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

IN THE MATTER OF THE PROTEST OF
JOY ODOM, **No. 11-04**
TO ASSESSMENTS ISSUED UNDER
ID NOS. L0473297280 and L0785941888

DECISION AND ORDER

A formal hearing on the above-referenced protest was held December 28, 2010, before Dee Dee Hoxie, Hearing Officer. The Taxation and Revenue Department ("Department") was represented by Ms. Amy Chavez-Romero, Special Assistant Attorney General. Ms. Andrea Umpleby, Auditor, also appeared on behalf of the Department. Ms. Joy Odom ("Taxpayer") appeared for the hearing by telephone and represented herself. The parties had filed a joint motion for the Taxpayer to appear by phone, which was granted. The Hearing Officer took notice of all documents in the administrative file. TRD #1 through #32 were admitted at the hearing. Taxpayer "A" through "E" were admitted at the hearing. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. Taxpayer was a New Mexico resident in 2005 and 2006.
2. Taxpayer received retirement income distributions in 2005 and 2006.
3. Taxpayer failed to file personal income tax with the Department for 2005 and 2006.
4. The Department determined that Taxpayer was a non-filer on personal income tax for 2005 and 2006 through her federal tax return, which was reported to the Department through the tape match system.

5. On April 25, 2008, the Department assessed the Taxpayer for personal income tax, penalty, and interest for the tax period ending on December 31, 2005.

6. On October 27, 2008, the Department assessed the Taxpayer for personal income tax, penalty, and interest for the tax period ending on December 31, 2006.

7. On May 2, 2008, September 27, 2008 and October 28, 2008, Taxpayer filed formal protest letters regarding the assessments.

8. On October 21, 2010, the Department filed a Request for Hearing asking that the Taxpayer's protests be scheduled for a formal administrative hearing.

9. Taxpayer argues that her income was from her retirement through the state of Texas, that she never worked in New Mexico, and that her retirement income is not subject to New Mexico tax.

DISCUSSION

The issue to be decided is whether the Taxpayer is liable for personal income tax, penalty, and interest for the tax periods ending in December 2005 and December 2006, due to her failure to file personal income tax returns on distributions from her retirement account in Texas.

Burden of Proof.

Assessments by the Department are presumed to be correct. *See* NMSA 1978, § 7-1-17. Tax includes, by definition, the amount of tax principal imposed and, unless the context otherwise requires, "the amount of any interest or civil penalty relating thereto." NMSA 1978, § 7-1-3. *See also, El Centro Villa Nursing Center v. Taxation and Revenue Department*, 108 N.M. 795, 779 P.2d 982 (Ct. App. 1989). Therefore, 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 she is not liable for the tax and is entitled to an abatement of penalty and interest.

Personal Income Tax on Retirement Income.

Taxpayer argues that only Texas and the federal government may tax the distributions on her retirement income because the account is maintained by the state of Texas and because she earned the income contributed to the account while she was working in Texas. Taxpayer argues that New Mexico may only tax wages earned from work done in New Mexico and that she never worked in New Mexico.

The Department argues that the state of residence has the right to tax a person who receives retirement distributions, regardless of where the person worked when contributing to the retirement plan.

The State imposes a tax upon the net income of every person who resides within New Mexico. *See* NMSA 1978, § 7-2-3 (1981). Net income is based in part on federal adjusted gross income. *See* NMSA 1978, § 7-2-2 (N) (2007) (the 2003 version would have been in effect at the time of Taxpayer's liabilities, but the substance of this section at that time was essentially the same as the current version). Some income may be taxable both in New Mexico and in another state. *See* NMSA 1978, § 7-2-11 (2001) (allowing allocation and apportionment of tax on income that is taxable in New Mexico as well as in another state). However, some types of income must be allocated solely to New Mexico, regardless of the source of the income. "Retirement income of a resident is allocable to New Mexico, regardless of the source of the retirement income, where it is paid from or whether the resident was a resident of New Mexico at the time of the employment which gave rise to the income." 3.3.11.13 (B) NMAC (2000). The regulation complies with federal law which prohibits any state from imposing an income tax on the retirement income of an individual who is not a resident of that state. *See* 4 U.S.C. § 114. A state may only impose an income tax on retirement income of its residents. *See id.*

States have long had the right to tax the income of their residents, including income attributable to activities in other states. *See Shaffer v. Carter*, 252 U.S. 37, 51 (1919) (holding that states have wide latitude to tax their own people). *See also Lawrence v. State Tax Commission of Mississippi*, 286 U.S. 276 (1932) (upholding a state's right to tax a resident on income earned in another state). Taxpayer argues that she should not be taxed by New Mexico merely because she resides there. However, it is a long-standing principle that "domicile in itself establishes a basis for taxation." *Id.* at 279. Taxpayer argues that New Mexico is taxing Texas because the retirement account is maintained by Texas. New Mexico tax on retirement income falls on the taxpayer, not the pension fund, when the funds are distributed to the taxpayer and the taxpayer is a resident of New Mexico. *See Alarid v. Secretary of NM Dep't. of Taxation and Revenue*, 118 N.M. 23, 28, 878 P.2d 341, 346 (Ct. App. 1994). The vast majority of New Mexico residents who have retirement income are subject to New Mexico personal income tax. *See id.* at 29.

Taxpayer was a resident of New Mexico in 2005 and 2006 when she received income from distributions from her retirement plan. New Mexico has the right to impose income tax on the total amount of those retirement distributions.

Amount of Tax.

Taxpayer disputes the amount of tax liability claimed by the State. Taxpayer argues that her federal returns, Taxpayer "A" and "B", show that her federal adjusted gross income (AGI) is less than the amount that the Department used in its calculations. Ms. Umpleby explained that the Department used the AGI amount that was provided by the IRS. Ms. Umpleby also explained that the discrepancy occurred because the Taxpayer excluded the total amount of her social security benefits from the taxable amount on her federal return. However, Ms. Umpleby

used the federal worksheet on social security benefits, and completed it using the Taxpayer's information in TRD #8 and #14. The worksheet indicated that a part of the Taxpayer's social security benefits were taxable, and the amount on the worksheet resulted in a total AGI that matched the amount that the IRS had also reported to the Department in TRD #6B and #12B.

The Taxpayer declined to explain how she did the worksheet and arrived at the conclusion that none of her social security benefits were taxable. The Taxpayer claimed that the information on the worksheet was her business and no one else's. The Taxpayer failed to overcome the presumption of correctness on the amount of the tax owed.

Assessment of Penalty.

Taxpayer argues that the Department should be precluded from collecting penalty and interest on the personal income tax for 2005 and 2006, because it never notified her that she would owe personal income tax on the distributions and should have notified her of her obligation in a timelier manner. Taxpayer called the Department when she moved to New Mexico and inquired whether she would have to pay personal income tax on her retirement income. Taxpayer was told that she would be sent information, but she never received anything from the Department. Taxpayer took the lack of follow-up information to mean that she did not owe personal income tax.

A taxpayer's lack of knowledge or erroneous belief that the taxpayer did not owe tax is considered to be negligence for purposes of assessment of penalty. *See Tiffany Const. Co., Inc. v. Bureau of Revenue*, 90 N.M. 16, 558 P.2d 1155 (Ct. App. 1976). Therefore, the penalty was properly assessed.

Computation of Penalty.

On both of the assessments issued in this matter, the Department seeks to impose a penalty of up to 20% under NMSA 1978, § 7-1-69 (2008). The assessments were issued for taxes due in 2006 and 2007 for the 2005 and 2006 tax years, respectively. The applicable penalty statute in effect for both the 2005 and 2006 tax years was capped at a maximum penalty of 10%. *See* NMSA 1978, § 7-1-69 (2003). At a maximum penalty not to exceed 10%, the penalty provision had been exhausted for both the 2005 and 2006 tax years before the January 1, 2008 effective date of NMSA 1978, Section 7-1-69 (2008). Ms. Umpleby testified that the Department had assessed a 20% cap because the tax was still outstanding after the effective date of the 2008 amendment and pointed out on TRD #9 and #15 that additional penalty was added after the effective date in 2008. Without evidence of legislative intent for retroactive application of NMSA 1978, Section 7-1-69 (2008), the outstanding tax due for tax years 2005 and 2006 were subject to a penalty "not to exceed" 10% pursuant to NMSA 1978, Section 7-1-69 (2003) because that was the provision in effect at the time the tax was due. *See Kewanee Industries, Inc. v. Reese*, 114 N.M. 784, 845 P.2d 1238 (1993) (holding that a modified penalty regulation would not apply retroactively when the regulation was enacted after the applicable tax year).

Assessment of Interest.

Interest "shall be paid" on taxes that are not paid on or before the date on which the tax is due. NMSA 1978, § 7-1-67 (A). The word "shall" indicates that the assessment of interest is mandatory, not discretionary. *See State v. Lujan*, 90 N.M. 103, 105, 560 P.2d 167, 169 (1977). The assessment of interest is not designed to punish taxpayers, but to compensate the state for the time value of unpaid revenues. Because the personal income tax was not paid when it was due, interest was properly assessed.

Timeliness of Assessment.

The Department has seven years from the end of the year in which the tax is due to make an assessment when the taxpayer failed to file any return. *See* NMSA 1978, § 7-1-18 (C). Although Taxpayer feels that the Department should have known that she owed the liability earlier, the statute governs the timeliness of an assessment. Taxpayer was assessed in 2008 for the 2005 and 2006 tax years. Therefore, the assessments were made in a timely manner. *See id.*

CONCLUSIONS OF LAW

1. Taxpayer filed a timely written protest to the Notice of Assessment of 2005 and 2006 personal income taxes issued under respective Letter ID numbers L0473297280 and L0785941888, and jurisdiction lies over the parties and the subject matter of this protest.

2. Taxpayer was properly assessed for personal income tax and interest for the 2005 and 2006 tax years.

3. The assessment of penalty for the 2005 and 2006 tax years was appropriate. However, the computation of penalty was incorrect. Penalty is capped at an amount not to exceed 10%. The amount of any penalty assessed in excess of the 10% cap is hereby abated.

For the foregoing reasons, the Taxpayer's protest **is GRANTED IN PART AND DENIED IN PART**.

DATED: February 10, 2011.