

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

IN THE MATTER OF THE PROTEST OF
SANDIA OIL COMPANY
PROTEST TO ASSESSMENT NUMBERS
15669, 15670, 15672, 2484951, 2484974,
2484975, 2484976 AND 2486055

NO. 01-01

DECISION AND ORDER

This matter came on for formal hearing on November 27, 2000 before Gerald B. Richardson, Hearing Officer. Sandia Oil Company, hereinafter, "Taxpayer", was represented by Patricia Tucker, Esq. of Laflin, Lieuwen, Tucker, Pick, Heer & Neerken, P.A. The Taxation and Revenue Department, hereinafter, "Department", was represented by Javier López, Special Assistant Attorney General. At the close of the evidence, the parties requested the opportunity to brief the issues. The Taxpayer submitted its brief and requested findings of fact and conclusions of law on December 12, 2000. The Department submitted its brief and requested findings of fact and conclusions of law on January 12, 2001. The Taxpayer submitted its reply brief by mailing it on January 24, 2001 and it was received for filing on January 29, 2001 and the matter was considered submitted for decision at that time. Based upon the evidence and arguments,

IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. Sandia Oil Company, Inc., hereinafter, "Taxpayer", is a corporation which operates gasoline distributorships and convenience stores in five states, including New Mexico.
2. During 1999, the officers, directors and owners of Taxpayer were Jack Douglas Adams (Doug Adams) and Steven Beddingfield. Taxpayer was formed in 1982. At that time, the owner and president was Tony Bernitsky.

3. Lucy Strong was bookkeeper of Sandia Oil Company from its inception in 1982 through December of 1999. She had previously worked for Tony Bernitsky at another oil company.

4. Lucy Strong was never an owner, officer, or director of Sandia Oil Company. She was a paid employee. During 1999, she was a subordinate of Doug Adams.

5. During her employment at Sandia Oil Company in the 1990's, Lucy Strong was office manager and bookkeeper and among her responsibilities were the timely preparation and filing of both the various gasoline tax returns and gross receipts and withholding tax returns.

6. Lucy Strong prepared gasoline tax returns for five states, and also prepared the company's federal employment tax returns and New Mexico gross receipts tax returns. She signed the returns as bookkeeper.

7. The corporation's federal income tax returns were prepared by an outside accountant after the end of its fiscal year on September 30.

8. Until the periods in issue, the company had a long history of timely compliance with both return filing and taxpaying responsibilities.

9. In 1999, the only persons authorized to sign checks for the corporation were Doug Adams, Tony Bernitsky and Steve Beddingfield.

10. During 1999, Susan Sanchez was the accounts payable clerk for the corporation.

11. Although Ms. Sanchez was the accounts payable clerk, Lucy Strong also had the ability to draw checks, and often did so for tax payments.

12. As of July 1, 1999, there was a change in the manner in which New Mexico gasoline tax was to be reported for sales by the corporation to Nambe Pueblo.

13. The change was anticipated, and the corporation sent Lucy Strong to all available seminars held by the Department explaining the change in the law and the new method of reporting.

14. During July through November of 1999, Lucy Strong gave all outward appearances of remaining current on filing the appropriate gasoline and gross receipts tax returns. She had returns spread over her desk, both at work and at home. She spoke often of working on the tax returns. She routinely worked after hours and on weekends.

15. During this period, an assistant was hired for Lucy Strong to assist her with the tax return preparation. He was employed for about two months.

16. At one point during the last half of 1999, Doug Adams mentioned to Lucy Strong that he had not signed tax checks in the recent past, and was told by Lucy Strong that the tax checks were being signed by Steve Beddingfield.

17. At one point during this period, Doug Adams asked Lucy Strong if she needed any help in preparing the tax returns, and was told by Lucy Strong that she did not need any help.

18. From April of 1999 throughout the rest of the year, Lucy Strong appeared to her coworkers and personal friends to be depressed. She mentioned depression several times to Sonja Kortsch.

19. Sonja Kortsch first met Lucy Strong through Kortsch's husband, who was a housemate of Lucy Strong. She became personal friends with Lucy Strong, and that friendship continued throughout 1999.

20. Sonja Kortsch began work at Sandia Oil Company as a receptionist, and later became an auditor. Ms. Kortsch became an auditor in late 1998, and became a dispatcher in October of 1999.

21. During the time that Sonja Kortsch was receptionist, she would often assist Lucy Strong in copying returns for the files or doing other clerical matters regarding the returns.

22. It was the practice of the company after the end of the fiscal year on September 30 to compile financial information for that fiscal year for transmittal to the outside accountants who prepared the income tax returns of the corporation.

23. It generally took a few weeks after the end of a fiscal year for the material to be compiled for transmittal to the accountants.

24. Some time in early November, 1999, Doug Adams asked Lucy Strong for the materials compiled for the outside accountant, so that he could review them prior to transmitting those materials. Lucy Strong responded that she had not yet completed her work and needed some more time to compile the materials.

25. Sometime after Thanksgiving, Lucy Strong became ill and was absent from the office.

26. During Lucy Strong's absence, Doug Adams began to pick up the office mail. One day, in the mail was a certified mail letter from the tax department of another state informing the corporation that it had not filed a tax return which was due. Doug Adams then went to the corporation files to look for the missing tax return and found an empty file where the tax returns should be.

27. Doug Adams asked Sonja Kortsch to call Lucy Strong and ask her where the missing tax returns were.

28. Lucy Strong responded that there was a box of tax returns in her office.

29. A search was made by Sonja Kortsch, Suzie Sanchez and Doug Adams for the box of tax returns. It was not found in Lucy Strong's office, which was a fairly contained area, nor was it found in any other part of the corporation's offices or storerooms.

30. When Lucy Strong was told that the box could not be located, she continued to insist that the box was in her office.

31. That night, Lucy Strong went into the office after other office personnel had left, and stayed in the office until about 2:00 a.m. the next morning.

32. The following morning, the box with year-end materials was found in a cubicle office that had been searched without success the day before.

33. In reviewing the materials in the box, Doug Adams found a number of partially completed tax returns for various states and federal withholding tax returns. Among the returns found was a copy of the New Mexico gasoline tax return for September of 1999 signed by Lucy Strong.

34. He then had staff search for vouchers to see if checks had been drawn to pay the taxes for the months for which copies of returns were missing. He found that vouchers did exist for payments of the various taxes which were delinquent.

35. Mr. Adams then went to the checkbooks to see if checks for those taxes had cleared. He found that none of those checks had cleared, and that the funds were still in the corporate bank account. Among the returns not filed were the gasoline tax returns for September, copies of which were found in Lucy Strong's year-end box.

36. Mr. Adams then checked with the various taxing authorities to confirm which returns were missing.

37. Mr. Adams discussed the situation of the delinquent returns with a representative of the Taxation and Revenue Department. That representative advised him to file the returns for November of 1999 before the due date of December 25, in order to prevent the accrual of interest and penalties on those returns, and to file the other delinquent returns by December 31 in order to stop the accrual of an additional month's interest and penalties.

38. Lucy Strong did not return to work at Sandia Oil Company after the discovery of the tax delinquencies. Her illness, which began with strep throat, developed into pneumonia and she had a slipped disk which required her to remain in bed for three months. She would not take telephone calls from anyone at Sandia Oil other than Sonja Kortsch, and eventually refused to take her calls. She became a recluse, and has not returned to work at other employment.

39. During the remainder of December, Mr. Adams personally prepared delinquent returns for New Mexico, federal employment taxes, and returns due to other states. He worked on Christmas Eve of 1999 to complete and mail the returns for November of 1999 in order to avoid any late filing penalty or interest on those returns. The returns were mailed on December 24, 1999.

40. Throughout the next week, Mr. Adams prepared, signed and dated the gasoline tax returns for August, September and October. Those nine returns were all completed, signed and dated by December 31, 1999.

41. Mr. Adams prepared a Request for Voucher Check dated December 31, 1999, for a check in the amount of \$309,102.23, in payment of the amount shown to be due on the nine gasoline tax returns, copies of which were introduced as Exhibits 2, 3 and 4.

42. Check number 9033 was issued on December 31, 1999 in response to the Request for Voucher Check. That check was payable to the New Mexico Taxation and Revenue Department in the amount of \$309,102.23.

43. All nine returns were mailed, with the check for full payment of the taxes shown to be due thereon on December 31, 1999.

44. On January 25, 2000, the Department issued Assessment Nos. 2484951, 2484974, 2484975, and 2484976 to the Taxpayer, assessing penalty and interest for unpaid gross receipts taxes for the November, 1998; July, 1999; August, 1999 and September, 1999 reporting periods.

45. On January 27, 2000, the Department issued Assessment No. 2484955 to the Taxpayer, assessing penalty and interest for unpaid gross receipts taxes for the October, 1999 reporting period.

46. On February 17, 2000, the Department issued Assessment Nos. 15669, 15670, 15671 and 15672 to the Taxpayer, assessing penalty and interest for unpaid gasoline taxes for the July through October, 1999 reporting periods.

47. On February 23, 2000, the Taxpayer wrote to the Department requesting an extension of time to file a protest to the assessments referenced in Findings 45, 46 and 47, above.

48. On March 22, 2000, the Taxpayer filed a written protest to the assessments referenced in Findings 45, 46 and 47, above.

49. On April 25, 2000, the Department granted a retroactive extension of time to protest the assessments referenced in Findings 45, 46, and 47, above and acknowledged the Taxpayer's protest of said assessments.

50. The Department and the Taxpayer have resolved their dispute as to the amount of interest assessed and the formal hearing concerned only the assessment of penalty. After adjustments, the amounts of penalty remaining in issue are as follows:

GASOLINE TAXES

July, 1999	\$11,230.27
August, 1999	\$ 7,868.84
September, 1999	\$ 4,959.09
October, 1999	\$ 2,732.27

GROSS RECEIPTS TAX

November, 1998	\$152.87
July, 1999	\$898.75
August, 1999	\$877.79
September, 1999	\$719.65
October, 1999	\$561.68

DISCUSSION

The sole issue to be determined herein is whether the assessment of penalty for the late filing of tax returns and the late payment of taxes is appropriate in the circumstances of this case. There is a presumption of correctness which attaches to the assessment of tax pursuant to § 7-1-17(C) NMSA 1978. Additionally, unless the context of the usage of the term requires otherwise, “tax” is defined to include the amount of any interest or civil penalty relating to taxes. § 7-1-3(X) NMSA 1978. Thus, the presumption of correctness attaches to an assessment of penalty as well. *Tiffany Construction Co. v. Bureau of Revenue*, 90 N.M. 16, 558 P.2d 1155 (Ct. App. 1976), cert. denied, 90 N.M. 255, 561 P.2d 1348 (1977). Thus, the burden was on the Taxpayer to overcome the presumption that the assessment of penalty was proper.

The imposition of penalty is governed by the provisions of Section 7-1-69(A) NMSA 1978 (1998 Repl. Pam.), which imposes a penalty of two percent per month, up to a maximum of ten percent:

...in the case of failure, due to negligence or disregard of rules and regulations, but without intent to evade or defeat any tax, to pay when due any amount of tax required to be paid,... or to file by the date required a return....

This statute imposes penalty based upon negligence (as opposed to a willful or fraudulent intent) for failure to timely pay tax. Taxpayer "negligence" for purposes of assessing penalty is defined in Regulation 3 NMAC 1.11.10 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.

The Department argues that the Taxpayer was negligent and penalty was properly assessed because Lucy Strong was an employee of the Taxpayer, she was negligent in failing to timely file the tax returns for her employer, and under the doctrine of *respondeat superior*, the Taxpayer is liable for the negligent acts of its employee and must bear the consequences of those acts.

The Taxpayer argues that a distinction should be made, in terms of the imposition of penalty, between the actions of corporate officers and managers and those of lower level employees. In making this argument, the Taxpayer relies on the distinction New Mexico courts have drawn with respect to liability for punitive damages, between the acts of corporate officers and managers and those of lower level employees who are not authorized to exercise all corporate powers. *See, Albuquerque Concrete Coring Company, Inc. v. Pan Am World Services, Inc.*, 118 N.M. 140, 879 P.2d 772 (1994). This distinction has no applicability to the imposition of tax penalty, however. This distinction was specifically rejected by the Court of Appeals, which stated that the distinction:

does not apply in this case because, as discussed above, the penalty imposed under Section 7-1-69(A) bears no resemblance to punitive or exemplary damages, which are limited to punishment of conduct that is intentional. (citation omitted)

El Centro Villa Nursing Center v. Taxation and Revenue Department, 108 N.M. 795, 798, 779 P.2d 982 (Ct. App. 1989).

The Taxpayer also argues that Ms. Strong had reliably and timely filed its tax returns for many years and that it reasonably relied upon Ms. Strong in continuing to do so. The Taxpayer also presented testimony that Ms. Strong had been observed working on tax returns, that Mr. Adams had noticed that he had not signed any checks recently to pay taxes and he had inquired of Ms. Strong about that fact and had been informed that another officer had signed the checks, and that Mr. Adams had asked Ms. Strong if she needed any help with preparing the taxes and she had said no help was needed. The Taxpayer thus argues that it exercised the degree of ordinary business care and prudence which reasonable taxpayers would have exercised in similar circumstances, establishing that it was not negligent under the standard of Regulation 3 NMAC 1.10.11.

I agree with the Department that merely delegating the duties to an employee or agent would not be sufficient for a taxpayer to escape the imposition of penalty when the employee or agent was negligent in performing their duties. The negligent acts of the agent or employee would be attributable to the taxpayer. This was the holding of the Court of Appeals in *El Centro Villa, supra.*, which upheld the imposition of penalty upon a taxpayer who had delegated the obligation to prepare and file its tax returns to an accountant. In that case the taxpayer had received unusual and large Medicaid payments based upon Medicaid reimbursement adjustments made by the Human Services Department. Although the taxpayer reported gross receipts taxes on its normal Medicaid payments, it failed to report and pay tax on the adjustment payments. The court found negligence on the part of both the taxpayer and its accountant. The finding of negligence by the taxpayer was

based on the taxpayer's failure to alert its accountant to the unusual payments and the nature of those payments. The court found that the accountant was negligent in failing to implement an accounting system in such a way that checks and balances in the system would have alerted the accountant to the unusual income items so that they would be examined and reported properly for tax purposes.

Applying the reasoning of *El Centro Villa*, the penalty assessed by Assessment No. 2484951 with respect to the Taxpayer's November, 1998 gross receipts tax return, was properly imposed. This return was for a period prior to the time that the Taxpayer had observed any problems with Ms. Strong's demeanor or her work and the Taxpayer presented no evidence about the circumstances surrounding this return other than it is assumed that Ms. Strong had the duty to prepare and file this return and that she failed to do so. In the absence of other evidence, the Taxpayer has failed to carry its burden to overcome the presumption of correctness attaching to the assessment of penalty and Ms. Strong's negligence is properly attributable to the Taxpayer.

With regard to the other penalty assessments, covering the periods of July through October, 1999, the Taxpayer presented substantial evidence to explain why it had not become aware of the fact that Ms. Strong had not filed the returns. Although the Taxpayer's management was aware of Ms. Strong's apparent depression, it took actions to ensure that her mental problems had not affected her responsibility to prepare and file the returns at issue. They offered her assistance in preparing the returns, which she refused. They observed her working on tax returns. Mr. Adams asked about the payment of the taxes because he had noticed that he had not signed any tax checks in the recent past. In response, Ms. Strong affirmatively misled Mr. Adams, informing him that the checks had been signed by the other officer authorized to sign such checks. Ms. Strong also apparently concealed the letters from the various state tax agencies asking about non-filed returns,

because she picked up the mail. Could the Taxpayer have done more to ensure that tax reports were being filed and taxes paid? Of course. In hind-sight, a number of things could have been done which could have revealed the problem, such as asking to see copies of the returns, etc. The legal standard to be applied, however, is not did the Taxpayer do everything it could to ensure that such things do not happen. The standard is whether the Taxpayer failed to exercise the degree of ordinary business care and prudence which reasonable taxpayers would exercise under similar circumstances. In the circumstances of this case, where inquiry was made by the Taxpayer's management and the management was affirmatively misled by the actions and words of an employee who had been trustworthy in the past, and the time frame in which taxes were not paid was of a relatively short duration¹ such that internal checks and balances might not reasonably be expected to detect the problem, I believe that the Taxpayer exercised the degree of ordinary business care and prudence which reasonable taxpayers would be expected to exercise. As such, the Taxpayer has presented sufficient evidence to establish that it did not act negligently with respect to the non-filing and non-payment of taxes for the July through October, 1999 time period.

CONCLUSIONS OF LAW

1. The Taxpayer filed timely, written protests to Assessment Nos. 15669, 15670, 15672, 2484951, 2484974, 2484975, 2484976 and 2486055 and jurisdiction lies over both the parties and the subject matter of this protest.
2. The presumption of correctness which attaches to the assessment of tax also applies to the assessment of penalty.

¹ The time frame referenced is the four month period of July through November, 1999. A system which fails to reveal a non-filing and non-payment problem for a longer period, such as the year between November of 1998 and November, 1999 would probably fail the reasonableness test.

3. The Taxpayer failed to present evidence sufficient to rebut the presumption of correctness with respect to the penalty assessed by Assessment No. 2484951 for the November, 1998 reporting period.

4. With respect to the late filing and payment of taxes for the periods of July 1999 through October, 1999, the Taxpayer established that it exercised the degree or ordinary business care and prudence which reasonable taxpayers would exercise under similar circumstances where it was affirmatively misled by a previously reliable employee with respect to the timely reporting and filing of its returns for those periods. Thus, the Taxpayer met its burden of establishing that it was not negligent with respect to the late filing and payment of taxes for said period and the assessment of penalty was improper.

For the foregoing reasons, the Taxpayer's protest IS HEREBY GRANTED IN PART AND DENIED IN PART.

IT IS FURTHER ORDERED that the Department abate the penalty portions of Assessment Nos. 15669, 15670, 15672, 2484974, 2484975, 2484976 and 2486055.

DONE, this 26TH day of February, 2001.