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

IN THE MATTER OF THE PROTEST OF
THOMAS J. NAGLE **No. 11-21**
TO ASSESSMENT ISSUED UNDER LETTER
ID NO. L0999557184

DECISION AND ORDER

A formal hearing on the above-referenced protest was held on September 13, 2011, before Monica Ontiveros, Hearing Officer. The Taxation and Revenue Department ("Department") was represented by Peter Breen, attorney for the Department. Mr. Thomas Dillon appeared and testified as a witness for the Department. Mr. Thomas J. Nagle ("Taxpayer") appeared at the appointed time. The Department presented no exhibits and Taxpayer presented Exhibits 1 and 2 which were admitted into the record. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. Taxpayer was married in 2006. He and his former wife, Gayle M. Nagle, failed to file a personal income tax return by April 16, 2007 for tax year 2006.

2. In 2006, Taxpayer was employed by Southern Wine & Spirits located in Albuquerque, New Mexico.

3. During the tax period of 2006, Taxpayer was an employee receiving a salary from Southern Wine & Spirits.

4. Ms. Nagle was employed on an hourly part time basis by Bernalillo County during the tax period of 2006. Her hours fluctuated while employed by Bernalillo County.

5. The Department assessed Taxpayer on March 29, 2010 in the amount of $2,516.00 in principal personal income tax, $503.20 in penalty and $548.47 in interest.

6. On April 21, 2010, Taxpayer filed a protest to the assessment.

7. On April 23, 2010, the Department acknowledged the protest.

8. The Department requested a hearing in this matter on July 16, 2010.

9. On July 21, 2010, the Hearings Bureau mailed a Notice of Administrative Hearing in this matter setting the hearing for March 1, 2011.

10. Taxpayer requested a continuance in this matter on February 25, 2011 and the matter was reset for September 13, 2011.

11. The Department's assessment was based on a tape match in which wage information was provided to the Department from the Department of Labor. The wage information did not include how much state income tax was withheld from the wages.

12. Taxpayer provided the Department with a wage statement or a pay stub through pay period December 15, 2006 indicating that his year-to-date state income tax withholding was $902.75.

13. The Department provided Taxpayer with a credit of $903.75 in withholding tax.

14. Mr. Dillon testified that after the adjustment, the amount of personal income principal tax due was $1,613.25, plus penalty and interest.

15. On August 30, 2011, Taxpayer filed a return for tax year 2006. The 2006 return is signed only by Taxpayer and not by Ms. Nagle.

16. At the time of the assessment, the Department used an amount on line 8, itemized deductions, that was different than the amount Taxpayer used on his filed 2006 personal income tax return.

17. The Department was unaware that Taxpayer had filed a 2006 return until the hearing. It was given an opportunity to review the return at the hearing.

18. At the hearing, the Department agreed to the amount of tax due on line 18 on the 2006 personal income tax return, or $1,725.00, less the withholding amount of $903.75.

19. At the hearing the Department agreed to all the amounts on the 2006 return except for the amount on line 20, or $1,146.00, the amount of New Mexico income tax claimed to be withheld by Taxpayer.

20. Since the Department agreed to the amount of tax due, and it had agreed to the amount of withholding tax credit of $903.75, the amount of principal income tax due claimed by the Department was $1,725.00 less a credit of $903.75 or $821.25.

21. Taxpayer argued that the amount of principal income tax due was $579.00 or the amount shown on the 2006 return.

22. The amount in dispute is $242.25, or $39.25 in withholding tax for Taxpayer and $203.00 in withholding tax for Mrs. Nagle.

23. The paychecks that Taxpayer received were "equal" and he earned the same salary each month during tax year 2006.

24. In 2007, Taxpayer separated from his wife, Gayle M. Nagle. They divorced sometime in February 2009.

25. The W-2s for both Taxpayer and Ms. Nagle could not be found by Taxpayer.

26. No W-2s for Ms. Nagle or Taxpayer were provided to the Department or at the hearing.

27. Taxpayer is liable for payment of the 2006 personal income tax liability.

DISCUSSION

The issue to be determined is whether Taxpayer provided sufficient documents or testimony to support his contention that the correct combined amount of tax withheld from his income and his former wife's income was $1,146.00 or the amount of withholding shown on the filed 2006 return. There are no legal issues in dispute. The Department contends that Taxpayer owes income tax of $821.25 (principal only) and Taxpayer claims that he owes income tax of $579.00 in principal. The amount in dispute is $242.25, plus penalty and interest. At the hearing Taxpayer did not dispute that he owed penalty and interest on the amount of principal tax due of $579.00.

Burden of Proof.

Section 7-1-17(C) provides that any assessment of taxes made by the Department is presumed to be correct. NMSA 1978, Section 7-1-17(C)(2007). Where an exemption or deduction from tax is claimed, the statute must be construed strictly in favor of the taxing authority, the right to the exemption or deduction must be clearly and unambiguously expressed in the statute, and the right must be clearly established by the taxpayer. *Wing Pawn Shop v. Taxation and Revenue Department*, 111 N.M. 735, 740, 809 P.2d 649, 654 (Ct. App. 1991). Accordingly, it is Taxpayer's burden to present evidence and legal argument to show that it is entitled to an abatement, in full or in part, of the assessment issued against it. When a taxpayer presents evidence sufficient to rebut the presumption, the burden shifts to the Department to show that the assessment is correct. *See MPC Ltd. v. N.M. Taxation and Revenue Dep't.*, 2003-NMCA-021, ¶ 13, 133 N.M. 217, 62 P.3d 308.

Amount of Withholding Tax.

Payment of withholding taxes is governed by the Withholding Tax Act, Sections 7-3-1, *et seq.*, NMSA 1978. Section 7-3-9 is the specific statute which requires the Department to credit against any state income tax liability for the taxable year the amount of tax withheld. During the period at issue, that section read as follows:

> The amount of tax deducted and withheld under the provisions of the Withholding Tax Act [Chapter 7, Article 3 NMSA 1978] during the taxable year shall be credited against any state income tax liability for that taxable year.

NMSA 1978, Section 7-3-9 (1990). The withheld amount is treated as a collected tax. NMSA 1978, Section 7-3-4 (1996). The Department cannot collect the tax from the employee a second time, even when the employer has failed to pay over the amount of tax withheld. In this case, there is no assertion by the Department that the employers of both Taxpayer and Ms. Nagle remitted the withholding income tax to the State of New Mexico. The only issue is that the Department does not know the amount of the withholding tax paid.

In 2006, Taxpayer was employed on a full time basis by Southern Wine & Spirits in Albuquerque, New Mexico and Ms. Nagle was employed on a part time basis by Bernalillo County. During the tax year 2006, Taxpayer was married to Gayle M. Nagle. Taxpayer credibly testified that sometime in 2007, he became separated from Ms. Nagle and he left the residence. As a consequence of the separation, the 2006 tax return was not filed by either Ms. Nagle or Taxpayer on April 16, 2007 (April 15, 2007 was a Sunday) as required by NMSA 1978, Section 7-2-12(A) (2003). This matter rests primarily on what amount was withheld from the incomes of Taxpayer

and Ms. Nagle.

In explaining the basis of the assessment, Mr. Dillon testified that Taxpayer and his wife were nonfilers for tax year 2006. The Department received information from the Department of Labor which reported that Taxpayer and his wife had wage income for tax year 2006. The Department used a zero withholding when calculating the amount of income tax due. Without information on the amount of state income tax that had been withheld, the Department issued an assessment based on a zero amount of withholding amount.

Sometime in 2011 prior to the hearing, Taxpayer found a wage statement for 2006. The wage statement that Taxpayer found had a pay period ending December 15, 2006 and not December 31, 2006. (For Taxpayer's withholding, the last pay period would represent a credit of $39.25. See Exhibit 2). On this wage statement, the amount withheld from Taxpayer's income was $902.75. Exhibit 2. Mr. Dillon provided an adjustment or credit in the amount of $903.75 against the amount of income tax calculated based on the income reported by the Department. (There is a $1.00 difference in the two amounts.) Mr. Dillon testified that after this adjustment, the total income tax due after this adjustment was $1,613.25, plus penalty and interest.

At the hearing, Taxpayer testified that he filed an income tax return for tax year 2006 on August 30, 2011. He credibly testified that in filing the return for 2006 in August 2011, he called the Internal Revenue Service to determine what amount was reported as wage income for both he and his former wife. He used this amount to prepare his federal return and his state return. The Department was unaware that Taxpayer had filed a return and it was given an opportunity to review the return. The return had an income tax due of $1,725.00. The Department did not

contest the wage amount listed on the return, line 6, or the itemized deduction amount listed on line 8. Exhibit 1. The Department further agreed that the amount of tax due was $1,725.00. Using the numbers that the Department agreed to, the amount of income tax due was $1,725.00 less $903.75, for a total tax due of $821.25. Mr. Dillon testified that he thought the withholding amount may be incorrect but without a wage statement for the last pay period or a W-2 for Taxpayer and without a wage statement or W-2 for Ms. Nagle, he could not make any further adjustments. Taxpayer argued that he was unwilling to get a W-2 or wage statement from his former wife and he was unwilling to ask his employer for the final wage statement showing year-to-date of withholding amounts.

Taxpayer argued that the Department did not need a W-2 or a wage statement for the last pay period for himself or a W-2 or wage statement for Ms. Nagle because it should be able to extrapolate the withholding amount using a percentage of 1.5% applied to the income. The Department did not argue that this was an impermissible method of calculating the amount of income tax withheld. It took the position that it simply did not know the amount of tax withheld.

Mr. Dillon testified that he was unable to retrieve information related to the amount of tax withheld to credit the Taxpayer's income tax liability. It was not made clear at the hearing whether employers are filing a statement with the Department pursuant to Section 7-3-7(A) (1990). Section 7-3-7(A) requires the employers to file with the Department the "total compensation paid the employee and the total amount of tax withheld for the calendar year or portion of a calendar year if the employee has worked less than a full calendar year."

Taxpayer's Withholding.

The only issue is whether Taxpayer rebutted the presumption of correctness that attached to the Department's assessment or whether he is entitled to receive a credit of $39.25, the amount of withholding for Taxpayer for the last pay period of 2006. Taxpayer presented his wage statement through December 15, 2006 and he testified that his paychecks were the same or "equal." Taxpayer's testimony was that he received the same salary every pay period and his employer withheld the same amount of state income tax on his wages, which entitled him to an additional credit against the tax of $39.25. Taxpayer argued that he should be provided this credit against the tax because he worked the final pay period of December. Taxpayer credibly testified that he was unable to find the W-2s and the final wage statement for tax year 2006. He also testified that he did not want to ask his employer for a W-2 or a wage statement for 2006 because he did not want to explain that he was a nonfiler. The Department did not contradict these statements other than to argue that Taxpayer could not prove with certainty that he had withholding taken out for this final pay period.

In closing the Department speculated that Taxpayer received bonuses and therefore, the Department has no way of knowing what the amount of Taxpayer's withholding was. Taxpayer argued that his withholding would be higher had he received a bonus in 2006. The Hearing Officer reopened the testimony to ascertain whether Taxpayer had received any bonuses for 2006.

The evidence submitted is sufficient to rebut the presumption of correctness. Taxpayer provided a wage statement through December 15, 2006. Exhibit 2. He also provided testimony about the regularity of the withholding. The Hearings Bureau in the past has accepted evidence

other than W-2s or wage statements presented by the taxpayer as evidence of the amount of tax withheld. *See Hal M. Dean, Decision and Order No. 01-31.* The burden shifts to the Department to prove that Taxpayer is incorrect or made a false statement. *See MPC Ltd. v. N.M. Taxation and Revenue Dep't.*, 2003-NMCA-021, ¶ 13, 133 N.M. 217, 62 P.3d 308. Since there was no testimony or evidence presented by the Department, the Hearing Officer agrees with Taxpayer that he has proven with sufficient evidence that he should be credited $39.25 withholding income tax against his income tax liability.

Gayle M. Nagle's Withholding.

Taxpayer also argued that $203.00 was withheld from Ms. Nagle's income for 2006 tax year. To deduce this amount of withholding, Taxpayer used a 1.5% calculation based on the reported wages to the Internal Revenue Service. Ms. Nagle did not testify nor did Taxpayer present a W-2 or any wage statements supporting this assertion. Ms. Nagle was a part time employee, whose hours fluctuated and there was no testimony offered as to the number of exemptions claimed by her in 2006. While the Department did not dispute the percentage calculation used by Taxpayer, it took the position that Taxpayer did not present documents to support the $203.00 in withholding tax for Ms. Nagle.

Generally, Taxpayers "shall maintain books of account or other records in a manner that will permit the accurate computation of state taxes or provide information required by the statute under which he is required to keep records." NMSA 1978, Section 7-1-10(A)(2001). The Department's regulations provide that "(t)he adequacy or inadequacy of taxpayer records is a matter of fact to be determined by the secretary or secretary's delegate. Taxpayers have a duty to

provide the secretary or secretary's delegate, upon request, with books of account and other records upon which to establish a basis for taxation." Regulation 3.1.5.8(A) NMAC (2000).

Taxpayer argued that while he had been ordered by the Second Judicial District Court in the Divorce Decree to pay the 2006 New Mexico income tax liability, he had no way in which to request a copy of Ms. Nagle's W-2 or a copy of her wage statement. Taxpayer agreed that he had an obligation to report the income and file the 2006 return per the Divorce Decree. Taxpayer had a corresponding duty to prepare a return using correct withholding information from a W-2 or wage statement. Taxpayer should have requested a copy of Ms. Nagle's W-2 statement or a final wage statement indicating the amount of withholding from her salary. Since he was unwilling to request a wage statement or a W-2 from Ms. Nagle, a credit cannot be given for an amount that is not determinable. Again, a taxpayer is required to "maintain books of account or other records in a manner that will permit the accurate computation of state taxes or provide information required by the statute under which he is required to keep records." NMSA1978, Section 7-1-10(A)(2001).

In this case, Taxpayer failed to present sufficient evidence that $203.00 had been withheld from Ms. Nagle's income, and therefore Taxpayer failed to overcome the presumption of correctness to claim a credit in the amount or $203.00. (Taxpayer made an assumption that Ms. Nagle had to have had an amount withheld for tax year 2006. The amount of withholding is dependent on the number of exemption allowances the employees claim. See New Mexico Taxation and Revenue Department FYI-104).

Civil Penalty.

At the hearing, Taxpayer argued that he was not contesting the penalty. The Department

imposed a civil penalty of 20% under NMSA 1978, § 7-1-69 (2008) rather than under NMSA 1978 Section 7-1-69 (2003, prior to amendments through 2007), in effect prior to January 1, 2008. The Hearing Officer interprets Taxpayer's argument regarding penalty to be that Taxpayer is not contesting that he was negligent. (Taxpayer's original protest letter indicates that he was protesting the entire assessment.) The Taxpayer's Bill of Rights requires that an assessment not be "incorrect, erroneous, or illegal," therefore, the accuracy of the computation of total penalty amount assessed is an issue for consideration in this protest. NMSA 1978, Section 7-1-4.2 (2003). Even when a Taxpayer is liable for civil negligence penalty, as in here, a Taxpayer is not required to pay a miscalculated or incorrect amount of penalty. *See id.*

The Hearings Bureau has taken the position that if the year in which the tax is due predates the effective date of changes or prior to January 1, 2008, then while a taxpayer may be negligent, the Department may only apply a 10% penalty to the amount of tax owed. This interpretation of the statute is based on the only change in NMSA 1978 Section 7-1-69 (2003, prior to amendments through 2007), in effect prior to January 1, 2008, versus NMSA 1978, § 7-1-69 (2008), which was in effect January 1, 2008. The change in the statute represents an increase in the maximum possible penalty amount not to exceed an amount of 20% from the previous 10% maximum limit. Under both the previous version and the amended version of the penalty provision, the Department was to apply two percent per month penalty from the time the tax was due and not paid until the penalty reached its statutorily prescribed "not to exceed" limit of either 10% under the previous version (which effectively means a five-month period of time from the time the tax was due but not paid) or 20% under the amended version (which effectively means a ten-month period of time

from the time the tax was due but not paid). Under both the previous and amended versions of the penalty provision, the Legislature prohibits the Department from imposing any additional penalty beyond the "not to exceed" limit.

By arguing that a 20% amount should apply the Department is impermissibly retroactively applying the amended penalty provision to increase a previously reached "not to exceed" limit of 10% by an additional 10% under the amended penalty provision without clear legislative intent allowing it to do so. As the New Mexico Court of Appeals recently indicated, "a statute or regulation is considered **retroactive if it**…**affixes new disabilities to past transactions**." *Wood v. State Educ. Ret. Bd.*, 2010 N.M. App. LEXIS 134 (N.M. Ct. App. Nov. 10, 2010), citing *Coleman v. United Eng'rs & Constructors, Inc.*, 118 N.M. 47, 52, 878 P.2d 996, 1001 (1994), [bold for emphasis].

A statute may only be applied retroactively if there is a clear, unambiguous legislative intent to do so. *See Psomas v. Psomas*, 99 N.M. 606, 609, 661 P.2d 884, 887 (1982). Absent such clear intent for a retroactive application, a statute only applies prospectively. *See id.* The Department has never presented any evidence, nor does the plain language of the statute contain any evidence, that the Legislature intended NMSA 1978 Section 7-1-69 (2007) to apply retroactively to obligations that originated before the January 1, 2008 effective date of that revision. Given the Legislature's silence on the question of retroactivity of NMSA 1978 Section 7-1-69 (2007), case law suggests that the amended statute should only apply prospectively. *See Psomas*; *See also N.M. Elec. Serv. Co. v. Jones*, 80 N.M. 791, 793, 461 P.2d 924, 926 (Ct. Appl. 1969) ("where an ambiguity or doubt exists as to the meaning or applicability of a tax statute, it should be construed most strongly against

the taxing authority and in favor of those taxed"). Moreover, in a case closely on point, the New Mexico Supreme Court has also found that the Department may not retroactively apply a modified penalty regulation against a taxpayer for an obligation that predates the effective date of the modified regulation. *See Kewanee Industries, Inc. v. Reese*, 114 N.M. 784, 845 P.2d 1238 (1993).

In this case, the old penalty statute in effect at the time of the Taxpayer's failure to file and pay tax is the applicable penalty amount or 10%. Taxpayer's failure to file and pay tax the 10% penalty was applied at 2% for five months and fully applied by September 2007. After that date, under the old penalty statute, no further civil penalty could be imposed because of the not to exceed language of the statute, regardless if the tax still remained due. Consequently, since the maximum penalty amount had been reached in 2007, the Department is prohibited from applying 20% penalty to the amount due.

Interest.

Taxpayer conceded that he owed interest on the amount of principal income tax he owed. 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 principal amount of tax was not paid when it was due, interest was properly assessed.

CONCLUSIONS OF LAW

A. Thomas J. Nagle, Inc. filed a timely written protest to the principal, penalty and

interest assessed under Letter ID L0999557184, and jurisdiction lies over the party and the subject matter of this protest.

B. The amount of tax due for tax year 2006 is $1,725.00.

C. The amount of withholding income tax paid was $903.75, plus $39.25 or $943.00.

D. Mr. Nagle was negligent in not filing and paying his income tax for tax year 2006.

E. The amount of income tax due is $782.00, plus penalty at a rate to be calculated at no more than 10% of the principal amount of tax owed pursuant to NMSA 1978, Section 7-1-69 (2003), and interest.

F. Taxpayer was unable to either rebut the presumption or prove by a preponderance of the evidence that an additional amount of withholding income tax in the amount of $203.00 had been deducted from Ms. Nagle's income.

G. Interest should be applied to the principal amount of tax due in accordance with this Decision.

For the foregoing reasons, Thomas J. Nagle's protest is GRANTED IN PART AND DENIED IN PART.

DATED: September 18, 2011.