

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

**IN THE MATTER OF THE PROTEST
OF LINDA LOMBARDO TO THE INTEREST
ASSESSED UNDER LETTER ID L2123112960**

No. 06-15

DECISION AND ORDER

A formal hearing on the above-referenced protest was held on September 12, 2006, before Margaret B. Alcock, Hearing Officer. The Taxation and Revenue Department (“Department”) was represented by Susanne Roubidoux, Special Assistant Attorney General. Linda Lombardo (“Taxpayer”) was represented by John Provost, certified public accountant. 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 at the beginning of the 2003 tax year.
2. In October 2003, the Taxpayer changed her residence to the State of Arizona.
3. The Taxpayer filed a 2003 Arizona “Part-Year Resident Personal Income Tax Return,” reporting Arizona adjusted gross income of \$59,971 and Arizona taxable income of \$55,319, resulting in an Arizona tax liability of \$1,953.
4. On October 15, 2004, the Taxpayer filed a 2003 New Mexico income tax return as a part-year resident and claimed a credit for taxes paid to Arizona in the amount of \$4,335.
5. The Department’s instructions to the 2003 PIT-ADJ Schedule to New Mexico’s 2003 personal income tax form PIT-1 advises taxpayers as follows:

A resident of New Mexico who must pay tax to another state on income that is also taxable in New Mexico may take a credit against New Mexico tax for tax owed to the other state.

This credit is for tax that another state imposes on any portion of income that by law is included in New Mexico net income.... If the specific item of income is not subject to taxation in both states, no credit is available. The credit may not be more than the New Mexico tax liability on line 15 of the Form PIT-1, or more than 5-1/2% of the income taxable in the other state. Attach a copy of the complete income tax return(s) from the other state(s). See the worksheet on this page.

6. The instructions also contain a “Worksheet for Computation of Allowable Credit For Taxes Paid to Other States by New Mexico Residents.” Line 1 of the worksheet states: “Enter amount of tax paid to the other state.” Line 2 states: “Enter taxable income on which the tax on line 1 was figured.” Line 3 instructs taxpayers to divide Line 1 by Line 2 to obtain the average effective tax rate on other state income. Line 4 directs taxpayers to enter the smaller of Line 3 or 5½%, which is the maximum that can be claimed against New Mexico taxes.

7. When completing the worksheet, Mr. Provost incorrectly entered Arizona gross income on Line 2 instead of Arizona taxable income. As a result of this error, the effective tax rate entered on Lines 3 and 4 of the worksheet was also incorrect.

8. Line 5 of the worksheet states: “Enter that portion of income that is subject to tax in both New Mexico and the other state.” Line 6 then instructs taxpayers to multiply Line 5 by the effective tax rate calculated on Line 4.

9. Mr. Provost entered the figure of \$132,972 on Line 5, which represented the Taxpayer’s capital gain from the sale of her New Mexico residence, and applied the effective tax rate he had calculated on Line 4, resulting in a claimed credit of \$4,335.

10. In completing Line 5 of the worksheet, Mr. Provost interpreted the phrase “income that is subject to tax in both New Mexico and the other state” to mean the amount of income reported on both states’ returns, rather than the amount of income actually taxed by both states. As a result, the \$4,335 credit the Taxpayer claimed exceeded the \$1,953 of tax she actually paid to Arizona.

11. Upon receipt of the Taxpayer’s return, the Department determined that she had incorrectly filed as a part-year resident. Because the Taxpayer was physically present in New Mexico for more than 185 days, she was a full-year resident under NMSA 1978, § 7-2-2(S) and was required to report all of her income as New Mexico income on her 2003 return.¹

12. The Department recomputed the Taxpayer’s New Mexico income tax and also disallowed the credit claimed for taxes paid to Arizona because the Taxpayer failed to provide a copy of her Arizona return as required by the Department’s instructions.

13. On October 27, 2004, the Department assessed the Taxpayer for additional New Mexico income tax in the amount of \$4,005, plus penalty and interest.

14. On November 22, 2004, Mr. Provost sent the Department a letter stating that the Taxpayer “is in disagreement with your re-computation notice” and enclosing a copy of the Taxpayer’s 2003 Arizona tax return.

15. On December 14, 2004, the Department sent a letter to Mr. Provost notifying him as follows: “After reviewing the Arizona return, the maximum credit allowed is the amount of

¹ At the administrative hearing, John Provost claimed that he made a mistake in filling out the dates of the Taxpayer’s New Mexico residency and that she was not present in the state for more than 185 days. Mr. Provost’s unsupported assertions are not sufficient to overcome the evidence of residency set out on the 2003 New Mexico and Arizona income tax returns filed by the Taxpayer.

\$1,953.00 shown on the Arizona return. The tax liability for New Mexico was decreased to \$2,052.00 plus penalty of \$469.28 and interest of \$776.78 that is still due.”

16. The Taxpayer and her accountant disagreed with the Department’s position that the credit allowed on Line 17 of the 2003 PIT-ADJ Schedule, which reads: “Credit for taxes paid to another state,” was limited to the amount of tax actually *paid* to another state.

17. Between January and September 2005, Mr. Provost wrote, telephoned and met with a number of Department employees in an attempt to convince them that the Taxpayer was entitled to claim a tax credit of \$4,335, even though the tax she owed—and paid—to Arizona was only \$1,953.

18. In September 2005, a Department employee provided Mr. Provost with a copy of NMSA 1978, § 7-2-13 of the New Mexico Income Tax Act, which states that New Mexico residents who owe tax to another state on income that is also included in New Mexico net income are entitled to “a credit against the tax due this state in the amount of the tax paid the other state with respect to income that is required to be either allocated or apportioned to New Mexico.”

19. After reading the statute, Mr. Provost conceded that the credit was limited to the \$1,953 of tax paid to Arizona, and on October 13, 2005, the Taxpayer paid the amount of tax principal assessed by the Department. The Taxpayer continued to dispute the assessment of penalty and interest.

20. The Department subsequently abated the penalty, leaving the Taxpayer’s liability for interest as the only issue in dispute.

DISCUSSION

John Provost, the Taxpayer's certified public accountant, concedes that the Taxpayer is liable for payment of interest that accrued between April 2004 (the original due date of her 2003 personal income taxes) and December 2004 (the date the Department notified her that the credit for taxes paid to Arizona was limited to the amount of taxes actually paid). Mr. Provost argues, however, that the Department is responsible for the accrual of interest between January and October 2005 and that the Taxpayer should not be required to pay this additional interest. As grounds for his argument, Mr. Provost maintains that the computation worksheet set out in the Department's 2003 instructions led him to the wrong result and that for nine months he was unable to obtain an explanation of the Department's position concerning taxes paid to other states. The evidence does not support Mr. Provost's assertions.

Department Instructions. On December 14, 2004, the Department notified the Taxpayer that: "After reviewing the Arizona return, the maximum credit allowed is the amount of \$1,953.00 shown on the Arizona return." This clearly states the Department's position that the credit the Taxpayer could claim on Line 17 of New Mexico's PIT-ADJ Schedule was limited to the amount of tax she actually paid to Arizona.

Mr. Provost testified that he needed additional information from the Department because the worksheet in the instructions indicated the Taxpayer could claim a credit in excess of the tax paid to another state. The evidence shows, however, that the error was not in the worksheet itself but in Mr. Provost's completion of the worksheet. First, Mr. Provost incorrectly entered Arizona gross income on Line 2 instead of Arizona *taxable* income. As a result, the effective tax rate entered on Lines 3 and 4 of the worksheet was also incorrect. When completing Line 5 of the

worksheet, Mr. Provost interpreted the phrase “income that is subject to tax in both New Mexico and the other state” to mean the amount of income reported on both states’ returns, rather than the amount of income actually taxed by both states. In addition, he treated the Taxpayer as a part-year resident instead of a full-year resident, which affected the amount of income attributed to New Mexico. Due to this combination of errors, Mr. Provost came up with a credit of \$4,335 instead of the \$1,953 of tax his client actually paid to Arizona.

Even assuming that the phrase “income that is subject to tax” on Line 5 of the worksheet is ambiguous, the remaining text of the instructions to PIT-ADJ should have alerted Mr. Provost to the fact that the credit cannot exceed the amount of tax paid. For example, the instructions state that a New Mexico resident “who must pay tax to another state on income that is also taxable in New Mexico may take a credit against New Mexico tax *for tax owed* to the other state” and that “[t]his credit is *for tax that another state imposes* on any portion of income that by law is included in New Mexico net income.” (emphasis added). The title of the worksheet itself reads: “Worksheet for Computation of Allowable Credit for *Taxes Paid to Other States* by New Mexico Residents.” (emphasis added). Finally, Line 17 of the PIT-ADJ Schedule identifies the amount to be entered as a “Credit *for taxes paid* to another state.” (emphasis added). There is simply no support for Mr. Provost’s contention that “no where in the published instructions ... does it state the credit is limited to the actual taxes paid the other state.” (See, October 18, 2005 letter to the Department).

There was a ten-month delay between the date Mr. Provost received the Department’s December 14, 2004 letter and the date the Taxpayer paid the additional tax due on her 2003 New Mexico personal income taxes. This delay cannot be attributed to the Department’s failure to

explain its position, but to Mr. Provost's unwillingness to accept that position. Had Mr. Provost taken the time to carefully re-read the Department's instructions, or the section of the Income Tax Act governing the credit for taxes paid to other states, he could easily have verified the Department's advice. NMSA 1978, § 7-2-13 clearly states that upon filing satisfactory evidence of the payment of tax to another state, a taxpayer may "receive a credit against the tax due this state *in the amount of the tax paid the other state* with respect to income that is required to be either allocated or apportioned to New Mexico." (emphasis added). Having been a certified public accountant for over ten years, Mr. Provost should have been able to locate a copy of the New Mexico Income Tax Act, which is readily available in any library as well as on the Department's web site.

Imposition of Interest. NMSA 1978, § 7-1-67 governs the imposition of interest on late payments of tax and provides, in pertinent part:

A. If a tax imposed is not paid on or before the day on which it becomes due, interest *shall be paid* to the state on that amount from the first day following the day on which the tax becomes due, without regard to any extension of time or installment agreement, until it is paid.... (emphasis added).

The legislature's use of the word "shall" indicates that the provisions of the statute are mandatory rather than discretionary. *State v. Lujan*, 90 N.M. 103, 105, 560 P.2d 167, 169 (1977). *See also*, NMSA 1978, § 12-2A-4(A) of the Uniform Statute and Rule Construction Act (the words "shall" and "must" express a duty, obligation, requirement or condition precedent). With limited exceptions that do not apply here, the New Mexico legislature has directed the Department to assess interest whenever taxes are not timely paid. Even taxpayers who obtain a formal extension

of time to pay tax are liable for interest from the original due date of the tax to the date payment is made. *See*, NMSA 1978, § 7-1-13(E).

The assessment of interest is intended to compensate the state for the time value of unpaid revenues. In this case, the Taxpayer failed to properly report and pay her 2003 personal income taxes. If those taxes had been computed correctly, the State of New Mexico would have received an additional \$2,052 in tax revenues in April 2004. As a result of her errors (or the errors of her accountant) the Taxpayer—rather than the state—had the use of this money for the period between the original due date and the date the taxes were paid in October 2005.

Finally, it must be recognized that New Mexico has a self-reporting tax system, and the law places the duty on taxpayers to accurately determine and pay their taxes by the statutory due date. NMSA 1978, § 7-1-13; *See also*, *Tiffany Construction Co. v. Bureau of Revenue*, 90 N.M. 16, 17, 558 P.2d 1155, 1156 (Ct. App. 1976), *cert. denied*, 90 N.M. 255, 561 P.2d 1348 (1977). While a taxpayer has the right to dispute her liability for any tax, this does not stay the accrual of interest in the event the tax is ultimately found to be due and owing to the state. NMSA 1978, § 7-1-67 clearly states that interest accrues “from the first day following the day on which the tax becomes due...until it is paid.” In this case, interest on the Taxpayer’s late payment of 2003 personal income taxes is due for the period beginning on April 15, 2004, the original due date of the tax, and ending on October 13, 2005, the date the additional tax was paid.

CONCLUSIONS OF LAW

A. The Taxpayer filed a timely, written protest to the assessment issued under Letter ID L2123112960, and jurisdiction lies over the parties and the subject matter of this protest.

B. Pursuant to NMSA 1978, § 7-1-67(A), the Taxpayer is liable for payment of the interest that accrued from the first day following the day on which her 2003 personal income tax became due in April 2004 until the date the underreported tax was paid in October 2005.

C. There is no legal basis for staying the accrual of interest against the Taxpayer based on any action or inaction of the Department.

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

DATED September 14, 2006.