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

**IN THE MATTER OF THE PROTEST OF**
**MAGNUM BUILDERS OF NEW MEXICO, INC.** **No. 15-16**
**TO ASSESSMENT ISSUED UNDER LETTER**
**ID NO. L0522171776**

## DECISION AND ORDER

A protest hearing occurred on the above captioned matter on August 5, 2014 and October 16, 2014 before Brian VanDenzen, Esq., Hearing Officer, in Santa Fe. Attorneys James Burn and Brian Close appeared, representing Magnum Builders of New Mexico, Inc. ("Taxpayer"). Stephen Jarrett Slatton and Patricia Padilla (only during the August 5, 2014 hearing) appeared as testifying witnesses for Taxpayer. Staff Attorney Elena Morgan appeared representing the State of New Mexico, Taxation and Revenue Department ("Department"). Protest Auditor Thomas Dillon and Auditor Joseph Coleman appeared as testifying witnesses for the Department. Taxpayer Exhibits #1-15 and Department Exhibits B and E were admitted into the record, as described in the Administrative Exhibit Log. Additionally, the February 13, 2015 joint statement of abatement submitted after conclusion of the hearing is admitted into the record. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

## FINDINGS OF FACT

1. On November 7, 2008, the Department assessed Taxpayer $120,769.29 in gross receipt tax, $25,765.37 in gross receipts tax penalty, $55,999.26 in gross receipts tax interest, $4,862.25 in compensating tax, $972.45 in compensating tax penalty, and $2,296.93 in

compensating tax penalty for a total assessment of $210,665.55 for the CRS reporting periods between January 31, 2002 and June 30, 2007. [Letter id. no. L0522171776].

2. On December 4, 2008, Taxpayer protested the Department's assessment.

3. On December 11, 2008, the Department acknowledged receipt of Taxpayer's protest.

4. The Hearings Bureau first learned of this matter when the Department requested a hearing on July 30, 2013.

5. On July 31, 2013, the Hearings Bureau issued Notice of Administrative Hearing, scheduling this matter for a hearing on October 28, 2013.

6. On October 18, 2013, Taxpayer moved to continue the October 28th scheduled hearing, a request opposed by the Department.

7. On October 22, 2013, the Hearings Bureau issued an Order of Continuance and Amended Notice of Hearing resetting this matter for a hearing on May 12, 2014.

8. On May 8, 2014, Taxpayer again sought a continuance in this matter.

9. On May 9, 2014, the Hearings Bureau issued an Order of Continuance, Hearing Officer Reassignment, and Amended Notice of Hearing resetting this matter for a hearing on August 5, 2014.

10. On August 5, 2014, a hearing in the above captioned matter occurred in Santa Fe. After taking testimony from Taxpayer witnesses and recessing for a late lunch break, the parties indicated that they had reached a proposed resolution of the issues at protest and requested a continuance to finalize that settlement. The Chief Hearing Officer offered to complete the hearing record given that a majority of the hearing had already occurred, but the parties insisted that the matter was resolved. The parties agreed on the record to a short hearing on September

12, 2014 where the parties could present closing arguments in the event that settlement did not occur.

11. On August 6, 2014, the Hearings Bureau issued an Order of Continuance and Amended Notice of Hearing resetting this matter for a short hearing on September 12, 2014.

12. When the settlement in this matter did not materialize, the Hearings Bureau offered the parties an additional day of hearing on September 11, 2014. Taxpayer declined and instead moved for a continuance of the September 12, 2014 hearing, partially because Mr. Slatton had arranged an out-of-state trip on that date despite the agreed upon hearing date.

13. On September 11, 2014, the Hearings Bureau issued the Final Order of Continuance and Amended Notice of Hearing resetting this matter for a hearing on October 16, 2014. That order also ruled that the failed settlement negotiations in this matter were not germane to the issues at protest.

14. Because of a series of pre-hearing and post-hearing abatements, the only issue remaining at protest in this matter is abatement of penalty[1].

15. Before January 1, 2003, Stephen Slatton was the sole proprietor of Magnum Builders, a construction business.

16. Magnum Builders employed a bookkeeper out of Gallup, PBS Services, to prepare its taxes.

17. On October 15, 2003, the business Mr. Slatton previously ran as a sole proprietorship was incorporated as Magnum Builders of New Mexico, Inc. ("Taxpayer").

18. There was a transition period of approximately six months where the sole proprietorship Magnum Builders continued to operate in order to finish off pending contracts,

[1] Consequently, the findings of fact are limited to facts relevant to that issue.

obtain insurance, etc. Therefore, Magnum Builders filed CRS returns under a separate ID number in overlapping periods to Taxpayer's CRS returns under its new CRS number.

19. Beginning in early 2004, Taxpayer hired Padilla and Company to prepare its CRS returns.

20. During the relevant period, when Taxpayer entered into contracts with new clients, Mr. Slatton acknowledged it was not a priority of Taxpayer to obtain non-taxable transaction certificates ("NTTC or NTTCs") from the clients. [10-16-14 CD 50:00-54; 01:14:55-01:15:51].

21. During the relevant period, upon receipt of a customer checks/invoices, Patricia Padilla of Padilla and Company would often advise Taxpayer of the necessity of obtaining a NTTC from the customer. [10-16-14 CD 01:16:00-01:17:24].

22. In 2007, Taxpayer was selected for Departmental Audit. The audit period encompassed the CRS reporting periods between January 1, 2002 and June 30, 2007. [Taxpayer Ex. #7-011].

23. Taxpayer completed a Taxpayer Information Authorization naming Padilla & Company, Patrick Padilla or Patricia Padilla as his representative for all state taxes at issue in the audit. [Department Ex. E].

24. On October 18, 2007, Department Auditor Joseph Coleman met with Patrick Padilla and Patricia Padilla, Taxpayer's designated representatives. Mr. Coleman hand-delivered a letter ("60-day letter") providing Taxpayer notice that any required NTTCs be in Taxpayer's possession within 60-days, by December 17, 2007, or the claimed deduction requiring a NTTC would be disallowed. [Department Ex. B; Taxpayer Ex. #7-013].

25. Patricia Padilla remembers that during the October 18, 2007 meeting, the auditor delivered an audit letter and requested that Patrick Padilla sign it. [08-05-14 CD 50:00-54].

26. On October 18, 2007, Mr. Padilla did not sign acknowledgement of the 60-day letter but told Mr. Coleman he would review it, sign it, and return it that day.

27. Padilla and Company attempted to assist Taxpayer in securing the missing NTTCs and advised Mr. Slatton of the necessity of obtaining the missing NTTCs. [Taxpayer Ex. #1; 10-16-14 CD 01:00:00-22].

28. On December 6, 2007, Mr. Coleman again met with Patrick Padilla and discussed NTTCs. [Taxpayer Ex. #7-013].

29. On December 6, 2007, Mr. Coleman also spoke with Patricia Padilla about receiving a copy of the signed 60-day letter back.

30. Padilla and Company never provided the Department with a signed copy of the 60-day letter.

31. Taxpayer did not present NTTCs supporting the disallowed claimed deductions that were executed by the December 17, 2007 deadline.

32. Padilla and Company obtained an extension to provide records for the audit to the Department from March 25, 2008 through May 26, 2008. [Taxpayer Ex. #7-010].

33. Padilla and Company obtained a second extension to provide records from May 26, 2008 until July 25, 2008. [Taxpayer Ex. #7-010].

34. Padilla and Company believed that these two extensions to provide records included an extension for submission of NTTCs and so informed Mr. Slatton. [08-05-14 CD 51:50-52:21; 1:13:50-1:14:59; 10-17-14 CD 1:11:34-59].

35. Because of Padilla and Company's belief that the extension applied to the NTTCs, Taxpayer continued to attempt to obtain the NTTCs through July 25, 2008.

36. Taxpayer ultimately presented eight untimely NTTCs. [Taxpayer Ex. #7-014].

37. The Department disallowed any claimed deduction where Taxpayer did not present a supporting NTTC executed by the December 17, 2007 deadline. [Taxpayer Ex. #7-014].

38. Based on the audit, the Department issued its assessment referenced in Finding of Fact #1.

39. After the August 5, 2014 hearing, the Department abated all assessed tax, penalty, and interest attributable to receipts of the sole proprietorship Magnum Builders, originally included in the audit exceptions, because that was not the entity audited or assessed.

40. On August 6, 2014, Taxpayer made a payment of $108,896.46 towards the remaining outstanding tax liability. [Taxpayer Ex. #13].

41. After the October 16, 2014 hearing, on October 21, 2014, the Department moved to hold open the record for presentation of additional Taxpayer evidence regarding the assessed tax principal, as issue that had been ruled upon during the hearing. Taxpayer did not respond to this motion.

42. By November 24, 2014, more than a month after the filing of the motion to hold the record open for additional evidence, neither party had submitted any additional evidence.

43. On November 24, 2014, the Hearings Bureau issued an order rejecting the submission of any further evidence into the record. However, that order did allow the Department to make any abatement of tax after review of additional information and submit a joint statement of such abatement by December 19, 2014.

44. On December 22, 2014, Taxpayer moved to extend the deadline for submission of a statement of abatement.

45. On January 16, 2015, the Hearings Bureau issued an extension of the deadline to submit a statement of abatement until January 30, 2015.

46. On January 28, 2015, the Department and Taxpayer moved for further extension to file a statement of abatement.

47. On February 3, 2015, the Hearings Bureau issued a final extension of the deadline to submit a statement of abatement until February 13, 2015.

48. On February 13, 2015, the Department and Taxpayer submitted a joint statement with attached documents showing the additional abatement of $48,864.96 in gross receipts tax, $1,100.00 in compensating tax, $10,158.24 in penalty, and $12,367.55 in interest for a total abatement of $71,390.75[2].

## DISCUSSION

After the various pre-hearing and post-hearing abatements, the main issue in this matter is whether penalty should be abated because Taxpayer relied on Padilla and Company's belief that the NTTC 60-day deadline of December 17, 2007 was extended twice until July 25, 2008.

**Presumption of Correctness.**

Under NMSA 1978, Section 7-1-17(C) (2007), the assessment of tax issued in this case is presumed correct. Unless otherwise specified, for the purposes of the Tax Administration Act, "tax" is defined to include interest and civil penalty. *See* NMSA 1978, §7-1-3 (X) (2013). Under Regulation 3.1.6.13 NMAC, the presumption of correctness under Section 7-1-17 (C)

[2] Because of all the handwritten annotations on the document, it is difficult to identify what remains as an alleged outstanding balance.

extends to the Department's assessment of penalty and interest. *See Chevron U.S.A., Inc. v. State ex rel. Dep't of Taxation & Revenue*, 2006-NMCA-50, ¶16, 139 N.M. 498, 503 (agency regulations interpreting a statute are presumed proper and are to be given substantial weight). Taxpayer has the burden to overcome the assessment. *See Archuleta v. O'Cheskey*, 1972-NMCA-165, ¶11, 84 N.M. 428, 431. However, once a taxpayer rebuts the presumption of correctness, the burden shifts to the Department to show the correctness of the assessed tax. *See MPC Ltd. v. N.M. Taxation & Revenue Dep't*, 2003 NMCA 21, ¶13, 133 N.M. 217.

**Gross Receipts Tax, the Deduction, and the Requirement for a Timely NTTC**

While the merits of the remaining assessed tax principal are not in dispute, it is still necessary to discuss the legal requirements of a deduction from gross receipts tax and the requirement for a NTTC because it provides necessary context to the penalty analysis.

For the privilege of engaging in business, New Mexico imposes a gross receipts tax on the receipts of any person engaged in business. *See* NMSA 1978, § 7-9-4 (2002). "Engaging in business" is defined as "carrying on or causing to be carried on any activity with the purpose of direct or indirect benefit." NMSA 1978, § 7-9-3.3 (2003). Under the Gross Receipts and Compensating Tax Act, there is a statutory presumption that all receipts of a person engaged in business are taxable. *See* NMSA 1978, § 7-9-5 (2002).

The New Mexico Gross Receipts and Compensating Tax Act provides numerous deductions of gross receipts tax. The deduction pertinent to this protest is the sale of construction services and construction-related services to persons engaged in the construction business under NMSA 1978, Section 7-9-52 (2000). The deduction is premised on the buyer delivering seller a NTTC.

NMSA 1978, Section 7-9-43 (2011) articulates the requirements for obtaining NTTCs:

> All nontaxable transaction certificates...should be in the possession of the seller or lessor for nontaxable transactions at the time the return is due for receipts from the transactions. If the seller or lessor is not in possession of the required nontaxable transaction certificates within sixty days from the date that the notice requiring possession of these nontaxable transaction certificates is given the seller or lessor by the department, deductions claimed by the seller or lessor that require delivery of these nontaxable transaction certificates shall be disallowed.

Under Section 7-9-43, Taxpayer had a statutory obligation to possess a NTTC at the time when the gross receipts tax was initially due. As Mr. Slatton acknowledged, obtaining NTTCs was not a priority for Taxpayer during this time of its business. Despite receiving reminders from Patricia Padilla about the necessity of obtaining a NTTC when she reviewed customer checks, Taxpayer did not possess the pertinent NTTCs at the time the corresponding tax was due.

While taxpayers "should" have possession of required NTTCs at the time the return is due from the receipts at issue, Section 7-9-43 gives taxpayers audited by the Department a second chance to obtain these NTTCs: within 60-days of when the Department gives notice, taxpayers must possess a NTTC in order to claim a deduction. Taxpayers who rely on this second chance provision run the risk of having their deductions disallowed if they are unable to meet the 60-day deadline set by the Legislature. The reason why a taxpayer cannot obtain a NTTC is irrelevant. The language of Section 7-9-43 is mandatory: if a seller is not in possession of required NTTCs within 60 days from the date of the Department's notice, "deductions claimed by the seller ... that require delivery of these nontaxable transaction certificates *shall be disallowed."* (emphasis added). *See Marbob Energy Corp. v. N.M. Oil Conservation Comm'n*, 2009-NMSC-013, ¶22, 146 N.M. 24 (use of the word "shall" in a statute indicates provision is mandatory absent clear indication to the contrary).

Consistent with the statutory language, under Regulation 3.2.201.12 (C) NMAC, a taxpayer "is not entitled to the deduction" when the NTTC is untimely. *See Chevron U.S.A., Inc.* ¶16 (agency

regulations interpreting a statute are presumed proper and are to be given substantial weight). The New Mexico Court of Appeals has held that despite its general reluctance to place "form over substance," the failure to timely and properly present a requisite NTTC is a "valid basis" for the Department to deny a claimed deduction. *Proficient Food Co. v. New Mexico Taxation & Revenue Dep't*, 1988-NMCA-042, ¶22, 107 N.M. 392. The Department personally delivered the 60-day notice to Taxpayer's designated accountants on October 18, 2007, making December 17, 2007 the NTTC deadline under statute. While the Department may still accept other records related to the audit after this 60-day deadline, there is no legal authority that allows the Department to extend the Legislature's firm second chance, 60-day NTTC deadline. Consistent with Section 7-9-43, Regulation 3.2.201.12 (C) NMAC, and *Proficient Food Co.*, the Department properly disallowed claimed deductions premised on NTTCs executed after that deadline.

**Civil Penalty**.

Under NMSA 1978, Section 7-1-69 (A) (2007), when a taxpayer fails to pay taxes due to the State because of negligence or disregard of rules and regulations, but without intent to evade or defeat a tax, by its use of the word "shall", civil penalty must be added to the assessment. As discussed above, the statute's use of the word "shall" makes the imposition of penalty mandatory in all instances where a taxpayer's actions or inactions meets the legal definition of "negligence." *See Marbob Energy Corp.* ¶22.

Regulation 3.1.11.10 NMAC defines negligence in three separate ways: (A) "failure to exercise that degree of ordinary business care and prudence which reasonable taxpayers would exercise under like circumstances;" (B) "inaction by taxpayer where action is required"; or (C) "inadvertence, indifference, thoughtlessness, carelessness, erroneous belief or inattention." Erroneous belief and inadvertent error meets the legal definition of "negligence" under the penalty

statute. *See El Centro Villa Nursing Center v. Taxation and Revenue Department*, 1989-NMCA-070, ¶10, 108 N.M. 795. In this case, Taxpayer's inaction in not obtaining the relevant NTTC either at the time of filing the tax returns for the transactions or before expiration of the 60-day second chance NTTC deadline constituted negligence under Regulation 3.1.11.10 NMAC, potentially subjecting Taxpayer to penalty under Section 7-1-69 (A).

In instances where a taxpayer might otherwise fall under the definition of civil negligence generally subject to penalty, Section 7-1-69 (B) provides a limited exception: "[n]o penalty shall be assessed against a taxpayer if the failure to pay an amount of tax when due results from a mistake of law made in good faith and on reasonable grounds." Failing to meet the deadline alone does not equate to making a mistake of law in good faith and on reasonable grounds. Despite counsel's argument that Taxpayer acted in good faith, there is no evidence to support that Taxpayer made any legal determination on reasonable grounds, either through its own research or through advice of counsel, that the NTTCs were not required by the 60-day deadline.

Further, in instances where a taxpayer might otherwise fall under the definition of civil negligence generally subject to penalty, Regulation 3.1.11.11 NMAC established eight instances of "nonnegligence" where penalty may be abated. In pertinent part to Taxpayer's argument to abate penalty in this matter is Regulation 3.1.11.11 (D) NMAC. Regulation 3.1.11.11 (D) NMAC states that penalty may be abated when

> the 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 the taxpayer's reliance on an agent.

Taxpayer's argument for abatement of penalty is that Mr. Slatton relied on the statements of its accountants at Padilla & Company that the 60-day deadline for obtaining NTTC's had been

extended, and therefore Taxpayer should not be penalized for the failure to timely produce the NTTCs. The Hearings Bureau has previously abated penalty when a taxpayer relied on a CPA's advice that no NTTC was needed for the deduction and therefore Taxpayer ran out of time to obtain one before the 60-day deadline expired. *See In the Matter of the Protest of Eileen P. Cahoon*, Decision and Order No. 98-38 (hearing officer abated penalty when, upon receipt of 60-day letter, taxpayer met with a CPA, relied on the CPA's incorrect advice that no NTTC was needed to support the claimed deduction, and ran out of time under the 60-day deadline to obtain the NTTC when taxpayer learned it was in fact necessary).

But there are some key facts in this protest that defeat Taxpayer's argument for abatement of penalty. Unlike *Cahoon*, Taxpayer engaged the services of Padilla and Company at or near the time of the transactions at issue in the protest rather than after receiving notice of audit. Unlike *Cahoon*, at no point—either before or after the notice of audit/6-day letter—did Taxpayer's accountants advise Taxpayer that NTTCs were unnecessary to support its claimed deductions. In fact, Patricia Padilla credibly testified that she would remind Taxpayer of the necessity of obtaining the NTTCs at the time she would receive the customer invoices/checks, which is consistent with the requirement under Section 7-9-43 that Taxpayer be in possession of the NTTCs at the time of the initial filing of the tax related to the receipts. Mr. Slatton acknowledged that gathering the NTTCs at the time of the transactions simply was not a priority for the company during that period. Because Taxpayer did not heed the valid advice of its accountants at the time of the transactions, Taxpayer forced upon itself the difficult task of needing to gather all NTTCs within 60-days of audit.

Once the audit period and 60-day NTTC second chance period commenced beginning on October 18, 2007, Taxpayer's accountants continued to assist Taxpayer with gathering the relevant

NTTCs. However, those NTTCs were not provided by the December 17, 2007 60-day deadline. The extension of time from March 26, 2008 until May 26, 2008 that Taxpayer's accountants, and hence Taxpayer, believed included the NTTCs deadline encompassed a time period after the statutory 60-day deadline had already expired. While Taxpayer's accountants provided Taxpayer incorrect advice that the extensions applied to NTTCs, there could be no detrimental reliance on this erroneous advice because the date of legal consequence had already occurred before the time of the extension from March 26, 2008 to May 26, 2008 and subsequently to July 25, 2008.

There are no grounds to abate penalty in this matter. Even if Taxpayer relied heavily on its accountants during the audit period, and those accountants misunderstood the purpose of the extension to provide documents as part of the audit, Taxpayer cannot "abdicate" its tax responsibilities "merely by appointing an accountant as its agent in tax matters." *See El Centro Villa Nursing Center*, ¶14. Ultimately, Taxpayer had the responsibility to support the claimed deduction by providing a timely executed NTTC. *See Tiffany Construction Co. v. Bureau of Revenue*, 1976-NMCA-127, ¶5, 90 N.M. 16 (under New Mexico's self-reporting tax system, "every person is charged with the reasonable duty to ascertain the possible tax consequences" of his or her actions). Taxpayer's protest for the abatement of penalty is denied.

## CONCLUSIONS OF LAW

A. Taxpayer filed a timely, written protest to the assessment. Jurisdiction lies over the parties and the subject matter of this protest.

B. Because of various prehearing and post hearing abatements, the only issue remaining at protest is whether Taxpayer was entitled to abatement of civil negligence penalty imposed under NMSA 1978, Section 7-1-69 (2007).

C. Under NMSA 1978, Section 7-1-69 (2007), Taxpayer is liable for civil negligence penalty because Taxpayer's inaction in failing to obtain NTTCs at the time of the transaction or within 60-day notice of the Department's audit meets the definition of civil negligence under Regulation 3.1.11.10 NMAC.

D. Under Section 7-1-69 (B), Taxpayer did not establish that its failure to obtain the NTTCs either at the time the tax was initially due or within 60-days of Department notice resulted from a mistake of law made in good faith and on reasonable grounds.

E. Taxpayer could not timely rely on its accountant's statements that the deadline for submission of the NTTCs had been extended because that extension encompassed a time period after the 60-day deadline had already occurred.

For the foregoing reasons, Taxpayer's protest **IS DENIED. The Department is ordered** to provide Taxpayer a clear spreadsheet articulating Taxpayer's outstanding liability in light of the prehearing abatement, Taxpayer's payment of tax after the first hearing, and the post-hearing abatement **within 7-days**. Taxpayer is liable for that remaining, outstanding amount.

DATED: May 6, 2015.

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