

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

IN THE MATTER OF THE PROTEST OF
R & R PROFESSIONAL PHARMACY, INC.
I.D. No. 02-253882-00 8
DENIAL OF CLAIM FOR REFUND

No. 00-14

DECISION AND ORDER

A formal hearing on the above-referenced protest was held May 11, 2000 before Margaret B. Alcock, Hearing Officer. R & R Pharmacy, Inc. ("Taxpayer") was represented by Judy M. Paynter, one of its owners. The Taxation and Revenue Department ("Department") was represented by Bridget A. Jacober, Special Assistant Attorney General. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. During the period 1994-1997, the Taxpayer operated a pharmacy located in Santa Fe, New Mexico.
2. The Taxpayer was registered with the Department for payment of gross receipts, compensating and withholding taxes and filed monthly CRS-1 returns with the Department.
3. On several occasions, Judy Paynter, a shareholder and treasurer of the Taxpayer, called the Department with the following questions: Are all sales to government agencies tax exempt? Are there any exceptions? Ms. Paynter was consistently told that receipts from sales of tangible personal property to all government agencies were deductible and not subject to gross receipts tax.

4. Because Ms. Paynter believed that sales to patients covered by the federal Medicare program were sales to the federal government, the Taxpayer did not pay gross receipts tax on its receipts from these sales.

6. Ms. Paynter never asked the Department whether sales of tangible personal property to patients covered by Medicare were sales to the government, nor did she ask whether receipts from sales to patients covered by Medicare were subject to gross receipts tax.

7. In October 1997, the Department sent a letter to many New Mexico pharmacies which read, in pertinent part:

The New Mexico Taxation and Revenue Department Tax Compliance Bureau has completed an investigation of the pharmacy industry. The investigation has revealed gross receipts reporting errors within your industry.

Please review your records to ensure that the following gross receipts items have been reported correctly:

1. Receipts received from Medicare or other insurance providers are fully taxable.
2. Receipts received as insurance co-payments from individuals are fully taxable.

8. The Taxpayer did not receive this advisory letter from the Department, but Ms. Paynter was provided a copy by another pharmacy located in Santa Fe.

9. As soon as she read the letter, Ms. Paynter amended the Taxpayer's CRS-1 returns for the period 1994-1997 to include receipts from sales of tangible personal property to patients covered by Medicare.

10. The Taxpayer was subsequently assessed \$1,203.89 of interest and \$361.52 of penalty on the underpaid gross receipts tax reflected on the Taxpayer's amended returns. Pursuant to Department Regulation 3 NMAC 1.11.11.5, no penalty was assessed for the twelve months immediately preceding the date the Taxpayer voluntarily filed its amended returns.

11. The Taxpayer paid the penalty and interest assessed and then filed a claim for refund, stating that its non-compliance was unintentional and that it had been "ill advised" by the Department regarding the deductibility of Medicare revenues.

12. On April 6, 1998, the Taxpayer's claim for refund was denied by the Department.

13. On April 20, 1998, the Taxpayer filed a written protest to the denial of its claim for refund of penalty in the amount of \$361.52.

DISCUSSION

The sole issue to be determined is whether the Taxpayer is entitled to a refund of the penalty assessed on its underpayment of gross receipts tax on receipts from selling tangible personal property to patients covered by Medicare. Section 7-1-17(C) NMSA 1978 provides that any assessment of taxes made by the Department is presumed to be correct. Section 7-1-3(U) NMSA 1978 defines tax to include not only the amount of tax principal imposed but also, unless the context otherwise requires, "the amount of any interest or civil penalty relating thereto." Accordingly, the presumption of correctness applies to the Department's assessment of penalty, and it is the Taxpayer's burden to come forward with evidence to show that the assessment was incorrect. *See, El Centro Villa Nursing Center v. Taxation and Revenue Department*, 108 N.M. 795, 779 P.2d 982 (Ct. App. 1989).

The penalty the Taxpayer seeks to recover was assessed pursuant to Section 7-1-69(A) NMSA 1978, 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...

The term "negligence" 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 Taxpayer's underreporting of tax in this case was due to Ms. Paynter's belief that receipts from sales of tangible personal property to patients covered by Medicare were deductible as sales to the federal government. The Taxpayer has not challenged the Department's determination that Medicare receipts are subject to gross receipts tax. The Taxpayer has only challenged the imposition of penalty, arguing that Ms. Paynter was ill advised by Department employees and is entitled to a refund under Regulation 3 NMAC 1.11.11.1, which authorizes abatement of penalty when a taxpayer "proves the taxpayer was affirmatively misled by a Department employee."

Although Ms. Paynter testified that she called the Department several times and spoke with three different employees in the Tax Policy and Information Office, there is no evidence these employees misled Ms. Paynter as to her liability for tax on receipts from sales to Medicare patients. The only question Ms. Paynter asked was whether sales to government agencies were exempt from tax. In response, she was correctly advised that receipts from sales of tangible personal property to state and federal agencies were deductible and not subject to gross receipts tax. *See*, Section 7-9-54 NMSA 1978. Ms. Paynter never asked the Department whether sales of tangible personal property to patients covered by Medicare were sales to the government, nor did she ask whether receipts from sales to patients covered by Medicare were subject to gross receipts tax. Had she done so, she would have been told these receipts were fully taxable. Since at least 1992, it has been the Department's position that receipts from providing goods and services to Medicare patients are no different than receipts from providing goods and services to patients covered by other insurance providers. *See*,

Department Rulings 405-92-1, 401-93-1, 401-97-2, 405-97-3, and the October 1997 letter referenced in Finding of Fact No. 7, above.

The Taxpayer also argues that it should be excused from the negligence penalty because there was a general misunderstanding as to the taxability of Medicare payments and the Department should have done more to inform pharmacies of their tax obligations. In fact, the Department makes a continuing effort to educate taxpayers concerning New Mexico's tax laws. The Department holds regular workshops at its district offices; it has a variety of publications addressing issues of concern to various businesses; it issues regulations and gives taxpayers the opportunity to ask for written rulings on issues not specifically covered in the Department's regulations and publications. The Department is not omniscient, however, and cannot be expected to know what misunderstandings or reporting errors exist within every industry. Here, there is evidence the Department took action to notify the state's pharmacies as soon as it became aware of the underreporting of gross receipts tax on Medicare and other insurance payments.

New Mexico has a self-reporting tax system. It is the obligation of taxpayers, who have the most direct knowledge of their business activities, to determine their tax liabilities and accurately report those liabilities to the state. *See*, Section 7-1-13(B) NMSA 1978; *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). A taxpayer's erroneous belief that it does not owe taxes may constitute negligence for purposes of Section 7-1-69 NMSA 1978. *Id.* In this case, the Taxpayer's belief that it did not owe gross receipts tax on Medicare payments, without a showing that its belief was based on specific advice received from the Department or from a competent tax advisor, fails to establish a basis for refunding the penalty assessed.

CONCLUSIONS OF LAW

1. The Taxpayer filed a timely, written protest to the Department's denial of its claim for refund of penalty, and jurisdiction lies over the parties and the subject matter of this protest.

2. The Taxpayer has failed to meet its burden of showing that the Department's assessment of the negligence penalty imposed by Section 7-1-69 NMSA 1978 was incorrect.

For the foregoing reasons, the Taxpayer's protest IS DENIED.

DATED May 15, 2000.