

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

**IN THE MATTER OF THE PROTEST OF
BENNY NEVAREZ
TO ASSESSMENT ISSUED UNDER LETTER
ID NO. L0225000064**

No. 11-30

DECISION AND ORDER

A hearing was held on the above captioned matter on November 18, 2011. Mr. Benny Nevarez (“Taxpayer”) appeared *pro se*. The Taxation and Revenue Department of the State of New Mexico (“Department”) was represented by Staff Attorney Ida M. Lujan. Protest Auditor Sylvia Sena appeared as a witness for the Department. In addition to the documents contained in the Administrative File articulated at the beginning of the hearing, Taxpayer Exhibits #1-3 and Department Exhibits A-G, as fully described in the Exhibit Cover Sheet, are admitted into the record. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. Taxpayer, a professional plumber, worked for 10-years as an employee of Pronto Plumbers, Inc (“Pronto Plumbers”) in Las Cruces/Mesilla Park, New Mexico.
2. In addition to his salary, Taxpayer was eligible to participate in Pronto Plumbers Profit Sharing Plan (“Profit Sharing Plan”).
3. While employed with Pronto Plumbers, Taxpayer vested in that Profit Sharing Plan.
4. At some point in 2001, Pronto Plumbers terminated Taxpayer’s employment.

5. In 2003, Taxpayer approached the owner of Pronto Plumbers, Mr. Thomas Levy, about withdrawing his distribution from the Profit Sharing Plan.

6. Mr. Levy provided Taxpayer with a packet of forms to prepare before any distributions from the Profit Sharing Plan could be made to Taxpayer. Taxpayer provided a copy of those forms into the record as Taxpayer Exhibits # 1.1-1.15.

7. Taxpayer brought the packet to Jackson Hewitt Tax Service to prepare the packet of materials needed to redeem his Profit Sharing Plan holdings.

8. On July 31, 2003, Pronto Plumbers informed Taxpayer that he was eligible for \$18,454.04 in distributions from the Profit Sharing Plan. However, that distribution would be subject to federal withholding taxes. [Taxpayer Exhibit 1.3]

9. Pronto Plumbers further informed Taxpayer that federal law required a federal withholding of 20%. [Taxpayer Exhibit 1.1]

10. Taxpayer Exhibits #1.1-1.15 do not indicate that Pronto Plumbers would withhold any amount of New Mexico income tax. Any reference to a withholding in those exhibits only comes in the context of federal withholdings.

11. On August 7, 2003, Pronto Plumbers issued a check from its Profit Sharing Plan trust account to Taxpayer in the amount of \$14,763.33, which mathematically equals the \$18,454.04 promised amount, less 20% in federal withholding taxes. [Taxpayer Exhibit #2]

12. On August 8, 2003, Pronto Plumbers issued a check from its Profit Sharing Plan trust account to Citizen's Bank in the amount of \$3,690.81 with a Federal Tax Deposit Coupon Form 8109-B attached. That amount equals the 20% in federal withholding taxes for Taxpayer's profit sharing distribution. [Taxpayer Exhibit #3]

13. There is no evidence that Pronto Plumbers made any New Mexico income tax withholdings on Taxpayer's distributions.

14. On April 9, 2004, Taxpayer filed his New Mexico personal income taxes. Taxpayer listed his federal adjusted gross income as \$31,337, an amount that did not include the \$18,454.04 in distributions from the Profit Sharing Plan. [Department Exhibit A]

15. As a result of the April 9, 2004 New Mexico personal income tax filing, Taxpayer received a \$393.00 income tax refund for tax year 2003.

16. Taxpayer redeemed that \$393.00 New Mexico 2003 personal income tax refund.

17. At some point thereafter, the Internal Revenue Service ("IRS") made a correction to Taxpayer's 2003 Adjusted Gross Income. As a result of this correction, Taxpayer's Federal Adjusted Gross Income was increased by \$21,457.00 to \$52,794.00. [Department Exhibit B]

18. This \$21,457.00 increase in Federal Adjusted Gross Income resulted from the \$18,454.04 distributions from the Profit Sharing Plan and \$3,003 in other unreported work income.

19. Taxpayer did not amend his 2003 New Mexico personal income tax to account for this corrected Federal Adjusted Gross Income.

20. As a result of the Department's information matching program with the IRS, the Department learned of a discrepancy between Taxpayer's corrected Federal Adjusted Gross Income of \$52,794 and the reported \$31,337 amount in Taxpayer's 2003 New Mexico personal income tax return.

21. On November 29, 2006 the Department sent Taxpayer notice of limited scope audit for personal income tax. [Department Exhibit B]

22. The Department, after considering the corrected Federal Adjusted Gross Income and accounting for the previously provided \$393.00 refund, determined that Taxpayer had a \$1,996.00 personal income tax liability for tax year 2003.

23. On January 29, 2007, the Department mailed Taxpayer a notice of potential assessment for personal income tax. [Department Exhibit C]

24. On March 7, 2007, the Department sent Taxpayer Notice of Assessment, Letter Id. No. L0225000064 for \$1,334.00 in personal income tax, \$133.40 in penalty (calculated to the maximum 10% limit then in affect), and \$572.10 in interest for the tax year 2003. [Department Exhibit D]

25. On April 2, 2007, Taxpayer protested the assessment issued in this matter. [Department Exhibit E]

26. On April 5, 2007, the Department acknowledged Taxpayer's protest of the assessment. [Department Exhibit F]

27. On October 14, 2011, the Department filed a Request for Hearing with the Department's Hearing Bureau.

28. On October 19, 2011, the Hearing Bureau sent Notice of Administrative Hearing, scheduling this matter for November 18, 2011.

29. As of the November 18, 2011 hearing, Taxpayer still owed \$1,334.00 in personal income tax, \$133.40 in penalty, and \$972.52 in interest, for a total outstanding balance of \$2,439.92. That total is subject to the continuing accrual of interest. [Department Exhibit G, corrected with testimony to reflect maximum penalty cap of 10% instead of the inadvertently listed 20% maximum penalty]

DISCUSSION

The issue in this case is whether Taxpayer is liable for personal income tax, penalty, and interest for tax year 2003 for the unreported distributions he received from his former employer's profit sharing plan. Taxpayer claimed that after he completed the packet of materials necessary to redeem his profit sharing distributions, his former employer was responsible for making the proper withholdings. However, because of his former employer's alleged grudge against him, Taxpayer claims that his former employer failed to assist him with the necessary documents to substantiate the State withholdings. In brief answer, Taxpayer is liable for 2003 personal income tax, penalty, and interest.

Presumption of Correctness and Burden of Proof.

Under NMSA 1978, Section 7-1-17(C) (2007), the assessment issued in this case is presumed to be correct. Consequently, the Taxpayer has the burden to overcome the assessment and establish that he was not required to pay the tax principal, interest, and penalty. *See Archuleta v. O'Cheskey*, 84 N.M. 428, 431, 504 P.2d 638, 641 (NM Ct. App. 1972).

2003 Personal Income Tax

Payment of New Mexico personal income tax is governed by NMSA 1978, §§ 7-2-1, *et seq.* Unless otherwise exempted by law, a tax is imposed "upon the net income of every" New Mexico resident. NMSA 1978, §7-2-3 (1981). The \$18,454.04 in profit sharing distribution that Taxpayer ultimately received in this matter qualifies as "net income" subject to income tax under NMSA 1978, Section 7-2-3 (1981).

Taxpayer was a full-time employee of Pronto Plumbing in Las Cruces for ten-years, until his termination in 2001. Apparently, at the time of his termination, Taxpayer had reported what Taxpayer alleges were some of Pronto Plumbing's questionable work quality and billing practices

to contractors and customers, resulting in a strained relationship between Taxpayer and his boss, Mr. Thomas Levy. However, before his 2001 termination, Taxpayer had vested in Pronto Plumbing's Profit Sharing Plan.

In 2003, Taxpayer returned to his former employer, Pronto Plumbing, to ask for his profit sharing distribution. Mr. Levy gave Taxpayer a packet of materials that needed to be completed in order for Taxpayer to receive his profit sharing distribution, Taxpayer Exhibits 1.1-1.15. While that packet referenced federal tax withholdings for the distribution, it did not indicate that any withholdings for state income tax purposes were to be made.

Taxpayer brought this packet of materials to Jackson Hewitt Tax Service in Las Cruces, who assisted him with the preparation of those documents. There is no evidence that Taxpayer ever discussed his state income tax obligations with Jackson Hewitt. After he completed the packet of materials, Taxpayer returned them to his former employer, Pronto Plumbing.

Pronto Plumbing informed Taxpayer that he was entitled an \$18,454.04 profit sharing distribution, less a 20% federal tax withholding. On August 7, 2003, Pronto Plumbing provided Taxpayer with a check in the amount of \$14,763.23. The following day, Pronto Plumbing deposited Taxpayer's 20% federal tax withholding totaling \$3,690.81 into the bank. Based on these two checks, which equaled the \$18,454.04 amount, Pronto Plumbing did not make any New Mexico tax withholdings from Taxpayer's profit sharing distribution. Moreover, there is no evidence that Taxpayer requested that such New Mexico withholdings be made on his behalf. Taxpayer did not have any W-2 forms related this profit sharing plan distribution at the time of the protest hearing to substantiate his suggestion that a State withholding may have been made by Pronto Plumbers.

On April 9, 2004, Taxpayer submitted his New Mexico personal income tax return based on a Federal Adjusted Gross Income of \$31,337. This \$31,337 did not include his profit sharing plan distribution. Based on this 2003 New Mexico personal income tax return, Taxpayer received a \$393.00 personal income tax refund.

At some point thereafter (neither party established the specific date), the IRS issued an unidentified letter, form, or ruling to Taxpayer that corrected Taxpayer's Federal Adjusted Gross Income in tax year 2003 in light of Taxpayer's profit sharing distribution and a small amount of other unreported income. The correction to Federal Adjusted Gross Income reflected an additional \$21,457 in income, raising the Federal Adjusted Gross Income from \$31,337 to \$52,794.

Through its matching program, the Department detected a difference between Taxpayer's corrected Federal Adjusted Gross Income and the Federal Adjusted Gross Income that Taxpayer reported to the State of New Mexico on his 2003 income tax return. Although under NMSA 1978, Section 7-1-13(C) (1994), Taxpayer had 90-days to amend his income tax return in light of the federal adjustment, Taxpayer failed to do so. Thus, on November 29, 2006, the Department sent Notice of Limited Scope Audit to Taxpayer, outlining the difference between his State-reported Federal Adjusted Gross Income and the corrected Federal Adjusted Gross Income amount reported by the IRS. When Taxpayer did not respond to that notice or another notice sent on January 29, 2007, the Department issued a Notice of Assessment on March 7, 2007. Including the \$393.00 refund issued to Taxpayer as a result of the incorrectly reported Federal Adjusted Income, Taxpayer had a 2003 personal income tax liability of \$1,334, penalty totaling \$133.40, and interest then totaling \$572.10 at the time of assessment.

Taxpayer indicated that he had difficulty obtaining any paperwork from Mr. Levy of Pronto Plumbers because of the sour relationship between them, making it difficult for him to contest the

assessment. Moreover, Taxpayer indicated that he believed in completing Pronto Plumbers' paperwork of materials, Pronto Plumbers assumed responsibility for withholding tax. However, nothing in Taxpayer Exhibits 1.1-1.15 supports this contention. While Taxpayer's situation with his former employer sounds sympathetic and could naturally lead to some misunderstandings due to a failure to communicate, New Mexico has a self-reporting tax regime where every taxpayer is tasked with the reasonable duty to ascertain the possible tax consequences of his or her actions. *See Tiffany Construction Co. v. Bureau of Revenue*, 90 N.M. 16, 558 P.2d 1155 (Ct. App. 1976), *cert. denied*, 90 N.M. 255, 561 P.2d 1348 (1977).

In sum, the evidence established that Taxpayer did not report \$21,457, including the \$18,454.04 profit sharing distribution, in 2003 personal income on his New Mexico personal income tax return, and did not amend his State return within 90-days of the federal correction to his Federal Adjusted Gross Income. Taxpayer presented no evidence that this \$21,457 was subject to an exemption or deduction. And the evidence established that no withholdings were made on this \$21,457 amount. Consequently, Taxpayer failed to overcome the presumption of correctness with the assessed personal income tax.

Assessment of 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, Section 7-1-67 (2008). 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 regardless of the explanation provided by a taxpayer. *See State v. Lujan*, 90 N.M. 103, 105, 560 P.2d 167, 169 (1977). The language of the statute also makes it clear that interest begins to run from the original due date of the tax and continues until the tax

principal is paid in full. The assessment of interest is not designed to punish taxpayers, but to compensate the state for the time value of unpaid revenues. Here, the Taxpayer failed to pay personal income tax due to the state. In effect, the Taxpayer had a loan of state funds during the time taxes were owed but not paid. Therefore, interest is due and continues to accrue until such time as the principal tax assessed is paid.

Assessment of Penalty.

The Department only seeks to impose a maximum 10% penalty pursuant to NMSA 1978 Section 7-1-69 (2003, prior to amendments through 2007). When a taxpayer fails to pay taxes due to the State as a result of negligence or disregard of rules and regulations, NMSA 1978, Section 7-1-69(A) (2003) imposes a penalty of two percent per month “from the date the tax was due,” not to exceed ten percent of the outstanding tax liability. Again, the statute’s use of the word “shall” makes the imposition of penalty mandatory in all instances where a taxpayer’s failure to act timely meets the legal definition of “negligence.” The term “negligence” is defined in Regulation §3.1.11.10 NMAC (1/15/01) to include “inadvertence, indifference, thoughtlessness, carelessness, erroneous belief or inattention.”

In this case, Taxpayer did not report his profit sharing income to New Mexico on his 2003 personal income tax return and did not amend his 2003 New Mexico income tax return to reflect his corrected Federal Adjusted Gross Income in light of his profit sharing distributions. By failing to initially report the income, and then by failing to amend his income tax return, Taxpayer met the definition of civil negligence based on his erroneous belief, inadvertent error, and inattention. This erroneous belief, inadvertent error, and inattention met the legal definition of “negligence” under the penalty statute. *See El Centro Villa Nursing Center v. Taxation and Revenue Department*, 108 N.M. 795, 799, 779 P.2d 982, 986 (Ct. App. 1989).

Taxpayer presented insufficient evidence under Regulation §3.1.11.11 NMAC (1/15/01) to demonstrate nonnegligence. While Taxpayer mentioned that he worked with Jackson Hewitt Tax Service to complete the paperwork necessary to obtain his profit sharing distribution, he presented no evidence that he ever discussed with them his potential state income tax liabilities from that distribution. Consequently, Taxpayer did not demonstrate the full disclosure necessary to show nonnegligence under Regulation §3.1.11.11(D) NMAC (1/15/01). As such, the Department is required by statute to impose penalty.

CONCLUSIONS OF LAW

1. Taxpayer filed a timely, written protest to the assessment of 2003 personal income tax, interest and penalty under Assessment No. # L0225000064, and jurisdiction lies over the parties and the subject matter of this protest.
2. The Taxpayer is liable for 2003 personal income tax and interest for income earned as a result of his unreported profit sharing plan distribution.
3. Taxpayer was civilly negligent in not reporting his profit sharing distributions as part of his 2003 New Mexico personal income tax return and in not amending his 2003 New Mexico personal income tax return upon learning of his corrected Federal Adjusted Gross Income that reflected his profit sharing distribution.

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

DATED: December 2, 2011.

BRIAN VANDENZEN
Tax Hearing Officer

NOTICE OF RIGHT TO APPEAL

Pursuant to NMSA 1978, §7-1-25, Taxpayer has the right to appeal this decision by filing a notice of appeal with the New Mexico Court of Appeals within 30 days of the date shown above. *See* NMRA, 12-601 of the Rules of Appellate Procedure. If an appeal is not filed within 30 days, this Decision and Order will become final.