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

IN THE MATTER OF THE PROTEST OF
MISTY BLUE a/k/a Misty Montgomery **No. 02-26**
ID NO. 02-341362-00-0
ASSESSMENT NO. 2279823

DECISION AND ORDER

A formal hearing on the above-referenced protest was held October 23, 2002, before Margaret B. Alcock, Hearing Officer. Misty Blue ("Taxpayer") represented herself. The Taxation and Revenue Department ("Department") was represented by Bruce J. Fort, Special Assistant Attorney General. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. From February 1988 through July 1994, the Taxpayer worked as the marketing director of Bright Beginnings Child Development Centers in Albuquerque, which qualified as a nonprofit organization under Section 501(c)(3) of the Internal Revenue Code.

2. In addition to paying her salary (from which state and federal income and social security taxes were withheld), Bright Beginnings made contributions into a profit-sharing plan on the Taxpayer's behalf and usually gave her a small holiday bonus.

3. In 1994, Bright Beginnings determined that it no longer needed the Taxpayer's services full time, but asked her to continue to provide marketing services on a part-time basis as an independent contractor.

4. Effective August 1, 1994, the Taxpayer and Bright Beginnings entered into a contract under which the Taxpayer was paid $900.00 per month to provide the company with a marketing plan and various marketing services.

5. At the time the contract was signed, Bright Beginnings told the Taxpayer that it would no longer withhold income or social security taxes from her paychecks and that she would be responsible for her own taxes. Bright Beginnings continued to make contributions into its profit-sharing plan on behalf of the Taxpayer and continued to pay the Taxpayer a small holiday bonus.

6. Bright Beginnings issued the Taxpayer a Type 9 New Mexico non-taxable transaction certificate ("NTTC"). The back of the NTTC form states that Type 9 certificates may be issued by governmental agencies and 501(c)(3) organizations "for the purchase of TANGIBLE PERSONAL PROPERTY ONLY. These certificates may not be used for the purchase of services...." (Emphasis in the original).

7. The Taxpayer did not read the back of the NTTC form and did not understand that the NTTC was not applicable to her sale of marketing services to Bright Beginnings.

8. The tasks the Taxpayer was required to perform under her contract with Bright Beginnings included preparing an annual budget, assessing mass mailing and survey programs, preparing brochures for each program area, working with advertising vendors, assessing the company's opportunity for growth, and attending and participating in workshops and meetings as requested.

9. The contract was result-oriented and did not require the Taxpayer to work any specified number of hours in return for the $900 monthly payment.

10. Bright Beginnings asked the Taxpayer to be in the office on certain days when the owner of the company would be present. Except for these requests, the Taxpayer set her own schedule and performed much of her work at home.

11. The Taxpayer purchased her own office supplies and used her home telephone and personal automobile in performing services for Bright Beginnings. During 1995, the Taxpayer also paid her own way to a child development conference held in Chicago.

12. Bright Beginnings was sold in August or September 1995, at which time it made lump-sum distributions from its profit-sharing plan. The Taxpayer received a $6,900 payment from the plan.

13. The Taxpayer's contract for marketing services continued under the new owners and was finally terminated in November 1996.

14. The Taxpayer filed a 1995 federal income tax return reporting the income from her marketing services as business income on Schedule C to her federal return. The Taxpayer also claimed a number of business expenses on Schedule C, including mileage for commuting between her home and the office, her travel expenses to the child development conference in Chicago, the portion of her telephone bills attributable to calls made on behalf of Bright Beginnings, and the cost of office supplies.

15. In 1998, the Department received information from the Internal Revenue Service concerning the business income reported on the Taxpayer's 1995 federal income tax return. When the Department investigated, it found that the Taxpayer was not registered with the Department and had not reported or paid gross receipts tax on this income.

16. On August 2, 1998, the Department issued Assessment No. 2279823 to the Taxpayer in the total amount of $1,513.03, representing gross receipts tax, penalty and interest on her business receipts for tax periods January through December 1995.

17. On August 20, 1998, the Taxpayer filed a written protest to the Department's assessment.

18. On July 3, 2002, the Department filed a request for hearing on the Taxpayer's protest. On July 10, 2002, a hearing was scheduled for October 23, 2002.

19. At the hearing, the Department stipulated that the Taxpayer is not liable for the gross receipts tax, penalty and interest assessed on the $6,900 lump sum payment she received in 1995 as a distribution from Bright Beginnings' profit-sharing plan.

DISCUSSION

The Taxpayer challenges the Department's assessment of gross receipts tax, penalty and interest on the income she earned under her contract with Bright Beginnings on the following grounds: (1) it was not clear to the Taxpayer that she was performing services as an independent contractor rather than as an employee; (2) the Taxpayer was entitled to rely on the Type 9 NTTC issued by Bright Beginnings; (3) the Department's delay in assessing the Taxpayer and in responding to the Taxpayer's correspondence should relieve the Taxpayer of her liability for all or part of the taxes, interest and penalty assessed; and (4) the Taxpayer has limited financial resources as a result of her decision to dedicate most of her time to volunteer community service, and she is unable to pay the full amount of the Department's assessment.

Burden of Proof. Section 7-1-17(C) NMSA 1978 provides that any assessment of tax by the Department is presumed to be correct. Accordingly, the Taxpayer has the burden of producing evidence to establish that the Department's assessment of gross receipts tax, penalty and interest on

her 1995 income is incorrect. *Archuleta v. O'Cheskey*, 84 N.M. 428, 431, 504 P.2d 638, 641 (Ct. App. 1972).

Employee v. Independent Contractor. The Taxpayer maintains that it is not clear whether she was performing services during 1995 as an independent contractor or as an employee. This distinction is important because income earned as an independent contractor is subject to gross receipts tax while income earned as an employee is not. *See*, Section 7-9-17 NMSA 1978.

In determining whether a person is an independent contractor or an employee, the principal consideration is the right to control. The relationship of employer and employee usually results where there is control over the manner and method of performance of the work to be performed. Where there is only control over the results, and not the details of the performance, the worker is usually considered to be an independent contractor. *Burruss v. B.M.C. Logging Co.*, 38 N.M. 254, 31 P.2d 263 (1934). *See also*, *Harger v. Structural Services, Inc.*, 121 N.M. 657, 663, 916 P.2d 1324, 1330 (1996). Department Regulation 3.2.105.7 NMAC sets out several factors to be considered in determining whether a worker qualifies as an employee, including whether taxes are withheld, whether worker's compensation and unemployment insurance contributions are made on behalf of the employee, and whether the employer has "a right to exercise control over the means of accomplishing a result or only over the result."

From February 1988 through the end of July 1994, the Taxpayer worked for Bright Beginnings as an employee and had income and social security taxes withheld from her paychecks. Beginning in August 1994, the parties changed their relationship and entered into a contract under which the Taxpayer was paid a flat monthly fee for the performance of her services. The Taxpayer's compensation was based on results, not on the number of hours worked. She was no longer required to keep regular office hours and much of her work was done at home. The Taxpayer purchased her own

office supplies and used her home telephone and personal automobile in performing her services. At the time the contract was signed, the Taxpayer understood that Bright Beginnings would not withhold income or social security taxes from the payments she received. The Taxpayer reported her 1995 income as business income on Schedule C to her federal income tax return and claimed a deduction for the expenses she incurred for mileage, travel, telephone calls and office supplies. The Taxpayer also paid both the employee's and the employer's share of social security tax due on her income based on her understanding that she was now self-employed.

Based on the evidence presented, there is no question that the Taxpayer was working as an independent contractor during 1995. Although the Taxpayer's failure to pay gross receipts tax on her income resulted from her lack of knowledge and not from an intent to evade her responsibilities to the state, that does not excuse her from payment of the tax due.

Reliance on NTTC. Bright Beginnings issued the Taxpayer a Type 9 New Mexico non-taxable transaction certificate ("NTTC"). The Taxpayer maintains that she relied on the following sentence appearing on the front of the NTTC form: "The seller must accept this certificate in good faith that the buyer will employ the property or service transferred in a nontaxable manner." This sentence must be read in conjunction with the information set out on the back of each NTTC, which explains the limitations on the use of each type of NTTC issued by the Department. The back of the Type 9 NTTC clearly states that Type 9 certificates may be issued by governmental agencies and 501(c)(3) organizations "for the purchase of TANGIBLE PERSONAL PROPERTY ONLY. These certificates may not be used for the purchase of services...." (Emphasis in the original). The Taxpayer acknowledged that she never read the back of the NTTC she accepted from Bright Beginnings. Had she done so, she would have known that she could not rely on the NTTC to deduct her receipts from the sale of marketing services to Bright Beginnings.

Delay in Assessment. The Taxpayer questions why the Department took so long to notify her of her gross receipts tax liability. By the time she received the Department's assessment in August 1998, the penalty had reached its statutory maximum of 10 percent and substantial interest had accrued. The Taxpayer testified that she would have paid the gross receipts tax if she had been alerted sooner, and believes the Department is at fault for the accrual of additional penalty and interest.

This argument is based on a misunderstanding of New Mexico's self-reporting tax system. It is the obligation of taxpayers, who have the most accurate and direct knowledge of their 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, 17, 558 P.2d 1155, 1156 (Ct. App. 1976), *cert. denied*, 90 N.M. 255, 561 P.2d 1348 (1977). There are insufficient government resources available for the Department to continually audit every citizen to determine whether he or she has fully complied with state tax laws. Although the Department performs periodic "tape matches" that compare information reported to the IRS with information reported to New Mexico, there is some delay before the federal tape match information is made available to the Department. Section 7-1-18(C) NMSA 1978 gives the Department seven years to assess taxes relating to any period for which required returns were not filed. The August 1998 assessment issued to the Taxpayer was well within the time limits provided by the New Mexico Legislature.

Delay in Setting a Hearing. Section 7-1-24(D) NMSA 1978 states: "Upon timely receipt of a protest, the department or hearing officer shall promptly set a date for hearing and on that date hear the protest or claim." The Taxpayer's protest of the Department's assessment was filed on August 20, 1998. On July 3, 2002, the Department's attorney filed a Request for Hearing, and on July 10, 2002, the Department's hearing officer scheduled a hearing for October 23, 2002. There is no

question that the Department was dilatory in its handling of the Taxpayer's protest. At the administrative hearing, the Department's attorney apologized to the Taxpayer for the delay in bringing this matter to hearing. The issue remains as to whether there is any legal basis for adjusting the amount of additional penalty and interest attributable to the Department's delay.

Section 7-1-69(A) NMSA 1978 imposes a negligence penalty of two percent per month, up to a maximum of ten percent, for a taxpayer's failure to pay taxes in a timely manner. Based on this statutory formula, penalty stops accruing five months after the due date of the tax. Here, the penalty assessed against the Taxpayer reached its maximum of ten percent prior to the date of the Department's assessment, and no additional penalty accrued as a result of the Department's delay in handling the Taxpayer's protest.

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

> A. 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; issues of negligence or nonnegligence are simply not relevant. 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. *See*, Section 7-1-13(E) NMSA 1978.

In this case, the Taxpayer failed to pay gross receipts tax due to the state. Although this failure was clearly not intentional, the fact remains that the state has been denied the use of funds to which it is legally entitled. In *In re Ranchers-Tufco Limestone Project Joint Venture*, 100 N.M. 632, 635, 674 P.2d 522, 525 (Ct. App.), *cert. denied,* 100 N.M. 505, 672 P.2d 1136 (1983), the New Mexico Court of Appeals held that administrative delay cannot serve as a defense to a taxpayer's statutory liability to the state:

> Assuming, but not deciding, that the tax collector violated Section 7-1-24(D), how does a taxpayer benefit from the violation? The statute says nothing as to the consequence of a violation. The general rule is that tardiness of public officers in the performance of statutory duties is not a defense to an action by the state to enforce a public right or to protect public interests. *State, ex rel. Dept. of Human Services v. Davis*, 99 N.M. 138, 654 P.2d 1038 (1982). The general rule is applicable in these cases unless Section 7-1-24(D) makes it inapplicable. Section 7-1-24(D) does not make the general rule inapplicable.

Based on the holding in *Ranchers-Tufco*, the Department's delay in setting a hearing on the Taxpayers' protest does not provide a basis for granting the Taxpayer's protest. I also note that Regulation 3.1.7.9 NMAC gives taxpayers the option of making principal payments on a disputed liability to stop the accrual of additional interest during the pendency of the administrative proceeding. If the taxpayer prevails on his or her protest, those payments are returned. No payments were made in this case. As a result, the Taxpayer, not the state, continued to have use of her unpaid gross receipts taxes.

Financial Hardship. Finally, the Taxpayer asks the Department to consider the fact that she has devoted most of her time to voluntary community service and has limited financial resources to pay the assessment. Unfortunately, these factors are not something the Department can consider. Department Regulation 3.1.6.14 NMAC specifically states that the Secretary "may not compromise a taxpayer's liability because of the taxpayer's inability to pay." Nor does the hearing officer have authority to relieve a taxpayer of his statutory liability for tax, penalty or interest. In *State ex rel.*

Taylor v. Johnson, 1998-NMSC-015 ¶ 022, 961 P.2d 768, 774-775, the supreme court made the following observations concerning the power of administrative agencies:

> Generally, the Legislature, not the administrative agency, declares the policy and establishes primary standards to which the agency must conform. *See State ex rel. State Park & Recreation Comm'n v. New Mexico State Authority*, 76 N.M. 1, 13, 411 P.2d 984, 993 (1966). The administrative agency's discretion may not justify altering, modifying or extending the reach of a law created by the Legislature....

The legislature has not granted the Department or its hearing officer the authority to abate or adjust tax assessments based on the financial or personal situations of individual taxpayers.

CONCLUSIONS OF LAW

1. The Taxpayer filed a timely, written protest to Assessment No. 2279823, and jurisdiction lies over the parties and the subject matter of this protest.

2. During 1995, the Taxpayer was performing services for Bright Beginnings as an independent contractor and gross receipts tax was due on those receipts.

3. There was no undue delay in the Department's assessment, which was issued within the time limitations set by the New Mexico Legislature in Section 7-1-18 NMSA 1978.

4. The Department's delay in setting a hearing on the Taxpayer's protest does not provide a legal basis for abating or reducing the Department's assessment.

5. The hearing officer does not have authority to override the provisions of New Mexico's tax laws to relieve the Taxpayer of her statutory obligation for payment of tax, penalty and interest due to the state.

For the foregoing reasons, the Taxpayer's protest IS DENIED, except for gross receipts tax, penalty and interest assessed on the $6,900 lump sum payment the Taxpayer received as a distribution from Bright Beginnings' profit-sharing plan, which the Department stipulated it would abate.

DATED October 29, 2002.