

**STATE OF NEW MEXICO
ADMINISTRATIVE HEARINGS OFFICE
TAX ADMINISTRATION ACT**

**IN THE MATTER OF THE PROTEST OF
FLOYD & ANNA RIVERA
TO ASSESSMENT ISSUED UNDER LETTER
ID NO. L1708617680**

No. 15-28

DECISION AND ORDER

A protest hearing occurred on the above captioned matter on June 29, 2015 before Brian VanDenzen, Esq., Chief Hearing Officer, in Santa Fe. At the hearing, Floyd Rivera appeared *pro se*, representing Floyd & Anna Rivera (“Taxpayers”). Staff Attorney Peter Breen appeared representing the State of New Mexico Taxation and Revenue Department (“Department”). Protest Auditor Sonya Varela appeared as a witness for the Department. Taxpayers’ Exhibits #1-10 were admitted into the record. Department Exhibits A-B were admitted into the record. All exhibits are more thoroughly described in the Administrative Exhibit Coversheet. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. On April 8, 2015, the Department assessed Taxpayers for \$483.00 in personal income tax, \$96.60 in penalty, and \$59.51 in interest for a total tax assessment of \$639.11 for the personal income tax period ending on December 31, 2010. [Letter id. no. L1708617680].
2. On April 10, 2015, the Department received Taxpayers’ protest of the assessment.
3. On June 10, 2015, the Department requested a hearing in this matter with the Hearings Bureau¹.

¹ On July 1, 2015, pursuant to enacted Senate Bill 356, the Hearings Bureau became the Administrative Hearings Office (“AHO”). Since most of the events, except issuance of this decision, occurred before that date, the Hearings Bureau will be referenced in the findings of fact even though the decision is issued under AHO’s caption.

4. On June 10, 2015, the Hearings Bureau set this matter for a hearing on June 29, 2015, within 90-days of Taxpayers' protest.
5. There is no dispute that Taxpayers timely filed 2010 Personal Income Tax federal and state returns with the IRS and New Mexico.
6. On June 9, 2011, Taxpayers received an assessment of taxes from the Department for an additional \$23.41. This is not the assessment at issue in this protest.
7. The Department detected a mismatch between Taxpayers' federal and state returns as part of the Tape Mismatch Program.
8. On October 19, 2014, the Department submitted to Taxpayers a Notice of Limited Scope Audit Commencement-2010 Personal Income Tax because of discrepancy between the New Mexico PIT return and the IRS return. [Taxpayers Ex. #1].
9. In trying to determine the discrepancy, Taxpayers made numerous contacts with Department employees and IRS employees. Taxpayers did learn of a discrepancy of \$280.00 in social security income, which is consistent with the \$23.41 in additional tax assessed on June 9, 2011.
10. The discrepancy in this case primarily relates to a misreporting on line 8 of the New Mexico 2010 PIT-1 form, where a taxpayer is to report the amount of state and local income or general sales tax deduction claimed on their federal itemized deduction, as shown on federal Schedule A. In error, Taxpayers only reported \$2,160 instead of the \$11,700 amount of state and local tax shown on Taxpayers' Schedule A. [Department Ex. A; 06-31-15 CD 27:38-32:16].
11. There were two other minor discrepancies related to an arithmetic error and a transposition of numbers. [06-31-15 CD 27:38-32:16].

12. Taxpayers only reported a state personal income tax liability of \$1045.00 but in light the errors had an actual tax liability of \$1,528.00, which is a tax liability approximately 46% higher than initially reported. [Department Ex. A; 06-31-15 CD 45:30-46:55].

13. Consequently, Taxpayers underreported their personal income tax liability in 2010 by more than 25%. [Department Ex. A; 06-31-15 CD 45:30-46:55].

14. Although Taxpayers' errors were unintentional, the errors were inadvertent and based on an erroneous belief that New Mexico treated the itemized deduction the same as the IRS. [06-31-15 CD 38:00-41:04].

15. As of the date of hearing, for the personal income tax reporting period ending on December 31, 2010, Taxpayers owed \$483.00 in personal income tax, \$96.60 in penalty, and \$63.00 in interest for a total tax liability of \$642.60. [Department Ex. B].

DISCUSSION

There are only two issues in this case. First, Taxpayers did not understand the discrepancy at issue and believed the returns were accurate with exception of one \$280 error. Secondly, Taxpayers argued that the statute of limitations had lapsed by the time the Department issued its assessment.

Under NMSA 1978, Section 7-1-17(C) (2007), the assessment of tax issued in this case is presumed correct. Unless otherwise specified, for the purposes of the Tax Administration Act, "tax" is defined to include interest and civil penalty. *See* NMSA 1978, §7-1-3 (X) (2013). Under Regulation 3.1.6.13 NMAC, the presumption of correctness under Section 7-1-17 (C) extends to the Department's assessment of penalty and interest. *See Chevron U.S.A., Inc. v. State ex rel. Dep't of Taxation & Revenue*, 2006-NMCA-50, ¶16, 139 N.M. 498, 503 (agency regulations interpreting a statute are presumed proper and are to be given substantial weight). Taxpayers have the burden to

overcome the assessment. *See Archuleta v. O'Cheskey*, 1972-NMCA-165, ¶11, 84 N.M. 428, 431. However, once a taxpayer rebuts the presumption of correctness, the burden shifts to the Department to show the correctness of the assessed tax. *See MPC Ltd. v. N.M. Taxation & Revenue Dep't*, 2003-NMCA-21, ¶13, 133 N.M. 217.

Payment of New Mexico personal income tax is governed by NMSA 1978, §§ 7-2-1 to 36. Unless otherwise exempted by law, a tax is imposed “upon the net income of every” New Mexico resident. NMSA 1978, § 7-2-3 (1981). NMSA 1978, Section 7-2-12 (2003) requires any resident or any person deriving income from New Mexico to file a state income tax return. Like many states, the calculation of New Mexico’s personal income tax liability begins with a taxpayer’s adjusted gross income as reported to the IRS. *See* NMSA 1978, § 7-2-2 (A) (2010); *See also Holt v. N.M. Dep't of Taxation & Revenue*, 2002- NMSC-34, ¶23, 133 N.M. 11 (“calculation of the taxpayers’ state income tax is based upon their adjusted gross income...on their federal return.”).

However, the federal adjusted gross income is only a beginning point, as New Mexico varies in its treatment of personal income tax from the IRS. *See Holt*, ¶6 (state has the authority to assess and collect tax independent of IRS). One of those areas where New Mexico varies is in the treatment state and local income or general income sales tax deductions claimed as part of the federal itemized deduction. *See* NMSA 1978, Section 7-2-2 (N) (2) (2010). Under Section 7-2-2 (N) (2), the amount of the state and local tax included in a taxpayer’s federal itemized deduction is not deductible in New Mexico and remains part of the “net income” subject to state personal income tax. To achieve this statutory requirement, New Mexico requires that the amount of state and local tax listed on a taxpayer’s Schedule A be added back to the federal adjusted gross income on Line 8 of New Mexico’s PIT-1 Return.

In large part, the Department's assessment in this case stems from Taxpayers' reporting error Line 8 of the New Mexico PIT-1 return. Taxpayers only reported \$2,160.00 on line 8 rather than the \$11,700.00 in state and local income taxes listed on Taxpayers' corresponding Schedule A. Because of this error, Taxpayers inadvertently underreported their New Mexico base income by \$9,540. This error, along with two other minor errors related to transposing numbers and an arithmetic error, substantiated the amount of Department's assessment at issue in this protest, a fact that Mr. Rivera implicitly acknowledged while cross-examining Department Auditor Sonya Varela.

Nevertheless, Taxpayers continued to argue that the normal three-year statute of limitations for an assessment of 2010 personal income taxes had lapsed by the time of the April 8, 2015 assessment in this case. The hearing officer agrees that the assessment was not made within three-years of the end of the calendar year from when the tax was due (2010 personal incomes were due on April 15, 2011, making three years from the end of the calendar year December 31, 2014), as generally required under NMSA 1978, Section 7-1-18 (A) (2013). However, under NMSA 1978, Section 7-1-18 (D) (2013), the Department has six years from the end of the calendar year to assess a taxpayer when the tax liability was underreported by more than 25%. Taxpayers' errors in this case related to the treatment of the state and local income under the itemized deduction resulted in underreporting their tax liability by more than 25% (they underreported by approximately 46%). Consequently, the Department's assessment made within four-years of the end of the calendar when the tax was due was timely under the relevant six-year statute of limitation articulated by Section 7-1-18 (D).

Part of Mr. Rivera's frustration in this case stems from what he believed was an unnecessary delay in assessing Taxpayers, resulting in additional accrual of interest and penalty. As just discussed, the Department timely assessed Taxpayers within the permissible statute of limitations.

Regarding 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 (2007) (italics for emphasis). 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. *See Marbob Energy Corp. v. N.M. Oil Conservation Comm'n*, 2009-NMSC-013, ¶22, 146 N.M. 24.

Turning to penalty, the Department has no basis to abate civil negligence penalty under NMSA 1978, Section 7-1-69 (2007) in this case. When a taxpayer fails to pay taxes due to the State because of negligence or disregard of rules and regulations, but without intent to evade or defeat a tax, by its use of the word “shall”, Section 7-1-69 requires that civil penalty be added to the assessment. As discussed above, the statute’s use of the word “shall” makes the imposition of penalty mandatory in all instances where a taxpayer’s actions or inactions meets the legal definition of “negligence.” Taxpayers erroneously believed New Mexico adopted the federal treatment of state and local income under the itemized deduction, resulting in the underreporting of New Mexico personal income tax. Although certainly unintentional, this erroneous belief and inadvertent error meets the definition of civil negligence subject to civil penalty under Regulation 3.1.11.10 (C) NMAC. *See El Centro Villa Nursing Center v. Taxation and Revenue Department*, 1989-NMCA-070, 108 N.M. 795 (inadvertent error constitutes civil negligence). Taxpayers’ protest is denied and Taxpayers owe the assessed amount.

CONCLUSIONS OF LAW

A. Taxpayers filed a timely, written protest to the assessment. Jurisdiction lies over the parties and the subject matter of this protest. The hearing was timely set and held in compliance with NMSA 1978, Section 7-1-24.1 (A) (2013).

B. Under NMSA 1978, Section 7-1-17 (2007), the assessment is presumed correct.

Taxpayers did not overcome this presumption.

C. Taxpayers failure to add back in the amount of state and local taxes claimed on the federal itemized deduction, as required by NMSA 1978, Section 7-2-2 (N) (2) (2010), caused the discrepancy that led to the Department's assessment.

D. The Department's assessment was timely made under NMSA 1978, Section 7-1-18 (D) (2013) because Taxpayers underreported their tax liability by more than 25% that year.

E. Under NMSA 1978, Section 7-1-67 (2007), Taxpayers are liable for accrued interest under the assessment. Interest continues to accrue until the tax principal is satisfied.

F. Under NMSA 1978, Section 7-1-69 (2007), Taxpayers are liable for civil negligence penalty under the negligence definition found under Regulation 3.1.11.10 (C) NMAC.

For the foregoing reasons, Taxpayers' protest **IS DENIED**. As of the date of hearing, Taxpayers owed \$483.00 in personal income tax, \$96.60 in penalty, and \$63.00 in interest for a total tax liability of \$642.60. Interest continues to accrue until the tax principal is satisfied.

DATED: August 4, 2015.

Brian VanDenzen
Interim Chief Hearing Officer
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