

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

**IN THE MATTER OF THE PROTEST OF
SARCON CONSTRUCTION CORPORATION
ID NO. 02-284743-00-0
ASSESSMENT NOS. 2516831 & 2516832**

No. 02-22

DECISION AND ORDER

A formal hearing on the above-referenced protest was held September 10, 2002, before Margaret B. Alcock, Hearing Officer. Sarcon Construction Corporation ("Taxpayer") was represented by Alan Brown, who is a certified public accountant and the company's controller. The Taxation and Revenue Department ("Department") was represented by Javier Lopez, 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 engaged in business in New Mexico and is registered with the Department for payment of gross receipts, compensating and withholding taxes, which are required to be paid monthly under the Department's combined reporting system ("CRS").
2. In June 1997, the Taxpayer hired a bookkeeper named Kathy to handle its in-house accounting and tax reporting. Kathy remained in this position during all periods relevant to this protest.
3. During 1999, the Taxpayer decided to switch its accounting software to accommodate growth in the Taxpayer's business and to insure that its accounting system would be Y2K compliant.

4. The transition to a new accounting system was not instantaneous and required Kathy to maintain parallel books for the months of October, November, and December 1999, which more than doubled her workload.

5. In January 2000, Kathy discovered inconsistencies in the 1999 year-end totals calculated by each accounting program. This required a reconciliation of data between the two systems and also impacted data entered into the Taxpayer's accounting system for 2000.

6. The Taxpayer's accountant needed accurate information to prepare the Taxpayer's 1999 financial reports, which the Taxpayer's surety company used to determine the Taxpayer's bonding capacity. Bonding capacity is critical to the Taxpayer's business, and the Taxpayer's corporate officers put increased pressure on Kathy to complete the transition to the new accounting system.

7. Because of the increased workload and her focus on the Taxpayer's accounting system, Kathy forgot to file CRS-1 returns with the Department for the January and February 2000 reporting periods.

8. In late March 2000, Kathy discovered her oversight and filed the Taxpayer's CRS-1 returns for January and February 2000. A check in payment of the tax principal accompanied the return.

9. On April 15, 2000, the Department issued Assessment Nos. 2516831 and 2516832 to the Taxpayer, assessing combined penalty and interest of \$5,075.51 on the Taxpayer's late payment of CRS taxes for the months of January and February 2000.

10. On May 17, 2000, the Taxpayer filed a written protest to the Department's assessments of penalty and interest, which was accepted as timely after the Department granted the Taxpayer's retroactive extension of time to file the protest.

DISCUSSION

The issue to be decided is whether the Taxpayer is liable for the interest and penalty assessed on its late payment of CRS taxes for the January 2000 and February 2000 reporting periods. Section 7-1-17 NMSA 1978 provides that any assessment of tax by the Department is presumed to be correct. Section 7-1-3 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." *See also, El Centro Villa Nursing Center v. Taxation and Revenue Department*, 108 N.M. 795, 779 P.2d 982 (Ct. App. 1989). Accordingly, the assessments issued to the Taxpayer are presumed to be correct, and it is the Taxpayer's burden to present evidence and legal argument showing that it is entitled to an abatement.

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

A. If a tax imposed is not paid on or before the day on which it becomes due, **interest shall be paid** to the state on that 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. In this case, the Taxpayer's late payment of CRS taxes denied the State the use of funds to which it was legally entitled. Pursuant to Section 7-1-67 NMSA 1978, interest was properly assessed for the period between the statutory due dates for those taxes and the date payment was received.

Assessment of Penalty. Section 7-1-69 NMSA 1978 governs the imposition of penalty. Subsection A imposes a penalty of two percent per month or any fraction of a month, up to a maximum of ten percent, that a taxpayer fails “due to negligence or disregard of rules and regulations” to pay taxes or file required tax reports in a timely manner. Taxpayer negligence for purposes of assessing penalty is defined in Regulation 3.1.11.10 NMAC as:

- A. failure to exercise that degree of ordinary business care and prudence which reasonable taxpayers would exercise under like circumstances;
- B. inaction by taxpayers where action is required;
- C. inadvertence, indifference, thoughtlessness, carelessness, erroneous belief or inattention.

New Mexico case law confirms that penalties may properly be assessed even when a taxpayer’s late payment is based on inadvertent error or unintentional failure to pay the tax due. *Arco Materials, Inc. v. Taxation & Revenue Department*, 118 N.M. 12, 16, 878 P.2d 330, 334 (Ct. App. 1994) *rev'd on other grounds by Blaze Construction Co. v. Taxation & Revenue Department*, 118 N.M. 647, 884 P.2d 803 (1994); *El Centro Villa Nursing Center v. Taxation & Revenue Department*, 108 N.M. 795, 797-798, 779 P.2d 982, 984-985 (Ct. App. 1989).

In this case, there was conflicting evidence concerning the reason for the Taxpayer’s late payment of CRS taxes. On May 17, 2000, Will Pestalozzi, the Taxpayer’s vice-president, submitted a letter protesting the Department’s assessments of penalty and interest. In setting out the grounds for the protest, Mr. Pestalozzi described the problems encountered in the transition to the Taxpayer’s new accounting system and explained the pressure that Kathy, the Taxpayer’s bookkeeper, was under to implement the system in a timely manner. As stated in the May 17, 2000 letter: “Under this additional pressure, starting in early January, Kathy neglected to pay the CRS-1 taxes, she simply forgot.”

Unfortunately, Mr. Pestalozzi passed away prior to the date of the hearing on the Taxpayer's protest and was not available to testify. Kathy had also left the company. The Taxpayer was represented at the hearing by Alan Brown, who became the Taxpayer's controller in April 2001. Mr. Brown's explanation for the Taxpayer's late payment of CRS taxes was somewhat different than Mr. Pestalozzi's explanation. According to Mr. Brown, Kathy did not forget to file the Taxpayer's returns for January and February 2000, but was unable to file the returns because she could not determine the correct amount of CRS taxes due to the State until she completed the reconciliation of data between the two accounting programs. Mr. Brown acknowledged that he had never spoken to Kathy and had no personal knowledge of the facts at issue. He said that his testimony was based on his conversations with the Taxpayer's president.

While I found Mr. Brown to be an honest and straightforward witness, I believe the statements in Mr. Pestalozzi's May 17, 2000 protest letter are more reliable than Mr. Brown's testimony, which is based on a third party's current recollection of events that occurred more than two years ago. Mr. Pestalozzi was the Taxpayer's vice-president during the period at issue and he was the person Kathy notified when she received the Department's assessments. Mr. Pestalozzi stated that he and Kathy "have discussed this issue at length." Aside from Kathy herself, it appears that he was in the best position to know why Kathy failed to file timely reports for January and February 2000. According to Mr. Pestalozzi, "she simply forgot." Forgetting to file tax returns clearly comes within the definition of negligence set out in the Department's regulations.

The negligence penalty would apply even under Mr. Brown's version of events. If Kathy had been unable to determine the Taxpayer's CRS liability using the data in the Taxpayer's accounting system, she could have turned to other sources of information. Mr. Brown acknowledged that it would have been possible to come up with a reasonable estimate of the taxes due using bank

deposits, invoices, and other records of the Taxpayer. He also conceded that it would have been prudent for the Taxpayer to notify the Department of the system problems and seek advice on how to proceed. Finally, the Taxpayer could have applied to the Department for an extension of time to file and pay its CRS taxes during the period that its computer system was inoperative. *See*, Section 7-1-13 NMSA 1978 and Department Regulation 3.1.4.12 NMAC, which provides instructions and specific examples to assist taxpayers in obtaining such extensions. Given the various alternatives available, the Taxpayer's failure to file timely CRS returns was negligent under either version of the facts presented.

CONCLUSIONS OF LAW

1. The Taxpayer filed a timely, written protest to Assessment Nos. 2516831 and 2516832, and jurisdiction lies over the parties and the subject matter of this protest.

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

3. The Taxpayer was negligent in failing to pay its CRS taxes in a timely manner and penalty was properly assessed pursuant to Section 7-1-69 NMSA 1978.

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

DATED September 16, 2002.