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ADMINISTRATIVE LAW—TAXATION

Summary

An appeal from a district court order granting a petition for judicial review in a tax matter.

Disposition/Outcome

The Court found that the Nevada Tax Commission improperly substituted its judgment for that of the administrative law judge, whose determination was based on substantial evidence. The Court also found that, because the only bar to filing a timely refund claim was a procedural technicality, equity warranted a tolling of the statute of limitations. Thus, the Court affirmed the district court’s decision to grant the taxpayer’s petition for judicial review and the taxpayer’s entire refund request.

Factual and Procedural History

Masco Builder Cabinet Group (“Masco”) is a cabinet-manufacturing company that sells its cabinets in retail showrooms and installs them in houses. Under Nevada’s tax code, Masco had to remit sales tax to the Nevada Department of Taxation (“Tax Department”) for each retail sale it made, and remit a use tax for each construction contract it entered into.\(^2\) Sales tax is calculated as percentage of the retail price while use tax is calculated as a percentage of the cost to acquire the cabinet components.\(^3\) Masco acquired Root Industries (“Root”) in 2003, and retained Root’s personnel, based in Reno, to handle Masco’s northern Nevada business. Root kept the same computer system and accounting program it used under its prior ownership. This program automatically added “sales tax” on every invoice sent to a customer, including ones for contract sales.

Masco’s construction contracts were structured differently than its retail contracts. Under its construction contracts, customers would pay a lump sum to Masco, and Masco would be responsible for paying any taxes. To ensure that the proper tax was paid, Masco had to calculate the tax into its lump price. Instead of applying the use tax, Masco would enter the price into its accounting system as the lump sum minus the sales tax and then remit the remainder to the Department of Taxation as “sales tax.”

In 2006, the Tax Department audited Masco and discovered that Masco had been remitting a “sales tax” for its contract work when it should have been remitting a “use tax.” The monetary difference between the two was substantial. Both the auditor and Masco preliminarily agreed that Masco was entitled to a refund and the auditor said he would consider the potential refund within the context of the audit.

\(^1\) By Rami Hernandez.
\(^3\) *Id.*
Under Nevada law, a taxpayer must file a formal refund claim within three years of when the purported overpayment occurred. Additionally, the Tax Department is only allowed to collect for underpayments that occurred within three years of when the deficiency is made. Because the audit would be lengthy, the Tax Department requested that Masco sign a waiver of the statute of limitations. This waiver would allow the Tax Department to collect on a past deficiency. Masco was under the understanding that it could collect for any overpayments as well. Upon this understanding, Masco did not file a formal refund claim until after the audit had concluded.

Per department policy, Tax Department waiver forms only extended the statute of limitations for three months at a time. As a result, Masco signed several waivers between mid-2006 and mid-2007. By 2007, the audit had been completed, but the auditor who performed it left the Tax Department without notifying or informing Masco that the audit had finished. Masco realized that the most recent waiver was about to expire and contacted the Tax Department to get the waiver extended, but its calls were not returned. Eventually, Masco spoke to the new auditor, but the last waiver had already expired. The new auditor told Masco that the Tax Department was denying its refund request.

Two months later, Masco received the Tax Department’s deficiency request, which made no mention of the refund request or why it was denied. Masco filed a formal refund claim in January 2008 as part of a petition for redetermination. At a hearing before an Administrative Law Judge (“ALJ”), the Tax Department maintained that Masco was not entitled to a refund because it had been acting as retail seller under the contracts in question and that even if entitled to a refund, any overpayments three years prior to January 2008 were time-barred.

The ALJ disagreed with the Tax Department, finding that Masco’s contracts were construction contracts and Masco was entitled to a refund on the overpaid sales tax. The ALJ also determined that Masco relied on the auditor’s representation that he would consider Masco’s refund request within the context of the audit.

The Tax Department appealed the ALJ’s determinations to the Tax Commission. After a hearing, the Tax Commission reversed the ALJ’s determination that Masco was entitled to a refund. It also found, without addressing Masco’s reliance on the auditor, that Masco’s failure to timely file a refund claim would render a portion of its refund request time-barred.

Masco filed a petition for judicial review. The district court granted Masco’s petition on the basis that the Tax Commission has improperly substituted its judgment for the ALJ’s. The court reinstated the ALJ’s original determination that Masco was entitled to a refund and that the refund should cover the entire audit period. The Tax Department appealed.

Discussion

The three-justice panel wrote its unanimous opinion per curiam. The Tax Department made two arguments at the appeals hearing. First, the Tax Commission acted properly because

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the ALJ’s determination was clearly erroneous. Second, even if Masco is entitled to a tax refund, it should be limited to three years prior to its filing for a claim in January 2008 per the statute of limitations.

Based on the substantial evidence in the record, the Supreme Court found that the ALJ’s determination that Masco was entitled to a refund was not clearly erroneous. The Court also found that under the “doctrine of equitable tolling,” the applicable statute of limitations tolled from the moment Masco signed the Tax Department’s first waiver in June 2006 with the understanding that its refund request would be considered in the context of the audit.

The standard of review the Court uses for reviewing an administrative agency’s decision is the same as that of a district court. Legal questions are reviewed de novo and factual questions are limited to whether the agency’s decision is supported by substantial evidence. The same standard as the Supreme Court’s analysis governed the Tax Commission’s review of the ALJ’s finding.

Because the Tax Commission’s finding was based on substantial evidence, it improperly substituted its own judgment for that of the ALJ. The Tax Department argued that the invoices from Root prove that Masco intended its construction contracts to be retail contracts. Masco disagreed, providing language from its original contracts showing they were more akin to construction contracts than retail contracts. Based on this evidence, the ALJ found that the construction contracts’ inclusion of lump sums demonstrate the contracts were construction contracts and not retail contracts. The invoices produced by Root, including the sales tax line, were merely clerical instruments not indicative of the contract’s intentions. The Tax Department did not address the ALJ’s evidentiary findings, nor why the invoices reflect Masco’s choice to act as a retail seller. The Court therefore affirmed the district court’s determination to reinstate the ALJ’s determination that Masco is entitled to a refund.

Concerning the question of the statutory period, the Court applied the doctrine of equitable tolling, which suspends the running of a statute of limitations when the only bar to a timely filed claim is a procedural technicality. Here, the Court found that the only basis for the Tax Department’s argument was a procedural technicality. Masco’s only shortcoming was that it did not send the Tax Department its refund request after telling the original tax auditor that it would be requesting one. The Tax Department knew of Masco’s basis for its refund request for the beginning of the audit and had investigated the matter. Thus, there was no danger of prejudice to the Tax Department. Finally, the Court found that the interests of justice require the suspension of the statute of limitations. Using a factors test found in case law, the Court found that Masco attempted to contact the Tax Department and was ignored. Effectively, the Tax Department lulled Masco into a “false sense of security” and then changed its mind because it was no longer convenient or financially beneficial.

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7 Id.
8 NEV. REV. STAT. § 360.390(2) (2007).
10 Copeland, 99 Nev. at 826, 673 P.2d at 492.
Conclusion

An Administrative Law Judge’s decision is subject to the same review as a court’s decision and factual decisions are limited to whether the agency’s decision is supported by substantial evidence. Additionally, the statute of limitations is suspended under the doctrine of equitable tolling when the only bar to filing a timely claim is a procedural technicality.