROSS RECEIPTS AND DENIED AS TO ALL OTHER AMOUNTS IN PROTEST.

DATED: September 9, 2011.