IN THE COURT OF APPEALS
OF THE STATE OF NEW MEXICO

GEA INTEGRATED COOLING TECHNOLOGY,

Appellant,

vs.

No. 30-790
Tax and Rev ADM-10-13

NEW MEXICO TAXATION AND REVENUE DEPARTMENT,

Appellee.

Appeal from the Tax Protest Hearing Office
of the New Mexico Taxation and Revenue Department

Gerald B. Richardson, Hearing Officer

REPLY BRIEF

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Introduction

NMSA 1978, § 7-1-69 (2003) was amended effective January 1, 2008, to increase the cap on penalties assessed for failure to timely report or pay a tax due from 10% to 20%. The sole issue on appeal is whether the 10% cap or the 20% cap is applicable to the penalty assessed against Appellant, where the penalty was incurred prior to the effective date of the amendment but assessed after.

ARGUMENT

I. The Amendment Affects Preexisting Rights and Obligations of the Parties, and Application to Appellant's Penalty Would Be an Unauthorized and Impermissible Retroactive Application of the Amendment.

The Hearing Officer held, and the New Mexico Taxation and Revenue Department ("Department") argues here, that the application of the increased cap to penalties incurred prior to the effective date of the amendment is not a retroactive application of the amendment. Both base their reasoning on the fact that the amount of the penalty is not calculated or assessed until the tax is assessed. (RP 6; Answer Brief at 5, 6, 11, 14-15, 18.) Specifically, they rely on the phrase in § 7-1-69(A) that states, "there shall be added to the amount assessed a penalty."

The Hearing Officer noted twice that the penalty is not imposed until after the tax is assessed. (RP 5, 6.) He then concluded that the rights and obligations of the parties arise at the moment of assessment. (RP 8.) This conclusion was essential to the Hearing Officer's holding, because it allowed him to say that the

application of the amended statute, which was in effect on the date of the assessment, did not affect rights acquired under the prior law, require new obligations, or impose new duties. If he were correct that the rights and obligations created by the penalty arise only upon the assessment of that penalty, then the existence of those rights and obligations are delayed until after the effective date of the amendment, and the Hearing Officer's application of the amendment in this case is not retroactive.

But this conclusion is wrong. Section 7-1-13 (2007) of the New Mexico Tax Administration Act imposes a duty on the taxpayer to timely file a return. Section 7-9-11 (1969) of the New Mexico Gross Receipts and Compensating Tax Act imposes a duty on the taxpayer to pay the tax due on the twenty-fifth day of the month following the month in which the taxable event occurred. If a taxpayer fails to comply with either statute, it has breached its statutory duty, and § 7-1-69 imposes a penalty for that breach. The taxpayer's obligation to pay that penalty and the state's right to that penalty exist as of the moment of the breach.

The later act of assessment, whether of the tax or the penalty, is both a procedural step in the collection process and a statement of the mathematical computation of the dollar amount involved. But the assessment does not create the obligation to report and pay the tax or to pay the penalty, or the state's right to

receive that tax and that penalty. The assessment is merely the quantification of that right, as well as a procedural step in the collection process.

If the Hearing Officer and the Department are right, and it is the assessment that creates the obligation on the part of the taxpayer, then perforce the obligation to pay the tax does not exist until the assessment is made. If there is no obligation to pay the tax until the assessment is made, then no penalty or interest can be levied for any date preceding the assessment, because no duty will have been breached and no tax owed until the assessment was made.

This is, of course, contrary to the structure of the tax, penalty, and interest statutes of the New Mexico tax codes. The state has a right to assess and collect the penalty on the first day after the taxpayer fails to comply with its reporting and payment obligations. And just as the state's right to the penalty comes into existence upon the taxpayer's failure to comply with the reporting and payment obligations, so too does the taxpayer's obligation to pay that penalty. The Department's effort to apply the amendment to alter those rights and obligations is an improper retroactive application of the amendment.

The language in § 7-1-69 providing that the penalty is assessed only after the tax is assessed, far from being support for the Department's strained effort to characterize its application of the amendment as prospective only, is simply a mathematical necessity. Since the amount of the penalty is calculated from the

amount of tax assessed, the amount of the penalty of course cannot be calculated or assessed until the amount of the tax is determined. The legislature didn't choose this process as an indication of its intent. It simply, mechanically, had no choice.

II. The Department's Position on the Amendment to the Penalty Cap Is Contradicted by Its Position on the Reduced Interest Rate under NMSA 1978, § 7-1-67 (2007).

The Hearing Officer and the Department argue that, because the specific dollar amount of the penalty cannot be known until the underlying tax is assessed, the parties' respective rights and obligations arising out of that penalty do not exist until the assessment of the tax. This, they argue, means that the application of the amended statute to penalties arising out of taxes due but unpaid before the effective date of the amendment is not retroactive.

It is puzzling, then, that the Department applies the amendment to the interest rate statute, requiring the state to charge interest at a lower rate, only to interest accruing after the effective date of the amendment, January 1, 2008. (RP 2, Hearing Officer's Finding of Fact 8.) The same argument that the Department is raising here on the application of the higher penalty would require the Department to apply the lower interest rate to all interest accruing from the date of the deficiency, when the deficiency was assessed after January 1, 2008.

Under § 7-1-67(A), interest is due from the first day that the tax is due but unpaid; under § 7-1-67(B), this interest is calculated as a stated percentage of the

unpaid tax. But since the amount of that tax is not known until it is assessed, the amount of interest due on that tax likewise cannot be known until the tax is assessed, precisely the same situation as in the calculation of the penalty. Using the Department's reasoning in the present case, the amended § 7-1-67 applies to all tax deficiencies assessed after January 1, 2008, from the date the deficiency arose.

The fact that the Department chooses not to apply its own reasoning to the lower interest rate demonstrates the fallacy of that reasoning.

III. The Plain Language of NMSA 1978, § 7-1-69 Requires the Reversal of the Hearing Officer's Application of the Higher Cap to Appellant's Penalty.

In Section II of its Answer Brief, the Department argues that a "plain reading" (Answer Brief at 18) of the "plain language" (Answer Brief at 14, 15) of § 7-1-69 requires that the higher cap be applied to penalties incurred before the effective date of the amendment.

It is instructive, in evaluating this argument, to know that the Hearing Officers of the Department's Hearing Office have addressed this precise issue in seven other published decisions. In every one of those seven decisions, authored by four different Hearing Officers, the Hearing Officers reviewed the "plain language" of § 7-1-69 and concluded that the application of the higher cap to penalties incurred before the effective date of the amendment but assessed after that date, would be an impermissible and unauthorized retroactive application of

the amendment. In re Protest of Alamo True Value Home Center, Dec. 09-02 (10/15/10; B. VanDenzen); In re Protest of Maria and Robert Cloutier, Dec. 09-05 (10/28/09; M. Ontiveros); In re Protest of Kimberly and William Flores, Dec. 10-5 (3/24/10; S. Galanter); In re Protest of Jason P. Able, Dec. 10-07 (5/27/10; B. VanDanzen); In re Protest of Christopher Martin, Dec. 10-08 (6/2/10; D. Hoxie); In re Protest of Steve Ortiz, Dec 10-09 (6/16/10; S. Galanter); and In re Protest of Rose Ann Mathews, Dec. 10-18 (10/20/10; D. Hoxie).

In an eighth published decision, the Hearing Officer noted that, when she requested that the parties submit additional analysis on the question of "whether the application of the 20% negligence penalty (in this matter) is an impermissible retroactive application of Section 7-1-69," the Department responded by voluntarily abating the additional 10% penalty assessment. In re Protest of Cadworks Home Design & Draft, Dec. 09-01 (3/30/09; S. Galanter) (Findings of Fact 37, 38).

The Department's argument that the "plain language" of § 7-1-69 supports its interpretation of the statute allowing the application of the higher cap to penalties incurred prior to its effective date is belied by the fact that every other hearing officer, in every other published decision in which this issue has been addressed, has found otherwise. In fact, the Department's interpretation of § 7-1-69 depends on a strained reading of the language of the statute, confusing the

clerical act of calculating the amount of the penalty for the imposition of the penalty itself.

The plain language of § 7-1-69 and the acknowledged restriction against retroactive application of the amendment require that the higher cap be applied only to penalties incurred after the effective date of the amendment.

Conclusion

The Hearing Officer improperly applied the amendment to § 7-1-69 retroactively to Appellant's failure to report and pay taxes that accrued prior to the effective date of the amendment. The Hearing Officer's Decision should be reversed, and the Taxation and Revenue Department ordered to reduce to 10% the penalty assessed for failure to report or pay regarding periods before January 1, 2008.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, R. Tracy Sprouls, hereby certify that on May 2, 2011, I caused a true and correct copy of Appellant's Reply Brief to be mailed to counsel for Appellee New Mexico Taxation and Revenue Department at the following address:

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