

## **DECISION OF MUNICIPAL TAX HEARING OFFICER**

Decision Date: June 29, 2012

Decision: MTHO # 695

***Taxpayer:***

Tax Collector: City of Tucson

Hearing Date: None

### **DISCUSSION**

#### **Introduction**

On January 31, 2012, a letter of protest was filed by ***Taxpayer*** of a tax assessment made by the City of Tucson (“City”). At the request of Taxpayer, this matter was classified as a redetermination. After submission of all memoranda by the parties, the Municipal Tax Hearing Officer (“Hearing Officer”) closed the record on June 5, 2012 and indicated a written decision would be issued on or before July 20, 2012.

### **DECISION**

On March 5, 2012, the City issued a tax assessment to Taxpayer for the period of November 2007 through August 2011. The assessment was for additional taxes in the amount of \$34,748.45, interest up through December 2011 in the amount of \$2,686.12, and penalties in the amount of \$6,949.72.

The City has been reviewing the accounts of taxpayers who are licensed for the business activities of telecommunications and public utility. The City indicated it taxed telecommunications income at a two percent rate up through June 2009. The City’s two percent public utility tax was also due on the same taxable income figure as the telecommunications income. In July 2009, the City’s public utility tax was increased to six percent. The City performed a desk audit of Taxpayer and concluded that for the period of November 2007 through March 2010 (except for August 2008), Taxpayer only reported the telecommunications income for one activity. The City determined that Taxpayer began reporting under both activities beginning in April 2010 with the exception of July 2010 through November 2010.

Taxpayer protested the entire assessment. Taxpayer asserted that tax was properly collected and paid but the tax returns were improperly filed. Taxpayer asserted that from June 2010 through November 2010, it improperly filed all utility and communications tax as communications tax. Taxpayer noted that it relied on a third party tax software vendor to provide Taxpayer with tax policies.

The City noted that the under reported amounts in the assessment were based on a comparison of the taxable amounts filed on the returns and the amounts that should have been reported as calculated on the 'Taxable Income' work paper. The City indicated that on the sheet named 'Taxable Income', a comparison was made of the taxable utility, telecommunications, and public utility amounts reported in each month. The City utilized the largest taxable income reported for each month as the adjusted actual taxable income for both the telecommunications and the public utility taxable income for each month since the taxable income should be identical for each of the two activities. The City requested Taxpayer provide actual records used to 'back into' taxable income. Taxpayer failed to provide actual income records. The City asserted that in the absence of records of taxable income, the City is authorized to utilize a reasonable method of estimating the correct taxable income pursuant to City Code Section 545(b) ("Section 545(b)"). After review of Taxpayer's protest, the City agreed to make adjustments for the months of July 2008, July 2009, and July 2010 through November 2010 based on the inconsistency of the taxable amounts reported. The City's proposed adjustments would reduce the tax due from \$34,748.45 to \$18,235.21.

In response to the City's proposed adjustments, Taxpayer provided further documents which it believed demonstrated no additional taxes were due. The City reviewed the additional documentation and concluded Taxpayer's did not demonstrate that the proper taxable income was reported. The City requested its proposed adjusted assessment be upheld since Taxpayer has still not provided any income documentation to show the City's work papers are incorrect. The City noted that under the City's proposed adjustments, additional tax is due for the periods of November 2007 through March 2010 with the exception of July 2008 and a very small amount in August 2008.

During the review period, Taxpayer was a public utility providing telecommunication services to consumers within the City. Section 1000 imposes a tax upon the gross income of persons on account of their public utility business activities. Section 1007 imposes a tax on the gross income on providing telecommunication services pursuant to Section 1007. Taxpayer's gross income was taxable pursuant to Sections 1000 and 1007. City Code Section 350 ("Section 350") provides that "It shall be the duty of every person subject to the tax imposed by this Chapter to keep and preserve suitable records and such other accounts as may be necessary to determine the amount of tax for which he is liable under this Chapter." The City requested specific records from Taxpayer and they were not provided. As a result, the City was authorized pursuant to Section 545(b) to make an estimate made on a reasonable basis. Section 545(b) provides that "It is the responsibility of the taxpayer to prove that the Tax Collector's estimate is not reasonable and correct, by providing sufficient documentation of the type and form required by this Chapter or satisfactory to the Tax Collector." In this case, it was proper for the City to make an estimate since Taxpayer failed to provide documents requested by the City. It was also proper for the City to revise the assessment based on additional documentation provided by Taxpayer. We conclude the City's estimate was made on a reasonable basis and that Taxpayer has failed to provide documents to prove the estimate was not reasonable.

The City was authorized to assess penalties for late payment of taxes pursuant to City Code Section 540 (“Section 540”). The City also assessed Taxpayer for a negligence penalty pursuant to Section 540. “Negligence” is defined in Section 540 as characterized chiefly by inadvertence, thoughtlessness, inattention, or the like, rather than an “honest mistake”. We conclude that Taxpayer’s failure to timely pay all of its taxes was due to an honest mistake that was caused by a change in the City Code and reliance on a third party vendor. As a result, any penalties for negligence are hereby waived. Based on all the above, we conclude the Taxpayer’s January 31, 2012 protest is hereby partially denied, and partially approved, consistent with the Discussion, Findings, and Conclusions, herein.

### **FINDINGS OF FACT**

1. On March 5, 2012, Taxpayer filed a protest of a tax assessment made by the City.
2. At the request of Taxpayer, this matter was classified as a redetermination.
3. Taxpayer was assessed taxes in the amount of \$34,748.45, penalties in the amount of \$6,949.72, interest up through December 2011 in the amount of \$2,686.12.
4. The City taxed telecommunications income at a two percent rate up through June 2009.
5. The City’s two percent public utility tax was also due on the same taxable income figure as the telecommunications income.
6. In July 2009, the City’s public utility tax was increased to six percent.
7. The City has been reviewing the accounts of taxpayers who are licensed for the business activities of telecommunications and public utility.
8. The City performed a desk audit of Taxpayer and concluded that for the period of November 2007 through March 2010 (except for August 2008), Taxpayer only reported the telecommunications income for one activity.
9. The City determined that Taxpayer began reporting under both activities beginning in April 2010 with the exception of July 2010 through November 2010.

10. The City noted that the under reported amounts in the assessment were based on a comparison of the taxable amounts filed on the returns and the amounts that should have been reported as calculated on the "Taxable Income" work paper.
11. The City requested Taxpayer provide actual income records as opposed to tax collected records used to "back into" taxable income.
12. Taxpayer failed to provide actual income records.
13. After review of Taxpayer's protest, the City agreed to make adjustments for the months of July 2008, July 2009, and July 2010 through November 2010 based on the inconsistency of the taxable amounts reported.
14. Taxpayer relied on a third party tax software vendor to provide Taxpayer with tax policies.

#### **CONCLUSIONS OF LAW**

1. Pursuant to ARS Section 42-6056, the Municipal Tax Hearing Officer is to hear all reviews of petitions for hearing or redetermination under the Model City Tax Code.
2. During the review period, Taxpayer was in the public utility business providing telecommunications services to consumers within the City.
3. Section 1000 imposes a tax on the gross income of persons on account of their public utility business activities.
4. Section 1007 imposes a tax on the gross income on providing telecommunication services within the City.
5. Taxpayer's gross income was taxable pursuant to Section's 1000 and 1007.
6. Section 350 imposes a duty on Taxpayer to keep and maintain suitable records to determine the correct tax for which it is liable.
7. Taxpayer failed to provide suitable records requested by the City.
8. The City was authorized pursuant to Section 545(b) to make a reasonable estimate.

9. Taxpayer failed to prove the City's estimate was not reasonable.
10. The City was authorized to impose penalties for failure to timely pay taxes pursuant to Section 540.
11. The City assessed Taxpayer for a negligence penalty pursuant to Section 540.
12. Taxpayer's failure to timely pay all of its taxes in a timely manner was due to an honest mistake.
13. Any penalties for negligence are hereby waived.
14. Based on all the above, Taxpayer's protest should be partly granted, partly denied, consistent with the Discussion, Conclusions, and Findings, herein.
15. The parties have timely rights of appeal to the Arizona Tax Court pursuant to Model City Tax Code Section-575.

### **ORDER**

It is therefore ordered that the March 5, 2012 protest by *Taxpayer* of a tax assessment made by the City of Tucson is hereby partly denied and partly granted, consistent with the Discussion, Findings, and Conclusions, herein.

It is further ordered that the City of Tucson shall revise its assessment consistent with its March 5, 2012 letter.

It is further ordered that all negligence penalties in this matter are hereby waived.

It is further ordered that this Decision is effective immediately.

Municipal Tax Hearing Officer