

05-1590
Audit
Signed 08/04/2006

BEFORE THE UTAH STATE TAX COMMISSION

PETITIONER,	)	ORDER	
)		
Petitioner,	)	Appeal No.	05-1590
)		
v.	)	Account No.	#####
	)	Tax Type:	10% Negligence Penalty /
AUDITING DIVISION	)		Environmental Assurance Fee
OF THE UTAH STATE	)	Tax Period:	04/01/2001 – 03/31/2004
TAX COMMISSION,)		
	)	Judge:	Chapman
Respondent.)		

Presiding:

Kerry R. Chapman, Administrative Law Judge

Appearances:

For Petitioner: PETITIONER REPRESENTATIVE, from PETITIONER
For Respondent: RESPONDENT REPRESENTATIVE 1, Assistant Attorney General
RESPONDENT REPRESENTATIVE 2, from the Auditing Division
RESPONDENT REPRESENTATIVE 3, from the Auditing Division

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for an Initial Hearing on July 19, 2006.

On October 17, 2005, Auditing Division (the “Division”) issued a Statutory Notice – Environmental Assurance Fee (“Statutory Notice”), in which it imposed additional environmental assurance fees on PETITIONER (“PETITIONER”) for the audit period April 1, 2001 through March 31, 2004. The assessment included \$\$\$\$ in additional fees, \$\$\$\$ for a 10% negligence penalty, and \$\$\$\$ in interest, for a total assessment of \$\$\$\$\$. PETITIONER agrees that it owed the additional fees and interest, and it has paid these amounts. However, it asks the Commission to abate or waive the \$\$\$\$ negligence penalty.

PETITIONER REPRESENTATIVE, a tax accountant with PETITIONER, explains that the deficiency resulted from accounting miscommunications between various divisions within the company. The

communication problems resulted in her division failing to “bill” some of the company’s locations (i.e., (X) stations) for the fee. As a result, PETITIONER’S general ledger did not show the total amount of fees associated with all of its stations, which led to the company requesting refunds of fees that were not due. PETITIONER REPRESENTATIVE explains that the discrepancy was difficult to detect because it only involved a limited number of stations. Taxpayer Services Division refunded the fees whenever PETITIONER made its requests. The erroneous refunds continued until near the end of the audit period when Auditing Division discovered the company’s error, which led to the assessment at issue.

PETITIONER REPRESENTATIVE asks the Commission to abate or waive all or a portion of the negligence penalty because PETITIONER has willingly paid the fees and interest and has taken steps to correct the problem that cause the deficiency. In a February 9, 2006 letter, PETITIONER REPRESENTATIVE specifically asked that the penalty be abated, explaining that:

In filing taxes for thirteen states plus federal excise tax for our various companies and accommodating what seems to be endless audits and auditors, it is difficult to devote the necessary time to give every account the thorough attention and sometimes extensive research it needs to keep up on probable errors. As stated above, the assessment here was due mostly to a matter of miscommunication and honest human error. There is no reason to assume fraudulent intentions as I do take pride in filing correct and timely returns and filling my responsibilities as best I can to the knowledge I have. It is for this reason that I feel the penalty should not be due and request an abatement of it.

At the hearing, PETITIONER REPRESENTATIVE explained that the company has both internal and external auditors who regularly audit the company’s accounting procedures. However, she does not know why the company’s auditors did not find an accounting error that continued for more than two years prior to the Division finding it.

The Division argues that waiver or abatement of the negligence penalty is unwarranted because the Petitioner’s internal accounting problems led to a significant deficiency that was in excess of

\$\$\$\$\$. Furthermore, the Division argues that this specific error was not a one-time event, but one that was systemic and lasted for years. The Division also proffered that the Petitioner has a history of “loose controls and little oversight” and that such management has continued beyond the audit period, which will result in future assessments. Lastly, the Division proffered that the Petitioner was assessed over \$\$\$\$ in penalties several years ago in association with a motor fuel audit deficiency. The Division also proffered that the Commission waived this motor fuel penalty as a “first-time error.” Even though the negligence penalty at issue does not relate to a motor fuel tax issue, the Division asks the Commission to consider the environmental assurance fee error for which the penalty was imposed to be a “second” error on the Petitioner’s account and not to waive the negligence penalty under the “first-time error” reasonable cause circumstance. For these reasons, the Division requests that the Commission sustain the 10% negligence penalty that it has imposed.

In response, PETITIONER REPRESENTATIVE stated that after the Auditing Division informed PETITIONER of the specific accounting problem that led to the assessment at issue, it corrected the problem. PETITIONER REPRESENTATIVE stated that its correction resulted in there being no delinquency of environmental assurance fee in the last six or seven months of the audit period.¹ Furthermore, concerning the Division’s “first-time error” argument, PETITIONER REPRESENTATIVE asks the Commission to consider its environmental assurance fee mistake, the error at issue in this matter, a separate error from the motor fuel error for which the company was previously assessed.

APPLICABLE LAW

Utah Code Ann. §19-6-410.5(4) provides that “[t]here is assessed an environmental assurance fee of 1/2 cent per gallon on the first sale or use of petroleum products in the state.” Subsection 19-6.410.5(6)

¹ The Division did not provide a complete copy of the Statutory Notice so we accept the Petitioner’s claim.

provides that the Tax Commission “is responsible for the collection of the fee and any penalties and interest imposed under this section.” Furthermore, Subsection 19-6-410.5(9)(a) provides that “[t]he penalties and interest for failure to file the form required under this section or to pay the environmental assurance fee are the same as the penalties and interest under Sections 59-1-401 and 59-1-402.”

UCA §59-1-401(5)(a)(i) provides that “if any underpayment of tax is due to negligence, the penalty is 10% of the underpayment.”

In those situations where penalty and interest have been properly imposed, the Tax Commission is granted the authority to waive, reduce, or compromise penalties and interest upon a showing of reasonable cause. UCA §59-1-401(11).

In Utah State Tax Commission Publication 17 (“Publication 17”), the Commission lists a number of circumstances that may constitute “reasonable cause” with regards to the waiver of penalties and interest. The circumstances listed include “First Time Filer” in Section J., which provides that reasonable cause may exist if “[i]t is the first return required to be filed and the taxes were filed and paid within a reasonable time[,]” and “Compliance History” in Section L., which provides that “[t]he Tax Commission will consider your recent history for payment, filing, and delinquencies in determining whether a penalty may be waived.”

DISCUSSION

At issue is the 10% negligence penalty that the Division imposed on the amounts of environmental assurance fee erroneously refunded to the Petitioner during the three-year audit period. The Division asks the Commission to sustain the negligence penalty in full, while the Petitioner asks the Commission to abate or waive all or a portion of the penalty.

The Commission must first determine if the negligence penalty was properly imposed. If the Commission determines that the negligence penalty was not properly imposed (e.g., the Petitioner's actions that led to the refunds did not rise to the level of negligence), the Commission will abate the penalty and overturn the Division's assessment.

On the other hand, if the Commission determines that the negligence penalty was properly imposed, it will not abate the penalty. Instead, it will consider whether reasonable cause exists to waive all or a portion of the penalty, pursuant to the authority provided to the Commission in Section 59-1-401(11).

I. Was the Negligence Penalty Properly Imposed? Section 19-6-410.5(9)(a) provides that the penalties for failure to pay the environmental assurance fee are the same as the penalties under Section 59-1-401. Accordingly, the Commission finds that the Division may impose a Section 59-1-401(5) negligence penalty in association with delinquent environmental assurance fees,² if the taxpayer's actions that led to the delinquency rise to the level of negligence.

In PETITIONER REPRESENTATIVE'S February 9, 2006 letter, she asks the Commission to abate the negligence penalty because PETITIONER'S actions that led to the refunds were neither intentional nor fraudulent. From the testimony proffered at the Initial Hearing, it does not appear that the Petitioner's actions were either intentional or fraudulent. However, an act does not require an element of intent or fraud in order to rise to the level of negligence. Black's Law Dictionary 930, 931 (5th ed. 1979) defines "negligence" to include the following:

Negligence is the failure to use such care as a reasonably prudent and careful person would use under similar circumstances; it is the doing of some act which a person of

² In *Jensen v. State Tax Comm.n.*, 835 P.2d 965 (Utah 1992), the Utah Supreme Court determined that the Tax Commission cannot rely on a general provision in 59-1-401 to penalize a taxpayer, but must instead find some basis in the tax chapter pertaining to the tax to which the penalty relates.

ordinary prudence would not have done under similar circumstances or failure to do what a person of ordinary prudence would have done under similar circumstances.

Given this definition, the Commission will look at the Petitioner's actions and determine if its failure to discover and correct internal accounting problems that continued for more than two years is an act that a reasonably prudent and careful business would also have committed. If the Commission concludes that a business of ordinary prudence would not have committed such an act, it will conclude that the Petitioner's failure was negligent and find that the Division properly imposed the penalty.

The Petitioner's actions consist of the following. Over a period of approximately two and one-half years, PETITIONER made numerous refund requests to Taxpayer Services Division for environmental assurance fees to which it was not entitled. The refund requests were due to two errors made in PETITIONER'S business operations. First, an accounting error occurred where the environmental assurance fees relating to a number of stations were not reflected on the company's general ledger. Second, PETITIONER REPRESENTATIVE describes in her letter that within several months of the accounting error first occurring, the company detected it and took steps to correct it. However, the correction was never made because of miscommunication between divisions within the company. Although PETITIONER employs both internal and external auditors, the accounting problem and refund requests continued for more than two years until Auditing Division discovered the error during an audit.

That a company either makes an accounting error or fails to find and correct such an error within a reasonable length of time is not necessarily a negligent act on its own. However, in this matter, PETITIONER detected the error within several months, but its attempts to correct it failed. In addition, its internal and external auditors also failed for more than two years to detect and correct the problem. The Commission does not find these actions, when considered as a whole, to be those of a reasonably careful and

prudent business. Accordingly, the Commission considers the Petitioner's actions that led to its refund requests to be negligent and finds that the Division properly imposed the negligence penalty.

II. Is there Reasonable Cause to Waive the Negligence Penalty? Section 59-1-401(11) authorizes the Commission, upon a showing of "reasonable cause," to waive all or part of a penalty that is imposed under Title 59, Chapter 1, Part 4 of the Utah Code. In Publication 17, the Commission lists a number of circumstances that may constitute "reasonable cause" for purposes of waiving a penalty. The Division argued that the Commission should not consider a "first-time error" reasonable cause argument in this matter. The Commission notes, however, that it removed the "first-time error" reasonable cause from the publication several years ago, at the same time it added the "first-time filer" and "compliance history" reasonable causes. In addition to the circumstances specifically listed, Publication 17 also provides that "[o]ther clearly supported extraordinary and unanticipated reasons for late filing or payment, which demonstrate reasonable cause and the inability to comply, may justify a waiver of the penalty."

The information available to the Commission at the Initial Hearing suggests that PETITIONER should receive a partial waiver of the negligence penalty at issue. The total amount of environmental assurance fee that the Division assessed in its Statutory Notice is \$\$\$\$\$. Although the Division convincingly argues that \$\$\$\$\$ is a significant dollar amount, further information is needed to determine whether it is a significant percentage of the Petitioner's total amount of fee obligations that it incurred during the audit period. The Petitioner asserted that the delinquency occurred over a period of approximately two and one-half years, or thirty months. The delinquency, if accrued over thirty months, would equate to approximately \$\$\$\$\$ per month. For a company as large as PETITIONER, a monthly discrepancy of \$\$\$\$\$ might not immediately alert the company of its error.³

3 The Division proffered the first page of the Statutory Notice to the Commission for review.

In addition, the Commission considers the accounting error that resulted in the delinquency to be a single error that occurred over approximately thirty monthly reporting periods. It does not consider the assessment to be the result of thirty distinguishable errors. Furthermore, the information available at the Initial Hearing would suggest that the Petitioner's compliance history, while not spotless, is relatively good. The Division proffered only one instance where the Petitioner has been assessed an audit deficiency and penalty (in that instance, for the motor fuel tax). Although the Division also stated that other discrepancies have been detected and would be assessed in the future, there is no evidence that audit assessments are forthcoming. The Commission does not consider one prior compliance error to be unreasonable for a company of the size and nature of PETITIONER. For these reasons, the Commission finds that the Petitioner's compliance history is sufficient to warrant consideration of a waiver.

Because the accounting error lasted for more than two years, however, the Commission does not find that a waiver is appropriate for the entire audit period. The Commission does not find it reasonable to waive the penalty for periods after which the Petitioner's internal and external auditors should have detected and corrected the accounting problem. For this reason, the Commission considers it reasonable to waive that portion of the penalty imposed on delinquencies that occurred during the first year of the audit period (i.e., April 1, 2001 through March 31, 2002). However, the Commission does not consider it reasonable to waive that portion of the penalty that was imposed on delinquencies that occurred during the last two years of the audit period (i.e., April 1, 2002 through March 31, 2004).

DECISION AND ORDER

Based upon the foregoing, the Commission finds the Division properly imposed the negligence penalty. Nevertheless, the Commission finds that reasonable cause exists to waive a portion of the

However, there is no information on this page to show how the amounts of PETITIONER'S monthly

Appeal No. 05-1590

penalty. The Commission orders that that portion of the penalty that relates to the assessments imposed for the periods between April 1, 2001 and March 31, 2002 be waived. The Commission sustains the remainder of the penalty. It is so ordered.

This decision does not limit a party's right to a Formal Hearing. However, this Decision and Order will become the Final Decision and Order of the Commission unless any party to this case files a written request within thirty (30) days of the date of this decision to proceed to a Formal Hearing. Such a request shall be mailed to the address listed below and must include the Petitioner's name, address, and appeal number:

Utah State Tax Commission
Appeals Division
210 North 1950 West
Salt Lake City, Utah 84134

Failure to request a Formal Hearing will preclude any further appeal rights in this matter.

DATED this _____ day of _____, 2006.

Kerry R. Chapman
Administrative Law Judge

BY ORDER OF THE UTAH STATE TAX COMMISSION.

The Commission has reviewed this case and the undersigned concur in this decision.

DATED this _____ day of _____, 2006.

Pam Hendrickson
Commission Chair

R. Bruce Johnson
Commissioner

delinquencies relate to the amounts of its total environmental assurance fee obligations.

Appeal No. 05-1590

Marc B. Johnson
Commissioner

D'Arcy Dixon Pignanelli
Commissioner

Notice: If a Formal Hearing is not requested as discussed above, failure to pay any remaining balance resulting from this order within thirty (30) days from the date of this order may result in a late payment penalty.

KRC/05-1590.int