

**BEFORE THE HEARING OFFICER
OF THE TAXATION AND REVENUE DEPARTMENT
OF THE STATE OF NEW MEXICO**

**IN THE MATTER OF THE PROTEST
OF THE WHITEHURST GROUP
TO ASSESSMENT OF PENALTY AND
INTEREST ISSUED UNDER LETTER
ID NO. L0480377472**

No. 10-02

DECISION AND ORDER

An administrative hearing on the above-referenced protest was held on December 10, 2009 at 9:00 AM, before Brian VanDenzen, Hearing Officer. The Taxation and Revenue Department (“Department”) was represented by Tonya Noonan Herring, Special Assistant Attorney General. Mr. Charles Whitehurst and Mrs. Jean Whitehurst appeared (“Whitehursts”). Mr. Whitehurst, as President of the Whitehurst Group, represented the Whitehurst Group (“Taxpayer Whitehurst Group”) pro se. Exhibits Department A-H are admitted into the record by stipulation. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. Taxpayer Whitehurst Group registered in New Mexico as an LLC in 2001.
2. Charles Whitehurst is registered as the corporate President of the Whitehurst Group.
3. Ms. Jean Whitehurst is a corporate officer in the Whitehurst Group
4. The Whitehursts moved to New Mexico permanently in 2003 from Baton Rouge.
5. Mr. Whitehurst made the decision to organize the Taxpayer Whitehurst Group as an LLC in order to protect the partners from personal liability.

6. Taxpayer Whitehurst Group filed both federal taxes and state taxes as an S-Corporation.
7. For tax year 2004, the Whitehursts filed a Federal income tax return where they requested that Taxpayer Whitehurst Group be given S-Corporation status.
8. For tax year 2004, the Whitehursts timely filed personal income tax returns, including a pass-through for their S-Corporation Whitehurst Group, with the State of New Mexico.
9. As part of that 2004 New Mexico personal income tax return, the Whitehursts timely submitted a payment of \$2,942.00.
10. At some point in early 2006, the Internal Revenue Service (“IRS”) informed the Whitehursts that Taxpayer Whitehurst Group did not qualify in the tax year of 2004 as an S-Corporation for failure to timely sign and submit the correct form.
11. As a result of personal income tax ramifications of the Taxpayer Whitehurst Group not being granted S-Corporation status for the tax-year 2004, the Whitehursts filed an amended New Mexico personal income tax return on November 16, 2006.
12. As a result of that amended personal income tax return for tax year 2004, the Whitehursts was entitled to a \$1,937.00 refund.
13. As a result of not being granted S-Corporation status for the tax-year 2004, on November 16, 2006, Taxpayer Whitehurst Group for the first time filed a tax-year 2004 New Mexico corporate income tax return for the Whitehurst Group.
14. New Mexico corporate income tax returns for the tax year 2004 were originally due on March 15, 2005.

15. Taxpayer Whitehurst Group's New Mexico corporate income tax return for tax year 2004 filed on November 16, 2006, indicated that the Taxpayer Whitehurst Group owed the State \$1,239.00 in tax principle.

16. On November 16, 2006, the Whitehursts also submitted a cover letter explaining the reason for their amended personal income tax return and the late filing of Taxpayer Whitehurst Group's corporate income tax returns.

17. In that letter, the Whitehursts informed the Department that because of financial difficulties, the Taxpayer Whitehurst Group would not be able to pay its outstanding corporate income tax until the Whitehursts received their personal income tax refund.

18. On March 8, 2007, the Department issued by mail a tax year 2004 personal income tax refund in the amount of \$1,937.00 to the Whitehursts.

19. On March 21, 2007, Taxpayer Whitehurst Group remitted the outstanding corporate income tax of \$1,239.00 to the Department.

20. On March 29, 2009, the Department issued the Taxpayer Whitehurst Group a Notice of Assessment for unpaid tax, penalty, and interest in the amount of \$1,736.28.

21. Ms. Andrea Umpleby is a Protest Auditor for the Department.

22. Ms. Umpleby audited the file of both the Taxpayer Whitehurst Group and the personal income tax returns of the Whitehursts.

23. In addition to crediting the \$1,239.00 payment of taxes made by Taxpayer Whitehurst Group and adjusting the outstanding interest as a result of that payment, Ms. Umpleby credited a \$50.00 payment against the amount originally listed in the Notice of Assessment.

24. As of the date of the hearing, penalty and interest in the amount of \$425.83 remained outstanding against Taxpayer Whitehurst Group.

25. Ms. Umpleby testified that the Department distinguishes between individual personal income tax returns and corporate income tax returns.

26. Ms. Umpleby testified that personal income tax returns are a separate account with a separate name based on an individual's social security number.

27. Ms. Umpleby testified that corporate income tax returns are a separate account with a separate name, based on a federal identification number issued to the corporation.

28. Taxpayer Whitehurst Group is a separate and distinct legal entity from the Whitehursts.

29. On April 9, 2007, Taxpayer Whitehurst Group timely filed a written protest to the assessment of interest and penalty.

DISCUSSION

The Whitehursts challenges the imposition of penalty and interest against the Taxpayer Whitehurst Group for the tax year 2004. The Whitehursts point out that they timely filed their personal income tax returns (including remittance of outstanding tax) for the tax year 2004 relying on the fact that the Taxpayer Whitehurst Group had always been accepted as an S-Corporation. Only after the IRS indicated that the Taxpayer Whitehurst Group had to file as a C-Corporation in 2006 did Taxpayer Whitehurst Group file corporate income tax returns. However, the Whitehursts argue that the outstanding amount of tax refund owed to them on their amended New Mexico 2004 personal income tax return was more than enough to meet the outstanding 2004 corporate income tax owed to the State by the Taxpayer Whitehurst Group. Taxpayer Whitehurst Group argues that since the State possessed the money necessary to satisfy

its outstanding 2004 corporate tax with the refund money owed personally to the Whitehursts as part of their 2004 personal income tax refund, the Taxpayer Whitehurst Group should not be charged penalty and interest.

Burden of Proof. NMSA 1978, §7-1-17(C) (2007) provides that any assessment of tax by the Department is presumed to be correct. NMSA 1978, §7-1-3 (2003) defines tax to include not only the amount of tax principal imposed but also, unless the context otherwise required, “the amount of any interest or civil penalty relating thereto.” See El Centro Villa Nursing Center v. Taxation and Revenue Department, 108 N.M. 795, 779 P.2d 982 (Ct. App. 1989). Accordingly, the assessment issued to the Taxpayer is presumed to be correct, and it is the Taxpayer’s burden to present evidence and legal argument to show that they are entitled to an abatement of the penalty and interest.

Distinction between Corporate Income Tax and Personal Income Tax. The Whitehursts argue that the Department should have credited the refund owed to them under their amended 2004 personal income tax return against the money owed to the State by the Taxpayer Whitehurst Group for 2004 corporate income taxes.

In New Mexico, personal income tax and corporate income tax are governed by two separate statutes. NMSA 1978, Sec. 7-2 governs the imposition of Personal Income Tax. NMSA 1978, Sec. 7-2A governs the imposition of Corporate Income and Franchise Tax. Each tax is a separate and distinct tax by law, with its own unique legal requirements and obligations. For the purposes of the Tax Code, Taxpayer Whitehurst Group and the Whitehursts are two separate and distinct taxpayers. No provision under the Tax Code allows the Department to credit a refund due from personal income tax against corporate income tax.

In addition to the Tax Code distinction between personal and corporate income tax, as a matter of execution of collection of those unique taxes, the Department treats personal income tax and corporate income tax as entirely distinct and separate accounts. According to Ms. Umpleby, each form of tax is tracked by a separate and distinct account number. Personal income tax is categorized by the individual's social security number, while corporate income tax is categorized by the federal identification number issued to the corporation.

Finally, it is a basic tenant of the law of corporations that a corporation is a legally distinct and separate entity from any of the individuals comprising the corporate structure. As Mr. Whitehurst acknowledged in his testimony, one of the benefits of forming a LLC is to shield the individual officers of the corporation from personal liability for corporation obligations. Yet, the Whitehursts' suggestion of credit between personal income tax accounts and corporate income tax accounts would defeat this personal-liability shield benefit that the Whitehursts' sought when forming the LLC. To credit the refund of an individual's personal income tax, even if that individual happens to be a corporate officer, against the outstanding corporate income taxes of the corporation would not only be contrary to the clear statutory structure of income tax in New Mexico, but would also be contrary to fundamental tenants of corporate law. Consequently, the fact that the Whitehursts as individuals were due a personal income tax refund for the year 2004, and that the State possessed that money, has no bearing on the separate and distinct corporate income tax liabilities and obligations of the Taxpayer Whitehurst Group.

Assessment of Interest. When a taxpayer fails to make timely payment of taxes due to the state, "interest shall be paid to the state on that amount from the first day following the day on which the tax becomes due...until it is paid." NMSA 1978, §7-1-67 (2003). Under the statute, the Department has no discretion in the imposition of interest, as the statutory use of the word "shall"

makes the imposition of interest mandatory regardless of the explanation provided by a taxpayer. See State v. Lujan, 90 N.M. 103, 105, 560 P.2d 167, 169 (1977). The language of the statute also makes it clear that interest begins to run from the original due date of the tax.

In this case, Taxpayer Whitehurst Group's corporate income tax return for the tax year 2004 was due on March 15, 2005. Although the Whitehursts have a perfectly understandable explanation for why no corporate income tax returns were filed or paid by that date, Taxpayer Whitehurst Group's corporate income tax still remained due and unpaid until March 21, 2007. Consequently, even though the problems in this case were not intentional, the statute mandates the imposition of interest for the time that the 2004 corporate income tax was due and unpaid until the time that Taxpayer Whitehurst Group remitted payment on March 21, 2007.

Assessment of Penalty. When a taxpayer fails to pay taxes due to the State as a result of negligence or disregard of rules and regulations, NMSA 1978, § 7-1-69(A) (2003) imposes a penalty of two percent per month "from the date the tax was due," not to exceed ten percent of the outstanding tax liability. Again, the statute's use of the word "shall" makes the imposition of penalty mandatory in all instances where a taxpayer's failure to act timely meets the legal definition of "negligence."

The term "negligence" is defined in Regulation §3.1.11.10 NMAC (1/15/01) to include "inadvertence, indifference, thoughtlessness, carelessness, erroneous belief or inattention." In this case, based on a past history of acceptance of the Whitehurst Group as an S-Corporation, Taxpayer Whitehurst Group was under the erroneous belief that the Whitehurst Group again would be recognized by the IRS as an S-Corporation during tax year 2004. The efforts of the Whitehursts to follow up with the IRS indicate that the Whitehursts were genuinely concerned with remedying the inadvertent and unintentional error. Nevertheless, inadvertent error based on an erroneous belief

meets the legal definition of “negligence” under the penalty statute. See El Centro Villa Nursing Center v. Taxation and Revenue Department, 108 N.M. 795, 799, 779 P.2d 982, 986 (Ct. App. 1989).

Taxpayer Whitehurst Group presented no convincing evidence under Regulation §3.1.11.11 NMAC (1/15/01) to demonstrate indicators of nonnegligence. Although Taxpayer Whitehurst Group did refer to using an accountant, there is no further evidence to demonstrate that Taxpayer Whitehurst Group reasonably relied on the accountant’s advice after full disclosure of all relevant facts. In fact, Taxpayer Whitehurst Group presented no evidence that the accountant played any role in making the initial inadvertent mistake. The Whitehursts did file an amended personal income tax return and new corporate income tax return on behalf of Taxpayer Whitehurst Group based on the advice of their accountant, but by that point the inadvertent error had already occurred based on the Taxpayer’s previous decision to file as an S-Corporation. In other words, rather than the source of the initial inadvertent error, the advice of the accountant that the Taxpayer Whitehurst Group relied on was merely to remedy the previously-made inadvertent error. Based on the Taxpayer Whitehurst Group’s numerous statements that they filed as an S-Corporation in 2004 because that is how they had filed in the past, the decision to file as an S-Corporation seems to be based on the Taxpayer’s own personal past history rather than on any specific professional advice of an accountant.

Because inadvertent error based on an erroneous belief meets the statutory and regulatory definition of negligence, and because the Taxpayer failed to demonstrate any indications of nonnegligence, the Department is mandated by statute to impose penalty on the Taxpayer in this case for failure to timely pay corporate income tax.

CONCLUSIONS OF LAW

A. The Taxpayer filed a timely protest to the Department's assessment of interest and penalty, and jurisdiction lies over the parties and the subject matter of this protest.

B. The Department's assessment was issued within the three-year limitations period provided in NMSA 1978, § 7-1-18.

C. Pursuant to NMSA 1978, § 7-1-67, the Taxpayer is liable for interest for late payment of 2004 corporate income tax.

D. Pursuant to NMSA 1978, § 7-1-69, the Taxpayer is liable for penalty for late payment of 2004 corporate income tax.

For the foregoing reasons, the **Taxpayer's protest IS DENIED.**

DATED: February 10, 2010.