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

IN THE MATTER OF THE PROTEST OF
WASTESTREAM RESOURCES No. 00-19
NM ID NO. 02-224688-00 6
ASSESSMENT NO. 2324585

DECISION AND ORDER

A formal hearing on the above-referenced protest was held June 22, 2000, before Margaret B. Alcock, Hearing Officer. WasteStream Resources was represented by its owner, Patricia A. Young ("Taxpayer"). The Taxation and Revenue Department ("Department") was represented by Monica M. Ontiveros, Special Assistant Attorney General. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. The Taxpayer is a sole proprietorship engaged in the environmental consulting business. The Taxpayer advises owners of small wastewater systems, acts as a liaison between system owners and engineers and, in some cases, acts as the operator of her client's wastewater treatment facilities.

2. During 1995, the Taxpayer's services included sampling and monitoring wastewater in accordance with government regulations and selecting and purchasing the equipment and supplies needed to operate her clients' treatment facilities.

3. All laboratory services, equipment and supplies ordered by the Taxpayer were billed directly to the Taxpayer, and the vendors looked to the Taxpayer for payment. Although the name of the Taxpayer's client was listed on the paperwork given to each laboratory to establish the chain of

custody for wastewater samples, the laboratory sent its invoices to the Taxpayer and it was her responsibility to pay the laboratory's charges.

4. The vendors who sold equipment, supplies and laboratory services to the Taxpayer included the New Mexico gross receipts tax as part of the price charged to the Taxpayer.

5. The Taxpayer invoiced each client for labor charges and the cost of laboratory services, equipment and supplies she purchased or leased for use in the client's wastewater treatment facility. By express agreement with her clients, the Taxpayer added a ten percent service fee to the cost of services and materials purchased from third parties. This fee was designed to compensate the Taxpayer for her expertise and the time she spent selecting the appropriate vendor and making the purchase.

6. The Taxpayer's invoices included gross receipts tax on labor charges and the ten percent service fee on purchases from third parties. The Taxpayer did not include gross receipts tax on her charges for services and materials purchased from third parties.

7. Consistent with her invoicing methods, the Taxpayer reported and paid gross receipts tax on her receipts from labor and service fees, but did not report or pay gross receipts tax on amounts she received from her clients as reimbursement for the cost of services and materials purchased from third parties.

8. The Taxpayer's 1995 federal income tax return reported all receipts from her environmental consulting business as business income on Schedule C to Form 1040, including the amount of reimbursed expenses.

9. In September 1998, the Department sent the Taxpayer notice that it was conducting a limited scope audit of her 1995 gross receipts taxes and asked her to explain why the receipts

reported on her 1995 gross receipts tax returns were lower than the receipts reported as business income on her 1995 federal income tax return.

10. In January 1998, the Taxpayer had received a similar inquiry from the Department concerning her 1994 gross receipts taxes. The Taxpayer responded to that inquiry with a letter explaining that the discrepancy between the income reported for state gross receipts tax purposes and the income reported for federal income tax purposes was attributable to reimbursements received for goods and services purchased on behalf of her clients. The Department accepted the Taxpayer's explanation and no assessment was issued against her for tax year 1994.

11. When the Taxpayer received the Department's inquiry concerning her 1995 gross receipts taxes, she responded with a letter of explanation that was virtually identical to the letter sent in response to the inquiry concerning her 1994 taxes. This time, however, the Department employee assigned to the audit requested more information to establish that the Taxpayer's receipts were not subject to gross receipts tax.

12. The Taxpayer subsequently met with the employee and the employee's supervisor in Albuquerque to discuss the matter. The Department's employees were uncertain as to whether the Taxpayer's receipts from reimbursed expenses were subject to tax and told the Taxpayer they would have to refer the matter to Santa Fe.

13. The Taxpayer did not hear anything further from the Department concerning the taxability of her receipts until December 17, 1998, when the Department issued Assessment No. 2324585 to the Taxpayer in the total amount of $2,813.22, representing gross receipts tax, penalty and interest due for tax periods January through December 1995.

14. On January 8, 1999, the Taxpayer filed a written protest to the Department's assessment.

15. Based on additional information provided by the taxpayer, the Department made a partial abatement of tax, penalty and interest attributable to services the Taxpayer performed for an Native American enterprise operating on tribal land. The current balance remaining on the assessment is $1,526.12 gross receipts tax, plus penalty and interest.

DISCUSSION

The Taxpayer challenges the Department's assessment on the following grounds: (1) the Taxpayer was purchasing goods and services as an agent for her clients and should not be liable for gross receipts tax on these reimbursed expenses; (2) imposing tax on the Taxpayer's reimbursed expenses results in double taxation; (3) the Taxpayer should be excused from payment of the tax because she was ill-advised by the Department; and (4) the Taxpayer should be excused from payment of penalty and interest because the tax laws are too complex for the average taxpayer to understand.

Section 7-1-17(C) NMSA 1978 provides that any assessment of tax 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 Taxpayer has the burden of producing evidence to establish that the Department's assessment of gross receipts tax, penalty and interest for tax year 1995 is incorrect. *See also*, *El Centro Villa Nursing Center v. Taxation and Revenue Department*, 108 N.M. 795, 779 P.2d 982 (Ct. App. 1989).

(1) Tax on Reimbursed Expenses. Section 7-9-4 NMSA 1978 imposes an excise tax on the gross receipts of any person engaging in business in New Mexico. Section 7-9-3(F) defines the term "gross receipts" to include receipts from selling property in New Mexico, leasing property employed in New Mexico or selling services performed in New Mexico. The term "gross receipts" does not include amounts received solely on behalf of another in a disclosed agency capacity.

Regulation 3 NMAC 2.1.19.3.1 provides the following explanation concerning reimbursements of expenses a taxpayer incurs on behalf of a client:

> 19.3 **REIMBURSED EXPENDITURES**:
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> 19.3.1 The receipts of any person received as a reimbursement of expenditures incurred in connection with the performance of a service or the sale or lease of property are gross receipts as defined by Subsection F of Section 7-9-3, unless that person incurs such expense as agent on behalf of a principal while acting in a disclosed agency capacity. An agency relationship exists if a person has the power to bind a principal in a contract with a third party so that the third party can enforce the contractual obligation against the principal.

In this case, the Taxpayer would be acting in a disclosed agency capacity only if she were authorized to legally bind her client to the terms of any purchase contract she entered into on the client's behalf. In that situation the client—not the Taxpayer—would be primarily liable for payment of the goods and services purchased.

Based on the facts presented at the hearing, the Taxpayer was not acting in a disclosed agency capacity in 1995. Instead, the Taxpayer was purchasing goods and services in her own name and either reselling those items to her clients or using the purchased items in the performance of her own services. Although a laboratory hired to analyze wastewater samples might have known the identity of the Taxpayer's client, the laboratory had no legal basis to sue the client if the Taxpayer failed to pay the laboratory's charges. Nor did vendors of equipment and supplies purchased by the Taxpayer have the right to enforce payment against the Taxpayer's clients. At the hearing, the Taxpayer testified that she did not always tell vendors the name of the client for whom she was purchasing goods. In some cases, items were bought in bulk and the vendor had no way of knowing which items would be used by the Taxpayer in performing services for a particular client. Given these facts, the payments the Taxpayer received as reimbursement for expenditures made on behalf

of her clients were not received in a disclosed agency capacity and were gross receipts subject to tax.

(2) Double Taxation. The Taxpayer argues that imposing tax on her reimbursed expenses results in double taxation because the vendors who sold equipment, supplies and laboratory services to the Taxpayer included the gross receipts tax as part of the purchase price. It is a popular misconception that there is something inherently illegal or unconstitutional with double taxation. In fact, New Mexico's courts have held, on numerous occasions, that there is no prohibition against double taxation. *See, e.g., New Mexico State Board of Public Accountancy v. Grant*, 61 N.M. 287, 299 P.2d 464 (1956); *Amarillo-Pecos Valley Truck Line, Inc. v. Gallegos*, 44 N.M. 120, 99 P.2d 447 (1940); *State ex rel. Attorney General v. Tittmann*, 42 N.M. 76, 75 P.2d 701 (1938). *See also*, *Ft. Smith Lumber Co. v. Arkansas*, 251 U.S. 532 (1920).

In construing the New Mexico Gross Receipts and Compensating Tax Act, the New Mexico courts have also held there is no double taxation where the two taxes complained of are imposed on the receipts of different taxpayers. *See, House of Carpets, Inc. v. Bureau of Revenue*, 87 N.M. 747, 507 P.2d 1078 (Ct. App. 1973); *New Mexico Sheriffs & Police Association v. Bureau of Revenue*, 85 N.M. 565, 514 P.2d 616 (Ct. App. 1973). That is the case here. When a vendor sells goods or services to the Taxpayer, the vendor is the entity liable for gross receipts tax on the sale—the Taxpayer has no obligation to report or pay tax on the vendor's receipts. When the Taxpayer charges her clients for the goods and services purchased from third parties, the Taxpayer is the entity liable for gross receipts tax on these transactions—neither the vendor nor the client has any obligation to report or pay tax on the Taxpayer's receipts. Although it is common practice for a seller to pass the cost of the gross receipts tax on to the buyer, this does not change the legal incidence of the tax. If

the buyer refuses or neglects to pay the amount of the passed-on gross receipts tax, the seller is still responsible for paying the tax to the state.

Even though taxing successive transactions is not double taxation, the New Mexico legislature has provided a number of statutory deductions to prevent the pyramiding or stacking of the gross receipts tax. For example, it has provided a deduction for the sale of tangible personal property for resale when the purchaser of the property provides the seller with a nontaxable transaction certificate (NTTC) and represents that the property will be resold. Section 7-9-47 NMSA 1978. There is also a deduction for the sale of services for resale when certain statutory conditions are met. Section 7-9-48 NMSA 1978. To the extent the Taxpayer is purchasing goods and services for resale to her clients (as opposed to using the items in the performance of her own services) the Taxpayer is eligible to apply to the Department to obtain NTTCs to give to her vendors. This would allow the vendors to deduct their receipts from the sale of goods and services to the Taxpayer and eliminate the vendors' gross receipts tax on these sales.

(3) Erroneous Advice from the Department. The Taxpayer contends she should be excused from payment of additional gross receipts tax because she was ill-advised by a Department employee. The Taxpayer was first contacted by the Department in January 1998. At that time, the Department asked the Taxpayer to explain the discrepancy between the receipts reported on her 1994 gross receipts tax returns and the receipts reported as business income on her 1994 federal income tax return. The Taxpayer responded with a letter explaining that the discrepancy was attributable to reimbursements received for goods and services purchased on behalf of her clients. The Department accepted the Taxpayer's explanation and no assessment was issued against her for tax year 1994. When the Taxpayer received the Department's inquiry concerning her 1995 gross receipts taxes, she responded in the same way. This time, however, the Department determined that her reimbursed

expenses were subject to gross receipts tax and issued the assessment that is the subject of this protest.

In her protest letter, the Taxpayer expressed her concern that the Department's failure to advise her correctly concerning her 1994 gross receipts taxes prevented her from obtaining timely NTTCs from her vendors. Under the facts of this case, the Taxpayer could not have avoided tax on her receipts through the use of NTTCs. As discussed in Section (2) above, the Taxpayer may be entitled to give NTTCs *to* its vendors—there is no basis for the Taxpayer to accept NTTCs *from* those vendors. If the Taxpayer had given NTTCs to its vendors in 1995, the vendors could have deducted their receipts from selling goods and services to the Taxpayer. The Taxpayer still would have been liable for gross receipts tax on her receipts from her clients, including amounts received as reimbursement for the cost of goods and services purchased from third parties.

This is not a situation where the Taxpayer was paying tax on her receipts and then stopped in reliance on advice received from the Department. The Taxpayer made her own determination that gross receipts tax was not due on her reimbursed expenses. It was not until 1998, three years after the taxes at issue were due, that the Taxpayer was contacted by the Department. In *Wing Pawn Shop v. Taxation and Revenue Department,*, 111 N.M. 735, 742, 809 P.2d 649, 656 (Ct. App. 1991), the court of appeals addressed a similar fact pattern as follows:

> Taxpayer argues that we may apply estoppel principles against the department if it misled taxpayer into thinking he did not owe the tax and he justifiably relied on the department to his detriment.... In support of his argument that estoppel principles are relevant here, taxpayer maintains that, before the audit period in question, representations justifying estoppel were made by the department.... Yet, taxpayer relies solely on the undated letter he received in 1986 in response to his protest. The record is absent of any prior representations, aside from taxpayer's bald assertion that they were made.
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> We reject taxpayer's estoppel arguments for two reasons. First, the undated letter, even if we assume that it misled taxpayer into believing the sale proceeds

> were not subject to gross receipts tax, was transmitted to him **after**, not before, the transactions in question occurred. It is difficult for us to fathom how a departmental communication to taxpayer after he had failed to pay gross receipts tax can be reasonably relied on for application of estoppel principles.... (emphasis the court's)

The advice the Taxpayer received from the Department in 1998 cannot serve as a basis to excuse the Taxpayer from payment of gross receipts taxes due in 1995.

(4) Complexity of the Tax Laws. The Taxpayer contends the tax laws are too complex for the average taxpayer to understand and asks the hearing officer to waive the penalty and interest assessed against her. Neither the Department nor the Department's hearing officer has the authority to relieve taxpayers of obligations imposed by the legislature. The hearing officer is limited to construing the tax statutes as written and applying those statutes in accordance with legislative intent. The hearing officer may not rewrite the language of the statutes or second-guess the wisdom of the legislature's enactments.

Interest. Section 7-1-67 NMSA 1978 governs the imposition of interest on late payments of tax and provides, in pertinent part:

> If any tax imposed is not paid on or before the day on which it becomes due, ***interest shall be paid*** to the state on such amount from the first day following the day on which the tax becomes due, without regard to any extension of time or installment agreement, until it is paid... (emphasis added).

The legislature's use of the word "shall" indicates that the assessment of interest is mandatory rather than discretionary. *State v. Lujan*, 90 N.M. 103, 560 P.2d 167 (1977). The legislature has directed the Department to assess interest whenever taxes are not timely paid and has provided no exceptions to the mandate of the statute. The assessment of interest is not designed to punish taxpayers, but to compensate the state for the time value of unpaid revenues. The reason for a late payment of tax is irrelevant to the imposition of interest. Even taxpayers who obtain a formal extension of time to pay

tax are liable for interest from the original due date of the tax to the date payment is made. Section 7-1-13(E) NMSA 1978.

In this case, the Taxpayer failed to pay gross receipts taxes due on her receipts from reimbursed expenses. Although it is clear the Taxpayer is an honest person who had no intent to cheat the state, it is also clear the taxes were due and owing. Under the provisions of Section 7-1-67 NMSA 1978, imposition of interest is mandatory.

Penalty. Section 7-1-69 NMSA 1978 governs the imposition of penalty. Sub-section A imposes a penalty of two percent per month, up to a maximum of ten percent, when a taxpayer fails "due to negligence or disregard of rules and regulations" to pay taxes in a timely manner. 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;
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> 2) inaction by taxpayers where action is required;
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> 3) inadvertence, indifference, thoughtlessness, carelessness, erroneous belief or inattention.

The Taxpayer's failure to pay gross receipts tax was due to her erroneous belief that tax was not due on reimbursed expenses. This comes within the definition of negligence. The Taxpayer maintains the tax laws were too complex for her to understand. There was no evidence presented, however, to explain exactly what efforts the Taxpayer made to determine the extent of her tax obligations.

Whether a taxpayer has acted negligently for purposes of the penalty imposed by Section 7-1-69 NMSA 1978 is determined as of the date the taxes were due. The Department has a regulation—which was in effect in 1995—that discusses when reimbursed expenses are subject to tax. *See*, Regulation 3 NMAC 2.1.19.3.1, quoted in Section (1), above. There is no evidence the Taxpayer

reviewed this or any other regulation prior to filing her 1995 gross receipts tax returns. There is no evidence the Taxpayer had any discussions with employees of the Department in 1995. Although the Taxpayer testified that her accountant prepared her 1995 income tax returns, there is no evidence the Taxpayer had any specific discussions with her accountant concerning the method she used to report her 1995 gross receipts taxes.

The New Mexico courts have held that 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 lack of knowledge or erroneous belief concerning the tax laws may constitute negligence when the taxpayer has failed to consult with an attorney or an accountant. *Id.* As confirmed in a recent decision of the court of appeals, this consultation must occur at the time the taxes are due:

> Where the taxpayer ignores its tax obligations and consults with an attorney or accountant about its tax obligations only **after** an audit and assessment by the Department, such conduct is not evidence of a diligent protest and does not provide a basis for avoiding a penalty. (emphasis the court's)

Sonic Industries, Inc. v. Taxation and Revenue Department, Court of Appeals Docket No. 20,676, Slip Opinion page 14 (filed July 3, 2000). Here, the Taxpayer's discussions with the Department and her various tax advisers concerning her 1995 gross receipts tax liability occurred more than three years after the taxes were due. Regardless of the complexity of the tax law at issue, these after-the-fact discussions do not support a waiver of penalty.

CONCLUSIONS OF LAW

1. The Taxpayer filed a timely, written protest to Assessment No. 2324585, and jurisdiction lies over the parties and the subject matter of this protest.

2. The reimbursements the Taxpayer received from her clients for goods and services purchased from third parties were not received solely on behalf of another in a disclosed agency capacity. These reimbursements were receipts from engaging in business and were subject to gross receipts tax.

3. The imposition of gross receipts tax on the Taxpayer's reimbursed expenses does not constitute illegal or unconstitutional double taxation.

4. The Taxpayer's receipt of erroneous advice from a Department employee more than three years after the date the taxes at issue were due does not provide a basis for abating the tax, penalty or interest assessed.

5. The Taxpayer was late in paying gross receipts taxes due to the state and interest was properly assessed pursuant to Section 7-1-67 NMSA 1978.

6. The Taxpayer was negligent in failing to pay gross receipts tax on her reimbursed expenses and penalty was properly assessed pursuant to Section 7-1-69 NMSA 1978.

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

DATED July 11, 2000.