

**Dana and Janice Rood**

**v.**

**Department of Revenue Administration**

**Docket No.: 17347-97BP**

**DECISION**

The "Taxpayer"<sup>1</sup> appeals, pursuant to RSA 21-J:28-b (Supp. 1997), the department of revenue administration's (DRA) assessment of an RSA Chapter 77-A business profits tax (BPT) for tax years 1992 and 1993. The main issue is, under RSA 77-A:4 III (a) (Supp. 1992), what is the proper deduction for compensation for the Taxpayer's personal services.

The burden is on the Taxpayer to show the reasonableness of the deduction. See RSA 77-A:4 III (a). The Taxpayer failed to carry this burden.

Therefore, the board upholds the DRA's determination of the compensation deduction, upholds the DRA's BPT assessment (with interest) and upholds the DRA's assessment of the RSA 21-J:33 penalty.

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<sup>1</sup> This decision will refer to the "Taxpayer" singularly, to mean Dana Rood. While the appeal was filed in both Dana Rood's and Janice Rood's names, the real estate involved is owned solely by Dana Rood, Dana Rood provided services to the manufactured-housing park whereas Janice Rood did not, and some of the tax forms have Janice Rood's name and signature blackened out. If the board's order results in a collection problem, the Taxpayer and the DRA may certainly try to clarify who is liable for the ordered taxes, interest and penalties.

The board held two hearings on this appeal. First, the board held a hearing on the BPT liability issue. This hearing was held on two days -- May 27, 1998, and June 2, 1998. The board then issued a draft decision and held a hearing solely on the issue of what penalties should be imposed. A separate

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hearing was held on August 31, 1998, to address the penalty issues. This decision addresses both issues.

### **Facts**

The material facts were not in dispute. Therefore, except as modified below, the board adopts the facts stated in the DRA's hearing memorandum.

Briefly stated, the Taxpayer owns and operates Concord Terrace, a mobile-home park in Concord with 139 lots. The Taxpayer is also the sole shareholder in Lakewood Development Corporation (Lakewood), which owns and operates mobile-home parks in Belmont and Canaan, New Hampshire.

The Taxpayer hired Stephen C. Robinson, CPA (Robinson) to prepare the 1992 and 1993 BPT returns. As detailed below, the Taxpayer on the 1992 BPT return treated all of the Concord Terrace income (remaining after expenses) as compensation, and on the 1993 BPT return, the Taxpayer treated virtually all of the income (remaining after expenses) as compensation. Therefore, the Taxpayer, in 1992, filed a BPT return without any BPT liability, and in 1993, filed a BPT return with minimal BPT liability, which was offset by the business enterprise tax (BET) credit. The DRA audited the Taxpayer's returns, revised the compensation deduction and assessed a BPT liability. The Taxpayer then appealed that determination through the DRA's redetermination process, and when the DRA ultimately ruled against him, the Taxpayer appealed to this

board.

**Analysis**

In determining taxable business profits, RSA 77-A:4 III (a) allows certain adjustments to gross business profits. "Generally speaking, these different adjustments are intended to establish a uniform tax base for BPT purposes for all business organizations." Dubrow, *The Deductibility of Compensation Payments to Owner Employees*, 33 New Hampshire Bar Journal 285 (March 1992). The specific adjustment at issue in this case is the RSA 77-A:4 III compensation deduction.

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RSA 77-A:4 III provides:

- III. (a) In the case of a proprietorship or partnership, a deduction equal to a fair and reasonable compensation for the personal services of the proprietor or partners actually devoting time and effort in the operation of the business organization. The purpose of this paragraph is to permit deduction from gross business profits of a proprietorship or partnership only of such amounts as are fairly attributable to the personal services of the proprietor or partners who are natural persons, but not to permit deduction of any amounts as are fairly attributable to a return on business assets or the labor of non-owner employees of the business organization. The burden shall be upon the business organization filing the return to demonstrate the reasonableness of a deduction claimed under this paragraph, by a preponderance of the evidence.
- In considering the reasonableness of a deduction claimed under this paragraph, the commissioner shall consider the claimed deduction in light of compensation for personal services of employees in positions requiring similar responsibility, devotion of time, education and experience in business organizations of similar size, volume and complexity. In addition, the commissioner shall take into account the value to the business organization of the labor of its non-owner employees, and the use of the business assets of the business organization and any other factor which may reasonably assist the commissioner in making a determination as to the reasonableness of the claimed deduction.

(b) The amount of any deduction claimed under subparagraph (a) shall not exceed the amount reported as earned income from the activities of the business organization as reflected on the federal income tax returns of the proprietor or partner rendering such personal services, but may also include an amount not to exceed net rental income as compensation for operating rental property, and an amount not to exceed 15 percent of the gross selling price as commissions on the sale of business assets. Provided, however, a minimum deduction of \$6,000 shall be allowed on account of the proprietor or each partner who is a natural person actually devoting time and effort in the operation of the business organization.

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In addition to the statutory language, the DRA Rev. 303.03 sheds further light on this issue.

**Rev. 303.03 Compensation for Personal Services of Proprietor or Partner.**

- (a)  
Compensation shall only be available to a proprietor or partner who is a natural person and who actually renders personal services to the business organization.
- (b) Compensation shall only be allowed for amounts which are reasonable pursuant to RSA 77-A:4 III (a) and not in excess of the maximum deduction allowable to the proprietor or partner actually rendering personal services to the business organization as determined in Rev. 303.03 (d).
- (c) Each proprietor or partner actually rendering personal services to the

business organization shall be allowed a minimum deduction of \$6,000.

(d) In determining the maximum deduction allowable under RSA 77-A:4 for the proprietor or partner's compensation, the proprietor or partner shall utilize the sum of the following amounts included in their federal income tax schedules:

- (1) Net profit or loss from Federal Form 1040, Schedule C.
  - (2) Income or loss from rental properties from Federal Form 1040, Schedule E.
  - (3) Net farm profit or loss from Federal Form 1040, Schedule F.
  - (4) 15 percent of the actual sales price as shown on Federal Form 4797 or 6252 for the sale of business assets provided the proprietor or partner acted as the broker or agent and no other broker or agent was involved in the sale of the property.
  - (5) In instances where the partner or proprietor act as a co-broker, the maximum deduction shall be the difference between the 15 percent of the actual sales price and the amounts paid to other brokers or agents.
  - (6) Ordinary income or loss from trade or business activities from Federal Form 1065, Schedule K-1.
  - (7) Guaranteed payments to partner from Federal Form 1065, Schedule K-1.
  - (8) Income or loss from activities in the regular trade or business of the partnership that are specifically allocated to the individual partner.
- (e) In determining the reasonableness of the compensation deduction the proprietor or partner shall maintain adequate records to demonstrate the activities performed by the individual and the methods used to determine the rate of compensation for such activities.

(f) A business organization may utilize comparative compensation data from business organizations of similar size, volume and complexity from industry statistics or from publications such as the most current editions of American Almanac of Jobs and Salaries, or New Hampshire Wages and Benefits, as a reference point. However, nothing in this rule shall prohibit the department from using such comparative data to determine the reasonableness of the deduction taken.

Source: Doc. #5355, eff. 3-16-92.

The Taxpayer reported the following on his Schedule E federal tax

return, which was used as the basis for the BPT return.

Taxpayer's Calculations

	1992	1993
Total Rents, etc.	\$389,536	\$400,794
Total Expenses	- <u>\$242,338</u>	- <u>\$292,245</u>
Net Income	\$147,198	\$108,549
BPT Compensation Deduction	- <u>\$147,198</u>	- <u>\$102,649</u>
Taxable Business Profits	\$ 0	\$ 5,900
BPT Tax	\$ 0	\$ 0 (due to BET credit)

The DRA recalculated the Taxpayer's liability as follows.

DRA's Calculations

	1992	1993
Net Income	\$147,198	\$108,549
Compensation Deduction	- <u>\$ 76,804</u>	- <u>\$ 76,804</u>
Taxable Business Profits	\$ 70,394	\$ 31,745
BPT	\$ 5,632 (8%) (plus interest and penalties)	\$ 2,381 (7.5%) \$ 378 (BET credit) <u>\$ 65 (paid)</u> \$ 1,938 (plus interest and penalties)

Based on the reasons below, the board upholds the DRA's determination of the BPT liability.

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**Taxpayer's Arguments**

The Taxpayer argued his compensation deductions were appropriate for the following reasons.

1) RSA 77-A:4 III (b) allows a compensation deduction equal to the net rental income, and therefore, the Taxpayer was correct to deduct the net rental income as compensation.

2) The Taxpayer performed all work necessary to operate Concord Terrace, and there were no other employees at Concord Terrace.

3) All of the net income earned at Concord Terrace was attributable to the Taxpayer's personal services and, therefore, were properly deducted as compensation. Any return on the real estate or other Concord Terrace assets would be received upon the sale of Concord Terrace.

4) The compensation deduction taken by the Taxpayer was reasonable based on the Certified Property Manager Profile and Compensation Study, (1993 rev. ed.) (hereinafter "the CPM Study").

5) The DRA's determination of compensation undervalued the Taxpayer's personal service to Concord Terrace.

**Board's Response to Taxpayer's Arguments**

The board, with paragraph numbers corresponding to the Taxpayer's arguments above, responds to the Taxpayer's arguments as follows.

1) The real crux of the Taxpayer's case is the Taxpayer's

interpretation of RSA 77-A:4 III (b). The Taxpayer asserted the statute authorizes a compensation deduction equal to Concord Terrace's total net rental income. Robinson, the Taxpayer's CPA, stated this was his reading of the statute. Robinson testified at the initial hearing that he took no steps to determine whether his interpretation of RSA 77-A:4 III (b) was correct. He did not check with an attorney, and he did not check with the DRA. Unfortunately for the Taxpayer, Robinson also stated that he did not read Rev. 303.03, quoted above, which certainly gives clarity to the statute.

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At the second hearing (August 31, 1998), Robinson stated that he had spoken with an attorney about this issue generally (i.e., not specific to the Taxpayer's situation) and that he had read Rev. 303.03.

Based on the testimony and the board's observations of Robinson's testimony and arguments (Mr. Robinson acted both as a witness and advocate at the first hearing), the board finds Robinson was not reasonably diligent in researching this issue and was not reasonable in interpreting RSA 77-A:4 III (b). Robinson's argument flies in the face of the purpose of the BPT, the purpose of the compensation deduction and the overriding standard that the compensation must be reasonable. To the extent Robinson viewed the issue differently, his efforts to review his conclusion were inadequate. Certainly, the more questionable (or aggressive) a position, the more research the preparer should perform.

2) The Taxpayer argued that all of the net income was deductible as reasonable compensation because the Taxpayer performed all services to operate Concord Terrace and because Concord Terrace had no other employees. This

argument is without merit for two reasons. First, the statement itself is wrong because the Taxpayer admitted at the hearing that a bookkeeper kept Concord Terrace's books, but the bookkeeper's salary was treated as a charge solely against the Taxpayer's other mobile-home parks (Lakewood).

Second, and most importantly, while the Taxpayer was Concord Terrace's principal worker, he did not present any documents or other supportable basis for the number of hours worked or the amount of compensation claimed for the specific duties performed. (The Taxpayer's discussion concerning the CPM Study will be discussed below.) RSA 77-A:4 III (a) places the burden on the Taxpayer to show that the compensation deduction was reasonable. It is not enough, as the Taxpayer tried to do here, to simply have the Taxpayer state that the compensation deduction was reasonable. Rather, the statute requires that the compensation deduction be supported and justified by the Taxpayer, which was not done in this case.

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The DRA's rules follow the statute and Rev. 303.03 (e) specifically requires that the proprietor maintain records to demonstrate the activities performed and the methods used to determine the rate of compensation for such activities. The Taxpayer did not present any such supporting information or documents. All the Taxpayer did was testify that he worked 3,400 hours per year, which equates to \$42.00 per hour in 1992 and \$29.33 per hour for 1993. Assuming the Taxpayer took two weeks vacation a year, this would mean he worked approximately 70 hours per week at Concord Terrace. The board finds no support for the Taxpayer's assertion that he worked 70 hours per week or that the rate for his services was worth \$42.00 per hour or \$29.00 per hour to

Concord Terrace. The reasons for this conclusion are as follows:

a) the individual lot owners maintain their own lots, leaving the Taxpayer with only common-area maintenance duties;

b) the Taxpayer did not perform bookkeeping functions because the Taxpayer had a bookkeeper at Lakewood that performed all bookkeeping functions for Concord Terrace; and

c) the Taxpayer had several other activities that brought into question the asserted number of hours worked at Concord Terrace, including his work at Lakewood, some limited consulting work, his legislative work on behalf of mobile-home parks and his coaching duties.

In addition to these individual reasons, the board has serious questions about the Taxpayer's credibility on the issue of the number of hours worked and on the amount of compensation for those hours. It was clear that when the BPT return was filled out, neither the Taxpayer nor his accountant, Robinson, performed any analysis to determine what was a reasonable compensation deduction. Rather, when completing the return the Taxpayer and Robinson simply concluded that all of the net income should be attributable to personal services. All of the subsequent attempts to justify the reasonable compensation were simply created to defend the deduction once the DRA questioned it.

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Another factor that weighs strongly against the Taxpayer's claim is his treatment of the Concord Terrace income on his federal tax returns. According to the DRA, the Taxpayer treated the Concord Terrace income (total income less expenses) as rental income, and therefore, he did not report this income as

earned income on his federal tax returns. This means the Taxpayer did not pay federal self-employment tax on the income he now claims was due to his personal services. Audit Division Response to Petition, pg. 1. The board finds this to be particularly disturbing. The Taxpayer and Robinson have argued before this board and before the DRA that all of the income was for personal services, yet on the federal returns they treat it as rental income and thereby avoided paying the self-employment tax.

At the August 31, 1998 hearing, Robinson asserted that it was reasonable to treat the income differently on the state and federal returns. Robinson then provided the board with IRS Revenue Ruling 83-139, 1983-2 CB150, IRC Sec(s) 1402.

The board, nonetheless, remains concerned. If the Taxpayer's treatment of the income was correct on the federal returns -- not earned income -- then why should the exact same income be for personal services on the state return?

Either way, this is a concern that is not essential to the board's conclusion. Despite the Taxpayer's total lack of support for the numbers used, the DRA, based on The American Almanac of Jobs and Salaries, (1990-91 ed.), assumed the Taxpayer worked 2,800 hours a year with a salary of \$61,443 and an additional 25% for other benefits, resulting in a \$76,804 deduction for compensation. While the board certainly has questions about whether all of the activities performed by the Taxpayer were CEO-type activities for which CEO dollars should be paid, the board finds the DRA made a reasonable attempt to ascertain a proper compensation deduction. Furthermore, the DRA looked at the compensation paid at Lakewood, and the DRA concluded the \$76,804

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compensation deduction was consistent with the compensation paid at Lakewood.<sup>2</sup>

3) The Taxpayer's second argument is equally without merit. The Taxpayer argued that all income that was earned by Concord Terrace was attributable to his personal services. This is a bogus argument that only warrants brief discussion. Concord Terrace is not a personal-service business. It is a mobile-home park. The residents pay rent for use of a specific site, i.e., they pay for the right to occupy a specific piece of real estate and for the amenities associated with the park. Because the business is real-estate based, certainly a significant portion of the income stream is related to return from the real estate and not just compensation for the personal services of maintaining the real estate. Therefore, to attribute all of the income to the Taxpayer's personal service is absurd and again demonstrates that the Taxpayer and Robinson were not attempting to reasonably comply with the law but were attempting to avoid taxation by whatever means possible. RSA 77-A:4 III (a) states: "The purpose of this paragraph is to permit deduction from gross business profits of a proprietorship or partnership only of such amounts as are fairly attributable to the personal services of the proprietor or partners who are natural persons, but not to permit deduction of any amounts as are fairly attributable to a return on business assets or the labor of non-owner employees of the business organization." There is no reasonable way to interpret the statute to reach the result proffered by the Taxpayer without violating the specific statutory purpose just enunciated.

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<sup>2</sup> The DRA's discussion concerning how it calculated the compensation can be found in the Audit Division Response to Petition (August 5, 1996), which can be found at Exhibit 3 of the Taxpayer's yellow bound booklet that was filed with the appeal on March 13, 1998.

4) The Taxpayer also argued that the compensation deduction was reasonable based on the CPM Study. Initially, we again point out that this is another back-pedaling argument. The Taxpayer did not review the CPM Study

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when filling out his BPT returns. Rather, Robinson admitted that he discovered the CPM Study while preparing to challenge the DRA's determination. Independent of this, the board still declines to rely upon the CPM Study for several reasons, including the following.

a) The Taxpayer is not a certified property manager. The whole basis of the CPM Study is that the individuals and salaries studied and presented were for people who hold the certification as a property manager. The Taxpayer does not hold such a designation, and therefore, the study does not apply to the Taxpayer.

b) The Taxpayer failed to show how the CPM Study accurately reflects the compensation due in his specific business, especially considering the type and size of business (139-site mobile-home park) and the specific income generated thereby.

c) The Taxpayer performed services at Concord Terrace that cannot be characterized as CEO activities, such as actually performing common-area maintenance. Such activities could have been hired out for substantially less than what one would pay a CEO.

d) The board reads RSA 77-A:4 III as only allowing a deduction based on the type of work performed. In other words, what would it cost to hire someone to perform the task. During the hearing, the Taxpayer was asked if he would pay someone \$147,198 or \$108,549 to operate the park. The Taxpayer

admitted he would not. This goes to the very heart of this case. The compensation deduction must be based on what the market would pay for the services rendered.

5) The Taxpayer, failing to make any reasonable support for its compensation deduction, attacked the DRA's calculation as undervaluing the Taxpayer's personal services. Initially, as stated above, the statute and the rule place the burden on the Taxpayer, not the DRA, to demonstrate what is the appropriate compensation deduction. The DRA took reasonable steps to calculate a reasonable compensation deduction. The board finds no better

evidence than the DRA's upon which a BPT tax could be calculated.

The board finds this Taxpayer argument to be without merit for the following reasons.

a) As discussed below, the purpose of the compensation deduction is to allow a deduction for personal services but not to allow a deduction for income generated by other business assets. To accept the Taxpayer's interpretation and to allow a deduction of all income generated by a real-estate based entity would fly in the face of the statute. Clearly, income is generated by other assets, namely the land and all the park improvements. It is not all attributable to the Taxpayer's personal services.

b) When RSA 77-A:4 III is read in its entirety and is read consistent with the statutory purpose of this section and the BPT chapter, it is clear that paragraph (a) of RSA 77-A:4 III only allows a reasonable compensation deduction, and paragraph (b) simply establishes the maximum deduction allowed under the law. To conclude otherwise would, again, require ignoring the specific statutory purpose and the entire BPT taxing scheme. This statutory interpretation is also supported by Rev. 303.03. This rule again reiterates that reasonable compensation is the standard but such reasonable compensation cannot be in excess of the maximum deductions stated in paragraph (b). See Rev. 303.03 (b). In summary, the board finds no basis to overrule the DRA's determination.

### **Penalties**

The board held a hearing to consider what penalties should be ordered. Board's July 23, 1998 order. After receiving the parties' arguments and evidence, the board orally informed the parties that the board would not order

penalties under RSA 21-J:33-a or RSA 21-J:33-b. The board concluded the penalties should not be ordered given the various legal and factual issues presented by the parties. The board understands that Robinson would prefer a statement approving his handling of this matter. We decline to make such an alternative ruling.

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The only remaining penalty is the RSA 21-J:33 I 10% failure to pay penalty (the Penalty). The DRA assessed this Penalty, and the Taxpayer appealed this determination. As stated in Appeal of Steele Hill Development, Inc., 121 N.H. 881, 885 (1981), the Taxpayer has the burden to show the DRA erred in imposing the Penalty. We find the Taxpayer failed to carry his burden.

RSA 21-J:33 I states:

**21-J:33 Penalties for Failure to Pay.** In addition to amounts due under this subdivision, penalties shall be imposed for failure to pay taxes when, and as, due as follows:

- I. If the failure to pay is due to willful neglect or intentional disregard of laws or rules, but without intent to defraud, the penalty shall be equal to 10 percent of the amount of the nonpayment or underpayment.

The DRA has no rules on this penalty.

The Penalty is due if:

- 1) the Taxpayer fails to pay or underpays a tax; and
- 2) the failure was to "due to willful neglect or intentional disregard of laws or rules."

There is no question that the Taxpayer failed to pay the BPT when due. The only question is whether that failure was due to willful neglect or

intentional disregard of laws or rules.

In deciding this question, we view the Taxpayer's and Robinson's actions together. The Taxpayer cannot avoid his responsibility by pointing to Robinson's erroneous advice. The Taxpayer has an independent duty to take reasonable steps to ensure returns are properly completed. Any reasonable person would know the returns were erroneous. Furthermore, even if the Taxpayer's reliance on Robinson's advice was reasonable, the Taxpayer is still responsible for Robinson's advice. As the board stated in B-Jac Investments v. Department of Revenue Administration, BTLA docket no.: 5592-88 (July 30, 1998), taxpayers are bound by their accountant's failures. See also Tessier v. Blood, 122 N.H.435 (1982) (attorney's neglect imputed to client).

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The terms "wilful neglect" and "intentional disregard" are not defined in RSA 21-J:33 I, and the DRA has no rule on RSA 21-J:33 I.

- Rev. 310.02, however, includes the same standard and states:
- (2) A tax preparer shall be deemed to have been wilfully negligent or have intentionally disregarded a statute, a rule, guidance in Information Releases or tax return instructions unless the preparer can provide evidence that one of following applies:
    - a. The return preparer had substantial authority as provided in Rev 310.01(d) for the tax treatment of the item; or
    - b. The return preparer exercised due care in an effort to apply the statute and rules to the information given to the preparer by the business organization unless the preparer knew or should have recognized that such information was incorrect or incomplete.

This rule is helpful but only advisory. If this is the standard, we find the Taxpayer lacked "substantial authority" for his position, and we find

the Taxpayer failed to exercise due care in preparing the returns. The Taxpayer wanted to avoid BPT liability, and this goal clouded any reasonable effort to properly analyze the tax laws and rules.

The board also reviewed New Hampshire caselaw for assistance. The phrases "wilful neglect" and "intentional disregard" are not clearly defined by caselaw. Ives v. Manchester Subaru, Inc., 126 NH 796, 801 (1985), states: A willful act is a voluntary act committed with an intent to cause its results. Black's Law Dictionary at 1434 (rev. 5th ed. 1979). It is not, by contrast, an accident or an act committed on the basis of a mistake of fact."

Further, we reviewed a legal dictionary to obtain some guidance on the terms at issue. Black's Law Dictionary at 1600 (6th ed. 1990), defines "wilful neglect" as "[t]he intentional disregard of a plain or manifest duty, in the performance of which the public \*\*\* has an interest. Wilful neglect suggests intentional, conscious, or known negligence -- a knowing or intentional mistake." Black's, at 810, defines "intent" as "a state of mind in which a person seeks to accomplish a given result through a course of action." Black's, at 810, defines "intentionally" as doing "something purposely, and not accidentally." Black's at 472, defines "disregard"

as "[t]o treat as unworthy of regard or notice; to take no notice of; to leave out of consideration; to ignore; to overlook; to fail to observe."

Based on the above review, willful neglect occurs when a person voluntarily decides to not act reasonably in analyzing the law and/or applying the law to the specific BPT issue. Intentional disregard occurs when a person purposefully ignores a statute or a rule. Under both standards, the facts demonstrate the Taxpayer and Robinson, individually and collectively, acted with wilful neglect and intentional disregard concerning the BPT statute and the DRA BPT rules.

The board finds the Taxpayer has not shown his actions were anything other than "due to wilful neglect or intentional disregard of law of rules." The Taxpayer's execution of the BPT returns shows wilful neglect and/or intentional disregard. This was borne out by both the Taxpayer's testimony and Robinson's testimony. They lacked any reasonable authority for their positions. Robinson's attitude was cavalier about his responsibility to take steps to reasonably interpret the BPT compensation deduction provision. Robinson, in his August 31, 1998 testimony, stated he had read the applicable rules and had spoken to an attorney, not in reference to the Taxpayer's return, but on the issue generally. If Robinson had read the BPT statute as a whole and had read the DRA's rules, especially Rev. 303.03, and if he had thought or consulted with others about a reasonable way to read RSA 77-A:4 III, he would not have completed the Taxpayer's BPT returns as he did.

We find the Taxpayer and Robinson had one goal -- to find a way to avoid BPT liability regardless of the statutes and rules. Their actions in completing the return and their arguments to this board presented no

legitimate bases to conclude otherwise. Their actions warrant imposition of the Penalty.

One closing note. The Taxpayer argued that the returns adequately revealed the Taxpayer's position, and thus, the penalty should not be imposed.

See RSA 21-J:33-a IV (b) (taxpayer can avoid the RSA 21-J:33-a IV penalty by disclosing tax treatment on return). This is not true and is another example of the Taxpayer's mishandling and groundless way this was handled. The BPT returns in no way indicated that there was any possible issue about the deduction. The Taxpayer merely completed the return as if there was no issue.

The Taxpayer should have fully described the premise for no tax liability in a statement attached with the return if the Taxpayer was indeed certain the basis of the return was correct.

**Findings of Fact and Rulings of Law**

The board attaches a copy of the requests for findings of fact and rulings of law submitted by the DRA with the responses handwritten in the margin because the numbering was inconsistent on page two, and the board wants to make sure its responses are clear to the parties.

Taxpayer

1. Granted.
2. Granted.
3. Neither granted nor denied.
4. Granted.
5. Denied, Robinson did not state that he presented this return issue to an attorney.
6. Denied.
7. Neither granted nor denied.
8. Granted.

9. Neither granted nor denied.

10. Granted.

11. Granted.

12. Granted.

13. Granted.
14. Neither granted nor denied.
15. Denied.
16. Denied.
17. Denied.
18. Neither granted nor denied.
19. Granted.
20. Denied.
21. Neither granted nor denied.
22. Neither granted nor denied.
23. Neither granted nor denied.
24. Neither granted nor denied.
25. Neither granted nor denied.

**DRA's June 16, 1998 Rehearing Motion**

The DRA filed a rehearing motion to the board's May 27, 1998 order that denied the DRA's Motion to Limit the Record Before the Board. Because the board has sustained the DRA's BPT determination, the board finds the rehearing motion to be moot, and therefore, the board denies the rehearing motion as moot.

**Rehearing and Appeal Procedure**

A motion for rehearing, reconsideration or clarification (collectively "rehearing motion") of this decision must be filed within thirty (30) days of the clerk's date below, not the date this decision is received. RSA 541:3; TAX 201.37. The rehearing motion must state with specificity all of the reasons supporting the request. RSA 541:4; TAX 201.37(b). A rehearing motion

is granted only if the moving party establishes: 1) the decision needs clarification; or 2) based on the evidence and arguments submitted to the board, the board's decision was erroneous in fact or in law. Thus, new evidence and new arguments are only allowed in very limited circumstances as

stated in board rule TAX 201.37(e). Filing a rehearing motion is a prerequisite for appealing to the supreme court, and the grounds on appeal are limited to those stated in the rehearing motion. RSA 541:6. Generally, if the board denies the rehearing motion, an appeal to the supreme court must be filed within thirty (30) days of the date on the board's denial.

SO ORDERED.

BOARD OF TAX AND LAND APPEALS

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Paul B. Franklin, Chairman

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Ignatius MacLellan, Esq., Member

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Michele E. LeBrun, Member

**Certification**

I hereby certify a copy of the foregoing decision has been mailed this date, postage prepaid, to Stephen C. Robinson, Agent for Dana and Janice Rood, Taxpayers; David W. Rayment, Esq., Attorney for Taxpayers; and John F. Hayes, Esq., Counsel for the Department of Revenue Administration.

Date: September 23, 1998

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Valerie B. Lanigan, Clerk

**Dana and Janice Rood**

**v.**

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**ORDER**

This order addresses the issue of what penalties should be assessed in this case. This issue was not fully heard, and thus, the board has scheduled a hearing for August 31, 1998, at 1:00 p.m. on this issue. (Separate hearing notice sent with this order.)

Attached to this order is the board's draft decision on the tax liability questions. The board has denied the "Taxpayer's" appeal and has upheld the "DRA's" "BPT" determination. As the draft decision demonstrates, the issue of appropriate penalties must be addressed.

The board will restrict the hearing to the penalty issues. The board will not accept any additional evidence or arguments on the BPT liability questions. Once the board has held this hearing and has issued a decision, parties may then file their rehearing motions to all issues.

Given the underlying facts, the statutes provide three possible penalties:

- 1) RSA 21-J:33 "Penalties for Failure to Pay" (The board assumes the penalty would be only under paragraph I of RSA 21-J:33.);
- 2) RSA 21-J:33-a (Supp. 1993) "Substantial Understatement Penalty"; and
- 3) RSA 21-J:33-b (Supp. 1993) "Understatement of Taxpayer's Liability by Tax Preparer."

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Concerning the RSA 21-J:33 and RSA 21-J:33-a penalties, the parties should be prepared to address whether or not penalties can be assessed under both statutes. The board addressed a related issue in Pitchfork Records, Inc. v. DRA, Docket No. 5406-88 (copy attached). Additionally, the parties should be prepared to explain their interpretation of RSA 21-J:33-a II, which states the threshold requirement for imposing this penalty.

Concerning the RSA 21-J:33-b penalty, this case raises serious questions about whether the Taxpayer's accountant "Robinson" should be personally assessed this penalty. Robinson, therefore, will be accorded an opportunity to address this issue. He may appear on his own or with representation. To the extent necessary, the board asserts jurisdiction over Robinson. Robinson is ordered to attend the hearing. This order constitutes the board's issuance of a subpoena under RSA 71-B:9.

In addressing these questions, the DRA shall provide the board and the Taxpayer with copies of the DRA's BPT penalty rules that applied to tax years 1992 and 1993. The DRA shall, at least 10 days before the hearing, file such rules with the board with a copy sent to the Taxpayer.

The board understands the DRA only assessed the RSA 21-J:33 penalty. The board, however, concludes it has a duty to review the facts and arguments

and then apply the law (here the penalties statutes).

SO ORDERED.

BOARD OF TAX AND LAND APPEALS

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Paul B. Franklin, Chairman

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Ignatius MacLellan, Esq., Member

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Michele E. LeBrun, Member

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**Certification**

I hereby certify a copy of the foregoing decision has been mailed this date, postage prepaid, to Dana Rood, Taxpayer; John F. Hayes, Esq., Counsel for the Department of Revenue Administration; and certified mail to Stephen C. Robinson, Agent for Dana and Janice Rood, Taxpayers.

Date: July 23, 1998

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Valerie B. Lanigan, Clerk

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Dana and Janice Rood

v.

Department of Revenue Administration

Docket No.: 17347-97BP

ORDER

This order responds to:

- 1) the "DRA's" motion to limit the record;
- 2) the DRA's continuance motion; and
- 3) the "Taxpayers'" summary judgement motion.

The board denies all motions.

DRA's Motion to Limit the Record

The DRA moved to limit the record before the board to the record created before the DRA. The DRA, however, did agree that the board could, if good cause was shown, allow supplemental evidence. The DRA wanted the board to accept a copy of the DRA hearing transcript and a copy of all documents submitted at the hearing and to use that, along with the parties' arguments, to be the record before the board. Therefore, if the board adopted the DRA's position, the parties would be bound by the administrative record, unless good cause was shown, and furthermore, the board would not receive live testimony

but would review the case on the cold record.

The board denies the DRA's motion for the following reasons.

1) Reading the specific appeal statute and the board's general enabling statute supports the conclusion that the appeal to the board provides the opportunity to taxpayers and the DRA to present new evidence and new arguments.

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In reviewing the statutes, the board will apply the following general rules of statutory interpretation.

In construing statutes, the board should first examine the language and, where possible, ascribe plain and ordinary meaning to the words unless the statute itself suggests otherwise. Appeal of Astro Spectacular, 138 N.H. 298, 300 (1994); Appeal of Campton School District, 138 N.H. 267, 269 (1994).

The board must read the language at issue in the context of the entire statute and the statutory scheme. Barksdale v. Town of Epsom, 136 N.H. 511, 514 (1992); Great Lakes Aircraft Co., Inc. v. City of Claremont, 135 N.H. 270, 277 (1992).

In determining legislative intent and in construing a statute, the basic purpose -- the problem the statute was intended to remedy -- should be considered. Inquiry must be made into the statute's declared purpose and essential characteristics. Rix, 136 N.H. at 550; American Automobile Association v. State, 136 N.H. 579, 585 (1992).

RSA 21-J:28-b describes the review procedure in state-tax cases. First, there is an internal DRA review that includes a hearing before the DRA. RSA 21-J:28-b I, II, and III.

Following the DRA determination, the taxpayer may appeal to either the board or the superior court under RSA 21-J:28-b IV and VI, which provide in part as follows.

IV. \*\*\* The board of tax and land appeals or the superior court, as

the case may be, shall determine de novo the correctness of the commissioner's actions.

VI. The board or court may grant such relief as may be just and equitable \*\*\*.

Clearly, the crux of deciding this issue depends on the meaning of the phrase "determine de novo the correctness of the commissioner's actions." In making this determination, the board looks first at the plain meaning of the statute, reviewing the words within the context of the statutory scheme.

The board will first look at the plain meaning of "de novo" and then look at this specific statute in the context of the other applicable RSA 21-J statutes, the board's enabling statute, RSA Chapter 71-B, and the administrative procedures act, RSA 541-A.

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According to Black's Law Dictionary (6th ed. 1990) 435 the words "de novo" mean: "Anew; afresh; a second time. \*\*\*" According to Webster's 9th New Collegiate Dictionary (1990) 339, "de novo" means: "Over again: anew." Therefore, the plain meaning is that taxpayers and the DRA have an opportunity for a full and new hearing before the board. The DRA did not submit any argument to overcome the plain meaning of the statute.

2) This plain-meaning conclusion is also supported by the other applicable statutes that must be reviewed because they are part of the statutory scheme in state-tax appeals. Specifically, RSA 21-J:28-b VI empowers the board to grant such relief as may be just and appropriate. This demonstrates that the board has broad remedial authority, which would also

imply a broad authority to hear the parties' evidence to correctly craft a remedy.

Additionally, RSA 71-B:5 establishes the board's broad review in all tax matters.

**RSA 71-B:5 Authorities; Duties.** It shall be the duty of the board and it shall have the power and authority:

- I. To hear and determine all matters involving questions of taxation properly brought before it. Such matters may be brought before the board at the pleasure of the taxpayer or as otherwise provided by law. In determining matters before it, the board may institute its own investigation, or hold hearings, or take such other action as it shall deem necessary. (Emphasis added.)

Clearly, in determining de novo, the legislature gave the board the ability to receive further evidence at hearing or through the board's own investigation. Again, nothing in RSA 71-B:5 I limits the board's authority to hear matters in their entirety.

The board's procedures are also governed by RSA Chapter 541-A. The board was unable to find any specific limitation in that chapter that supported the DRA's position. The board concludes that chapter actually supports a true de novo hearing. Specifically, RSA 541-A:31 IV states: "Opportunity shall be afforded all parties to respond and present evidence and argument on all issues involved." This provides to the taxpayer the right to have a full hearing before the board. RSA 541-A:33 spells out additional

hearing rights that taxpayers and Page 4  
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the DRA hold, including the right of cross examination. That statute, RSA 541-A:33, also places restrictions on the board's ability to keep evidence out of the record. RSA 541-A:33 I allows the board to only exclude "irrelevant, immaterial or unduly repetitious evidence." The board does not have the

authority to keep out evidence simply because it is new. This is further evidence of the parties' rights to present a full case to the board.

3) The board concludes it cannot fulfill its statutory obligation simply by reviewing a written transcript from the DRA hearing. The board often has specific questions that need to be addressed at the hearing so the board can have before it the information necessary to decide the case. Thus, a full hearing is required to enable the board to carry out its RSA 71-B:5 I function and its RSA 21-J:28-b VI function to "grant such relief as may be just and equitable \*\*\*." The board has, almost without exception, found the live testimony to be essential in deciding cases both from an information gathering perspective and from a credibility perspective.

Furthermore, the live testimony is essential in allowing the board to decide whether certain penalties should apply. For example, RSA 21-J:31 provides a penalty when a taxpayer fails to file, but the penalty does not apply when "the failure to file was due to reasonable cause and not willful neglect of the taxpayer." Making such a determination on a cold record would be very difficult. The same is true for the other penalties provided by RSA 21-J, all of which require some determination concerning the taxpayer's action and motivations. See e.g., RSA 21-J:32, 33, 33-a.

4) It is also important to remember the legislative purpose behind granting a taxpayer a de novo determination before the board or the court. The appeal to either the board or to the court provides the first real non-DRA review of a taxpayer's case. While the DRA hearing is an adjudicative proceeding, it is nonetheless a hearing by the DRA's own personnel of determinations made by other DRA personnel. Both the audit division and the individuals who hold hearings for the DRA are subsets of the DRA and subject to the authority of the Page 5

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DRA commissioner. See RSA 21-J:3. It is only after an appeal is taken, pursuant to RSA 21-J:28-b, that the DRA commissioner no longer has final determination in state-tax matters. See also RSA 21-J:3 V.

As was discussed during the hearing on these motions, the Taxpayers asserted the DRA process was stacked against them. While the board makes no conclusion about whether this is true or not, it is clear that the legislature wanted to provide taxpayers with an unbiased non-DRA controlled appeal. Thus, it is essential that taxpayers have a fresh opportunity to present evidence and arguments.

5) The DRA's motion also runs contrary to a long-established practice of allowing taxpayers a full hearing before the board. Given this long-standing practice, the board is reluctant to change the practice when the legislature has not seen fit to redefine the board's role.

6) The DRA raised a concern that taxpayers would not fully prosecute their appeal at the DRA level if the parties knew they had a new opportunity at the board. The board has several comments on this point. First, whether parties will attempt to thwart the DRA's internal review should not enter into the analysis of what type of review is available before the board and the court. Second, the board expects parties to make reasonable efforts to comply with the DRA hearing process. At the same time, the board is mindful that the DRA hearing process will, in some instances, be less thorough and less well prepared than presentations made to the board or the court. This may be due to a taxpayer's attempt to informally, within the DRA, resolve the matter without spending additional dollars that might not be necessary if a resolution can be reached at the DRA level. If the DRA review still is not to

the taxpayer's satisfaction, there should be nothing that prevents the taxpayer from hiring attorneys and experts to more fully prepare the case. Nonetheless, the board expects taxpayers to reasonably and in good faith participate in the DRA review process.

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If the taxpayer fails to make such a good-faith effort, there may be remedies available to address that, including the imposition of attorneys fees and costs under RSA 21-J:28-b VI.

**DRA's Continuance Motion**

The board denies the DRA's continuance motion. The DRA asserted that if the board did not limit the evidence as requested above, the DRA would need a continuance to conduct discovery. The board finds this argument to be insufficient because: 1) the DRA already knew the board's position on the first motion because the board had denied a similar motion in Appleton Inns, Inc. v. DRA, Docket No.: 16734-96BP (October 16, 1997); and 2) the evidence and arguments submitted before the board will most likely be identical to that which has already been submitted to the DRA. If the DRA or the Taxpayers conclude, at the end of the hearing, that they need additional time to supplement the record, the parties may make such a request.

**Taxpayers' Summary Judgement Motion**

The Taxpayers moved for summary judgement based on the Taxpayers' assertion that the DRA review process was not fair because "the Department completely disregarded the taxpayers' constitutional rights to due process, a fair, impartial and swift decision." The board finds no basis in the

Taxpayers' motion to grant summary judgement. Whatever occurred at the DRA level is not determinative of whether the Taxpayers were correctly assessed the business profits tax. This issue will be determined by the board at the upcoming hearing.

### **Rehearing and Appeals**

A motion for rehearing, reconsideration or clarification (collectively "rehearing motion") of this order must be filed within thirty (30) days of the clerk's date below, not the date this decision is received. RSA 541:3; TAX 201.37. The rehearing motion must state with specificity all of the reasons supporting the request. RSA 541:4; TAX 201.37(b). A rehearing motion is granted only if the moving party establishes: 1) the decision needs clarification; or 2) based on the evidence and arguments submitted to the

board, the board's

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decision was erroneous in fact or in law. Thus, new evidence and new arguments are only allowed in very limited circumstances as stated in board rule TAX 201.37(e). Filing a rehearing motion is a prerequisite for appealing to the supreme court, and the grounds on appeal are limited to those stated in the

rehearing motion. RSA 541:6. Generally, if the board denies the rehearing motion, an appeal to the supreme court must be filed within thirty (30) days of the date on the board's denial.

Please Note: The board will not rule on any rehearing motions to this order until the board has issued its final decision. The board will then rule on all rehearing motions to this order and to the final decision. This way the issues are all in one order if an appeal is taken.

SO ORDERED.

BOARD OF TAX AND LAND APPEALS

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Paul B. Franklin, Chairman

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Ignatius MacLellan, Esq., Member

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Michele E. LeBrun, Member

**Certification**

I hereby certify that a copy of the foregoing order has been mailed this date, postage prepaid, to Stephen C. Robinson, representative for the Taxpayers; and John F. Hayes, Esq., counsel for the DRA.

Date: May 27, 1998

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Valerie B. Lanigan, Clerk

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