

**STATE OF NEW MEXICO
ADMINISTRATIVE HEARINGS OFFICE
TAX ADMINISTRATION ACT**

**IN THE MATTER OF THE PROTEST OF
HECTOR MARTINEZ
TO ASSESSMENT ISSUED UNDER LETTER
ID NO. L1466178512**

No. 16-46

DECISION AND ORDER

A protest hearing occurred on the above captioned matter on June 21, 2016 before Brian VanDenzen, Esq., Chief Hearing Officer, in Santa Fe. At the hearing, Hector Martinez (“Taxpayer”) appeared pro se, along with interpreter Darlene Parra. Staff Attorney Elena Morgan appeared representing the State of New Mexico Taxation and Revenue Department (“Department”). Protest Auditor Milagros Bernardo appeared as a witness for the Department. Taxpayer Exhibit #1-9 and Department Exhibits A-E were admitted into the record. All exhibits are more thoroughly described in the Administrative Exhibit Coversheet. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. On April 1, 2016, through letter id. no. L1881463344, the Department assessed Taxpayer for \$28,268.57 in gross receipts tax, \$5,653.70 in penalty, and \$3,757.52 in interest for a total assessment of \$37,679.79 for the CRS reporting periods from January 1, 2009 through December 31, 2013.
2. On April 12, 2016, Taxpayer protested the Department’s assessment. The Department received the protest on April 14, 2016.
3. On April 22, 2016, the Department’s protest office acknowledged receipt of a valid protest in this matter.

4. On May 25, 2016, the Department filed a request for hearing in this matter with the Administrative Hearings Office, an agency independent of the Department under the Administrative Hearings Office Act.

5. On May 27, 2016, the Administrative Hearings Office sent Notice of Administrative Hearing, scheduling this matter for the merits hearing on June 21, 2016.

6. Taxpayer is a sole-proprietor that provides tile-installation services in New Mexico.

7. During the relevant period, Taxpayer worked with a bookkeeper on preparing his taxes.

8. The bookkeeper informed Taxpayer that he needed to obtain NTTCs for his work.

9. During the relevant period, Taxpayer provided tile-installation services for Five-Star Floor Covering.

10. Five-Star Floor Covering (“Five Star”) issued a Type 2 NTTC on August 5, 2011. However, Five-Star Floor Covering did not properly complete that Type 2 NTTC by failing to fill out any seller information on the seller’s copy and did not complete the execution date. [Dept. Ex. B-2].

11. Five Star provided seller-Taxpayer with the buyer’s copy of the incomplete Type 2 NTTC rather than the seller’s copy that should have been provided. [Dept. Ex. B-1].

12. Some two-years after the initial listed execution date on the seller’s copy, someone handwrote in the seller information, listing Taxpayer, on the buyer’s copy of the NTTC, and noted an execution date of April 23, 2013. [Dept. Ex. B-1].

13. The Department's internal electronic database of issued NTTCs still shows that the Type 2 NTTC Five Star attempted to execute to Taxpayer as incomplete without seller identification information or an execution date. [Dept. Ex. B-3].

14. Through its Schedule C mismatch program with the IRS, the Department detected a variance between the amount of gross receipts tax reported and paid to the Department and the amount of business income reported to the IRS on Taxpayer's Schedule C. [Dept. Ex. D-1].

15. Based on this mismatch, the Department selected Taxpayer for a limited scope audit. [Dept. Ex. D-1].

16. On January 1, 2016, the Department mailed Taxpayer a limited scope audit commencement notice, informing Taxpayer that he had 60-days, until March 1, 2016, to present any required NTTCs. [Dept. Ex. D-1 & Dept. Ex. D-5, showing printing/ mailing info].

17. Taxpayer submitted all his documentation to the Department in January of 2016. The Department informed Taxpayer and Taxpayer's bookkeeper that the Type 2 NTTC was inadequate to support the claimed deduction.

18. Taxpayer did not timely present any properly completed and executed NTTC by the March 1, 2016 60-day deadline.

19. On March 1, 2016, the Department sent Taxpayer a letter stating that there remained a discrepancy and that the Department was preparing to issue an assessment to Taxpayer.

20. On March 18, 2016, 17-days after the 60-day deadline, Taxpayer presented an untimely but properly executed and completed Type 5 NTTC from Five Star.

21. As of the date of hearing, Taxpayer owed \$28,268.57 in gross receipts tax, \$5,653.70 in penalty, and \$3,967.57 in interest for a total outstanding liability of \$37,889.84. [Dept. Ex. E].

DISCUSSION

The main issues in this case involve whether Taxpayer had a requisite, timely, and properly completed NTTC to support the claimed deduction and whether Taxpayer could otherwise accept an inappropriate series of NTTC in good faith to support the NTTC. A second issue is whether Taxpayer's reliance on a bookkeeper may be a basis for abatement of penalty.

Presumption of Correctness.

Under NMSA 1978, Section 7-1-17 (C) (2007), the assessment issued in this case is presumed correct. Consequently, Taxpayer has the burden to overcome the assessment. *See Archuleta v. O'Cheskey*, 1972-NMCA-165, ¶11, 84 N.M. 428. 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) 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).

Moreover, "[w]here 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*, 1991-NMCA-024, ¶16, 111 N.M. 735 (internal citation omitted); *See also TPL, Inc. v. N.M. Taxation & Revenue Dep't*, 2003-

NMSC-7, ¶9, 133 N.M. 447. Because Taxpayer is claiming a deduction from gross receipts tax, Taxpayer must establish its right to claim the deduction.

Gross Receipts Tax, Deduction, and the Requirement of a Timely NTTC

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). Under NMSA 1978, Section 7-9-3.5 (A) (1) (2007), the term “gross receipts” is broadly defined to mean

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.

“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). Gross receipts tax applies to the performance of a service in New Mexico. *See* NMSA 1978, § 7-9-3.5 (2007). 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). Unless otherwise deductible, Taxpayer’s receipts from performing tile installation services were subject to gross receipts tax.

The New Mexico Gross Receipts and Compensating Tax Act provides numerous deductions of gross receipts tax. The deduction potentially at issue in this case the sale of a service for resale deduction under NMSA 1978, Section 7-9-48 (2000), which states that:

Receipts from selling a service for resale may be deducted from gross receipts or governmental gross receipts if the sale is made to a person who delivers a nontaxable transaction certificate to the seller. The buyer delivering the nontaxable transaction certificate must resell the service in the ordinary course of business and the resale must be subject to the gross receipts tax....

The deduction is premised on the sale of a service for resale when the resale occurs in the regular course of business and the resale is subject to New Mexico gross receipts tax. Taxpayer did not establish that Five Star was reselling the tile installation services in its regular course of business, although even if it did, this case still turns on the NTTC issue. This deduction is generally covered by a Type 5 NTTC. Simply selling the service for resale, as the Taxpayer did in this instance, is not enough to satisfy the requirements of the deduction under Section 7-9-48. The statute clearly and unambiguously conditions the deduction on a sale made to a person/entity who delivers a NTTC.

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

All nontaxable transaction certificates of the appropriate series executed by buyers or lessees 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 except as provided in Subsection E of this section....

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), a taxpayer "is not entitled to the deduction" when the NTTC is untimely. 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.

In this case, Taxpayer did possess a Type 2 NTTC, an inappropriate series for the deduction at issue, by the 60-day deadline. Since the Type 2 NTTC was of the inappropriate series for the deduction at issue, that NTTC does not satisfy the statutory language Section 7-9-43 (A), which requires a NTTC of the appropriate series. Taxpayer did not timely possess the appropriate series Type 5 NTTC by the March 1, 2016, 60-day deadline. In fact, the Type 5 NTTC was executed some 18-days after the 60-day deadline. Thus, the Department was required to disallow the sale of a service for resale deduction under Section 7-9-48. The Department lacked authority to accept Taxpayer's untimely presentation of the Type 5 NTTC, executed on March 18, 2016, after the 60-day second chance deadline had already passed.

Nevertheless, despite not possessing the correct type of NTTC to support the deduction, the question remains whether the inappropriate series Type 2 NTTC that Taxpayer did timely present before expiration of the 60-day deadline entitles Taxpayer to relief from the assessment under the good-faith, safe harbor protection articulated by Section 7-9-43 (A).

Section 7-9-43 (A) grants taxpayers a good-faith acceptance, safe harbor from taxation protection in some circumstances:

[w]hen the seller or lessor accepts a nontaxable transaction certificate within the required time and in good faith that the buyer or lessee will employ the property or service transferred in a nontaxable manner, the properly executed nontaxable transaction certificate shall be conclusive evidence, and the only material evidence, that the proceeds from the transaction are deductible from the seller's or lessor's gross receipts.

In other words, the statute grants the seller of the service safe harbor from taxation when the seller timely accepts a properly executed NTTC in good faith from the buyer. Regulation 3.2.201.15

NMAC (05/31/01) discusses good faith acceptance of a NTTC:

Acceptance of [NTTCs] in good faith that the property or service sold thereunder will be employed by the purchaser in a nontaxable manner is determined at the time of each transaction. The taxpayer claiming the protection of a certificate continues to be responsible that the goods delivered or services performed thereafter are of the type covered by the certificate.

The Administrative Hearings Office, and its predecessor the Hearings Bureau, have employed a broader view of the good-faith, safe harbor protection since the 2013 issuance of the decision and order *In the Matter of the Protest of Case Manager*, No. 13-12 (non-precedential) and *In the Matter of the Protest of Rio Grande Electric Co., Inc*, No. 13-16 (non-precedential). Essentially this interpretation is that so long as the transaction at issue otherwise would qualify for a statutory deduction, a timely and properly executed but inappropriate series NTTC accepted in good-faith by a taxpayer may still entitle a taxpayer to the deduction under the good-faith, safe harbor statutory provision. In an unpublished decision, the New Mexico Court of Appeals affirmed the ruling in the *Case Manager* decision and order narrowly under a right for any reason standard. *See New Mexico Taxation and Revenue Dep't. v. Case Manager*, No. 32,940 (N.M. Ct. App. April 29, 2015) (non-precedential). On July 25, 2016, the Court of Appeals looked favorably

upon the good-faith, safe harbor provision as previously applied by the Administrative Hearings Office/Hearings Bureau *In the Matter of the Protest of Case Manager*, No. 13-12 (non-precedential). See *Southwest Mobile Service and Richard Cameron v. New Mexico Taxation and Revenue Department*, No. 34,551 (N.M. Ct. App. July 25, 2016) (non-precedential) (although the Court of Appeals overturned the hearing officer on whether the good faith analysis applies on a MTC rather than a NTTC, it relied extensively on the *Case Manager* analysis in reaching its conclusion). A recent Decision and Order of the Administrative Hearings Office continued with that interpretation. See *Decision and Order in the Matter of the Protest of SPMC, Inc.*, No. 16-45 (non-precedential).

However, unlike those other cases, this case does not turn on whether Taxpayer substantively accepted the Type 2 NTTC in good faith, but rather on a much narrower basis discussed in the first case addressing the safe harbor protection, *Leaco Rural Tel. Coop. v. Bureau of Revenue*, 1974-NMCA-076, ¶15, 86 N.M. 629. In *Leaco*, the New Mexico Court of Appeals considered what requirements must be met “before an NTTC becomes conclusive evidence that proceeds of a transaction are deductible.” While the *Leaco* Court of Appeals was considering NMSA 1978, §7-9-43(A) (2011)’s predecessor statute, NMSA 1953, Section 72-16A-13(A), the good faith, safe harbor provision of both statutes is substantially the same. In *Leaco*, a buyer had executed a NTTC to a seller for a transaction held to be subject to tax. The *Leaco* court found that a seller-taxpayer must satisfy three statutory requirements before the good faith, safe harbor protection attaches to the transaction. See *id.* As the *Leaco* Court of Appeals expounded those three “requirements are timeliness of acceptance of the NTTC, good faith acceptance of the NTTC and a properly executed NTTC.” *id.* By “properly executed” the *Leaco* Court of Appeals—relying on the Black’s Law Dictionary—meant only that the NTTC forms were filled out and signed. See *id.*, ¶14.

If these three conditions are met, then the *Leaco* Court of Appeals found that the NTTC becomes the only material and conclusive evidence establishing that the seller-taxpayer is entitled to the claimed deduction even when the buyer improperly issued the NTTC to the seller. *See id.*, ¶15; *See also Rainbo Baking Co. v. Commissioner of Revenue*, 84 N.M. 303, 305 502 P.2d 406, 408 (N.M. Ct. App. 1972) (absent a claim of bad faith, some other issue of good faith, or a claim of improper execution of the NTTC, a taxpayer’s presentation of the NTTC established that taxpayer’s claim with conclusive evidence). The *Leaco* Court of Appeals found no relevance to the fact that the buyer had improperly issued a NTTC to the seller by stating that was an issue between the Department and the buyer. *See Leaco* at ¶20.

In this case, the Type 2 NTTC that Taxpayer presented was not “properly executed” under the *Leaco* requirement because it was incomplete. At the time of initial execution, August 5, 2011, Five Star did not list or provide the Seller information on either the seller’s copy or buyer’s copy of the NTTC form, making the form incomplete, not filled out, and not properly signed. On April 23, 2013, some two years later, someone handwrote the seller’s information on the buyer’s copy of the Type 2 NTTC. However, in this case Taxpayer was the seller, and needed the seller’s copy to establish that the NTTC form was properly executed. While admittedly this is a form over substance issue, proper completion of the NTTC form allows the Department to track both the buyer and a seller engaged in the transaction subject to a NTTC, which gives the Department the means necessary to pursue the buyer for improperly issuing the NTTC, the Department’s exact remedy described by the Court of Appeals in *Leaco*. The Department’s internal electronic database still shows that the Type 2 NTTC at issue was incomplete, without any seller information or an execution date. Since the form was not properly completed, Taxpayer did not establish it was entitled to the good-faith, safe harbor provision of Section 7-9-43 (A) under the three-requirements

articulated in *Leaco*, ¶14. See also *Proficient Food Co. v. New Mexico Taxation & Revenue Dep't*, 1988-NMCA-042, 107 N.M. 392 (taxpayer not entitled to a deduction when the nontaxable transaction form presented was not in the NTTC form proscribed by the Department).

Consequently, the Department properly denied Taxpayer's claim for the deduction.

Penalty and Interest.

When a taxpayer fails to make timely payment of taxes due to the state, "interest *shall* be paid to the state on that amount from the first day following the day on which the tax becomes due...until it is paid." NMSA 1978, § 7-1-67 (2007) (italics for emphasis). Under the statute, regardless of the reason for non-payment of the tax, the Department has no discretion in the imposition of interest, as the statutory use of the word "shall" makes the imposition of interest mandatory. See *Marbob Energy Corp.*, ¶22. The language of Section 7-1-67 also makes it clear that interest begins to run from the original due date of the tax until the tax principal is paid in full. The Department has no discretion under Section 7-1-67 and must assess interest against Taxpayer until Taxpayer satisfies the gross receipts tax principal.

However, there are grounds to abate civil negligence penalty under NMSA 1978, Section 7-1-69 (2007) in this case. 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", Section 7-1-69 requires that civil penalty 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." Nevertheless, because Taxpayer's bookkeeper failed to advise Taxpayer of the necessity of getting a properly completed NTTC (an obvious error) or a NTTC of the correct type for the

transaction at issue, penalty is abated under Section 7-1-69 (B) and Regulation 3.1.11.11 (D) NMAC.

CONCLUSIONS OF LAW

- A. Taxpayer filed a timely, written protest to the Department's assessment, and jurisdiction lies over the parties and the subject matter of this protest.
- B. The hearing was timely set and held within 90-days of protest under NMSA 1978, Section 7-1B-8 (2015).
- C. Taxpayer did not overcome the presumption of correctness that attached to the assessed tax principal and interest under NMSA 1978, Section 7-1-17 (C) (2007) and *Archuleta v. O'Cheskey*, 1972-NMCA-165, ¶11, 84 N.M. 428.
- D. Taxpayer was engaged in business in New Mexico selling tile installation services and therefore all of Taxpayer's receipts during the audit period are presumed subject to gross receipts tax under NMSA 1978, Section 7-9-5 (2002).
- E. Taxpayer did not present timely executed NTTCs to support the claimed deduction for the sale of a service for resale under NMSA 1978, Section 7-9-48 (2000). The Type 5 NTTC Taxpayer presented was executed after the 60-day deadline. Under NMSA 1978, Section 7-9-43 (2011) and Regulation 3.2.201.12 (C), without a timely executed NTTC at either the time of the filing of returns or within 60-days of notice of audit, the Department is not allowed to grant and Taxpayer is not entitled to the claimed deduction under Section 7-9-51. *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). *See also Proficient Food Co. v. New Mexico Taxation & Revenue Dep't*, 1988-NMCA-042, ¶22, 107 N.M. 392 (Court

found it valid for the Department to deny a claimed deduction when taxpayer did not timely present a requisite NTTC).

F. The Type 2 NTTC that Taxpayer presented with an execution date before the expiration of the 60-day deadline was not properly executed because it was incomplete, thereby failing one of the *Leaco Rural Tel. Coop. v. Bureau of Revenue*, 1974-NMCA-076, ¶14, 86 N.M. 629 requirements for the good-faith, safe harbor provision to apply.

G. Under NMSA 1978, Section 7-1-67 (2007), Taxpayer is liable for accrued interest under the assessment. Interest continues to accrue until the tax principal is satisfied.

H. Because Taxpayer's bookkeeper failed to inform Taxpayer that Taxpayer had both the wrong type of NTTC and that the NTTC was not properly completed and executed, penalty is abated in this matter pursuant to NMSA 1978, Section 7-1-69 (B) (2007) and Regulation 3.1.11.11 (D) NMAC.

For the foregoing reasons, the Taxpayers' protest **IS PARTIALLY GRANTED AND PARTIALLY DENIED**. Taxpayer is liable for the \$28,268.57 in gross receipts tax and \$3,967.57 in interest. Under Section 7-1-67, interest continues to accrue until tax principal is satisfied. The civil negligence penalty totaling \$5,653.70 is abated.

DATED: September 23, 2016.

Brian VanDenzen
Chief Hearing Officer
Administrative Hearings Office
P.O. Box 6400
Santa Fe, NM 87502

NOTICE OF RIGHT TO APPEAL

Pursuant to NMSA 1978, Section 7-1-25 (1989), the parties have the right to appeal this decision by *filing a notice of appeal with the New Mexico Court of Appeals* within 30 days of the date shown above. *See* Rule 12-601 NMRA. If an appeal is not filed within 30 days, this Decision and Order will become final. Either party filing an appeal shall file a courtesy copy of the appeal with the Administrative Hearings Office contemporaneous with the Court of Appeals filing so that the Administrative Hearings Office may be preparing the record proper.