

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

**IN THE MATTER OF THE PROTEST OF
STUART SCHOENMANN AND CHARLOTTE COULOMBE No. 12-12
TO THE DENIALS OF REFUND ISSUED UNDER
ID NOS. L0063812160 and L1136948800**

DECISION AND ORDER

A formal hearing on the above-referenced protests was held March 8, 2012, before Dee Dee Hoxie, Hearing Officer. The Taxation and Revenue Department (Department) was represented by Mr. Nelson Goodin, Chief Legal Counsel. Ms. Milagros Bernardo, Auditor, also appeared on behalf of the Department. Mr. Stuart Schoenmann (Taxpayer) appeared for the hearing and was represented by his accountants, Mr. John Grisham and Mr. Curt McGill. The Hearing Officer took notice of all documents in the administrative file. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. The Taxpayer was a resident of New Mexico in 2009 and 2010. The Taxpayer was a member of an LLC during those years and also served as the LLC's Chief Executive Officer (CEO) during those years.
2. The Taxpayer received guaranteed payments for his duties as CEO. The Taxpayer also received distributive shares of income as a member of the LLC.
3. The Taxpayer filed personal income tax returns with New Mexico for 2009 and 2010. The Taxpayer claimed refunds for 2009 and 2010. The Taxpayer allocated and apportioned his income from the distributive shares to various states in which the LLC

does business. The Taxpayer allocated all of his income from the guaranteed payments to New Mexico as compensation and applied for credit for taxes paid to other states.

4. The Department denied the Taxpayer's claims for refund and assessed additional tax for each year.
5. The Taxpayer filed timely protests.
6. The Department abated the assessments and partially granted the claims for refund. The amount still at issue for the 2009 tax year is \$5,022.00. The amount still at issue for the 2010 tax year is \$1,937.00. The amounts in controversy arise from the allocation of all of the guaranteed payments to New Mexico and the claim of credit for taxes paid to other states.
7. On October 27, 2011, the Department filed a Request for Hearing asking that the Taxpayer's protest on the 2009 tax year be scheduled for a formal administrative hearing.
8. On March 2, 2012, the Department filed a Motion to Consolidate the hearings for the 2009 and 2010 tax years as they involved the same issues. The Request for Hearing for the 2010 tax year was filed on the date of the hearing.
9. The Motion to Consolidate was unopposed and was granted.
10. The parties stipulated to the facts at the hearing.

DISCUSSION

The issue to be decided is whether the Taxpayer's receipt of guaranteed payments for acting as CEO of the LLC should be allocated entirely to New Mexico or should be allocated and apportioned to the other states in which the Taxpayer conducts business.

Allocation of Income.

The Taxpayer argues that the guaranteed payments were compensation for his services as CEO and should be allocated to New Mexico. The Department argues that the guaranteed payments do not meet the statutory definition of compensation as the Taxpayer was not technically considered to be an employee because he was a member of the LLC.

For income taxable in this state as well as in another, compensation of residents of this state must be allocated to this state. *See* NMSA 1978, § 7-2-11 (A) (3). Compensation is defined as “wages, salaries, commissions, and any other form of remuneration paid to *employees* for personal services”. NMSA 1978, § 7-2-2 (C) (emphasis added). *See also* NMSA 1978, § 7-4-2 (C). Other income is to be allocated and apportioned as required by the Uniform Division of Income for Tax Purposes Act. *See* NMSA 1978, § 7-2-11 (A) (2). If that Act does not specify how a certain type of income should be apportioned, then the income will be apportioned in accordance with rulings, instructions, or regulations of the Department. *See id.*

The parties agreed that the Taxpayer was not technically considered an employee of the LLC because he had become a member of the LLC. The Taxpayer started out as the CEO and later bought into the LLC. The Taxpayer continued to act as the CEO after he became a member of the LLC. The Taxpayer’s salary was recategorized as guaranteed payments after he became a member. The LLC was still able to treat the guaranteed payments as wages paid for its tax purposes. *See* I.R.C. §707. The Taxpayer argues that he was still being compensated for acting as CEO and that the guaranteed payments should be considered compensation for allocation purposes. The Department argues that he was not technically an employee and that the statutory definition should control what is considered to be compensation.

The statutes do not define the term “employee”. *See* NMSA 1978, § 7-2-2, and § 7-4-2. *See also* NMSA 1978, § 7-1-3 (D) (defining “employee of the department” as any employee or

any person acting as agent or who is authorized to act on behalf of the department in any capacity). The regulations governing allocation and apportionment actually seem to promote the use of common-law rules in determining whether a person is an employee. *See* 3.5.14.8 (E) NMAC (defining employee as “any officer of a corporation or any individual who, under the usual common-law rules applicable in determining the employer-employee relationship, has the status of an employee.”). Using a common-law approach, the Taxpayer was an employee of the LLC in his capacity as CEO. Moreover, income that is from “the rendering of purely personal services by an *individual*” is excepted from the requirement of allocation and apportionment. *See* NMSA 1978, § 7-4-3 (emphasis added). This statute does not require that the individual be an employee. *See id.* The Uniform Division of Income for Tax Purposes Act does not provide how income derived from rendering personal services should be allocated or apportioned. *See* NMSA 1978, § 7-4-1, *et seq.* The regulations are also silent on this issue. *See* 3.3.11.8 through 3.3.11.14 NMAC. *See also* 3.5.3.7 through 3.5.3.11, and 3.5.19.8 through 3.5.19.19 NMAC. Allocation and apportionment is a function of statutory and regulatory provisions. *See* NMSA 1978, § 7-2-11.

As there is not a statutory or regulatory provision governing how to allocate and apportion a guaranteed payment that is made to an individual for the performance of a personal service, the income should be allocated to New Mexico. *See* NMSA 1978, § 7-2-3 (providing generally that all net income of residents of the state is subject to taxation). *See also* NMSA 1978, § 7-4-3 (specifically exempting income from personal service from the requirements of allocation and apportionment). Consequently, the Taxpayer’s claims for refund were valid based upon his allocation of the total amount of guaranteed payments to New Mexico.

CONCLUSIONS OF LAW

1. The Taxpayer filed a timely written protest to the denials of refunds for 2009 and 2010 issued under respective Letter ID numbers L0063812160 and L1136948800, and jurisdiction lies over the parties and the subject matter of this protest.

2. The Taxpayer received guaranteed payments from the LLC for services rendered in 2009 and 2010.

3. As there are not any statutory or regulatory provisions requiring allocation and apportionment of guaranteed payments that are made for services rendered by an individual, the Taxpayer appropriately allocated the entire amount of the guaranteed payments to New Mexico. *See* NMSA 1978, § 7-4-3.

4. The Taxpayer's claims for refund were valid and should have been granted.

For the foregoing reasons, the Taxpayer's protest is **GRANTED** and the Department is hereby ordered to grant the remaining claims for refunds to the Taxpayer.

DATED: April 9, 2012.

DEE DEE HOXIE
Hearing Officer
Taxation & Revenue Department
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