

07-1517
Audit
Signed 08/05/2008

BEFORE THE UTAH STATE TAX COMMISSION

PETITIONER, Petitioner, v. AUDITING DIVISION OF THE UTAH STATE TAX COMMISSION, Respondent.	INITIAL HEARING ORDER Appeal No. 07-1517 Account No. ##### Tax Type: Sales Tax / Negligence Penalty Audit Period: 01/01/03 – 08/31/07 Judge: Chapman
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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 Auditing Division

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for an Initial Hearing on July 30, 2008.

The taxpayer is appealing Auditing Division's (the "Division") assessment of a 10% negligence penalty. On November 26, 2007, the Division issued a Statutory Notice – Sales and Use Tax ("Statutory Notice") to the taxpayer, in which it imposed additional tax, a 10% negligence penalty, and interest, as follows:

<u>Year</u>	<u>Tax</u>	<u>10% Neg. Penalty</u>	<u>Interest</u>	<u>Total</u>
2003	\$\$\$\$\$	\$\$\$\$\$	\$\$\$\$\$	\$\$\$\$\$

The additional tax was imposed on the taxpayer's tax-free purchases of items that it bought from out-of-state suppliers who did not charge sales tax. The taxpayer consumed these items without reporting and paying Utah use tax. During the audit period, these purchases totaled approximately \$\$\$\$\$. The taxpayer

admits that it owes the additional tax and interest, but asks the Commission to abate the negligence penalty because it does not believe that its actions were negligent.

In the Statutory Notice, the Division stated that it was imposing the negligence penalty because:

- The adjustments in this audit are for the same types of errors as determined in the previous audit dated January 30, 2003, and the amounts are significant.
- Reasonable controls to ensure proper accrual of the tax had not been instituted.
- A use tax account had been used briefly following the prior audit, but the account was closed, though the company continued to make purchases subject to use tax.

The Division asks the Commission to sustain the negligence penalty in its entirety.

APPLICABLE LAW

Utah Code Ann. §59-1-401(7)(a)(i) provides that “if any underpayment of tax is due to negligence, the penalty is 10% of the underpayment.” UCA §59-1-401(13) authorizes the Commission to waive, reduce, or compromise penalties and interest upon a showing of reasonable cause.

DISCUSSION

PETITIONER REPRESENTATIVE explains that the taxpayer is a small pharmaceutical development company that does not sell any taxable items. As a result, the only sales and use tax liability that the company must report is associated with its purchasers from out-of-state sellers who do not charge sales tax.

PETITIONER REPRESENTATIVE admits that a prior audit in 2002 found that the taxpayer had failed to remit use tax for similar purchases.¹

After the prior audit, the company opened a sales and use tax account and filed one quarterly return, specifically in January 2003 for the last quarter of 2002. Unfortunately, the receptionist who had been

¹ The Division stated that no penalties were imposed in the first audit because it was the first time the taxpayer had been made aware of its mistake.

given the task of remitting the quarterly returns mistakenly completed boxes on the return to close the account.

Because the Commission closed the account per the company's instructions, the Commission did not send the company sales and use tax returns to complete for future periods.

In addition, PETITIONER REPRESENTATIVE explains that the receptionist and the Vice-President of Finance both left the company in April 2003 and that no other employees were aware of the prior audit and of the company's use tax responsibilities. Due to these circumstances, PETITIONER REPRESENTATIVE proffers that the company's actions do not arise to the level of negligence. As a result, he asks the Commission to abate the negligence penalty.

From the testimony proffered at the Initial Hearing, it does not appear that the company'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 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 believes that a reasonably prudent and careful company would have put sufficient controls in place to ensure that it timely paid its use tax liabilities for future periods. The Commission believes that reasonable controls would have included ones to ensure that the use tax would be paid regardless of personnel changes. Because the company did not institute such controls, the Commission finds the company's actions to lack ordinary prudence and, thus, to be negligent. Accordingly, the Commission finds that the Division properly imposed the negligence penalty authorized by Section 59-1-401(7)(a)(i).

Although the Commission may waive all or part of a negligence penalty for reasonable cause in accordance with Section 59-1-401(13), the Commission does not believe that such cause exists under the circumstances. Although the receptionist made a mistake on the first use tax return she filed, there is no indication that the Vice President of Finance reviewed the return for mistakes to ensure that the new procedures were properly implemented. The controls the taxpayer put in place after receiving notice of its use tax responsibilities in the first audit were inadequate. For these reasons, the Commission finds that reasonable cause does not exist to justify a waiver of all or a portion of the penalty.

DECISION AND ORDER

Based upon the foregoing, the Commission finds the Division properly imposed the negligence penalty and that no reasonable cause exists to waive all or a portion of the penalty. Accordingly, the Commission sustains the negligence penalty and denies the taxpayer's appeal. 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 taxpayer'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 _____, 2008.

Kerry R. Chapman
Administrative Law Judge

Appeal No. 07-1517

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 _____, 2008.

Pam Hendrickson
Commission Chair

R. Bruce Johnson
Commissioner

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.

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