

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

**IN THE MATTER OF THE PROTEST OF
WILLIAM S. MIDKIFF,
PROTEST TO
ASSESSMENT NOS. 568744 & 568745**

No. 94-03

DECISION AND ORDER

This matter came on for hearing on November 22, 1994 before Gerald B. Richardson, Hearing Officer. William S. Midkiff, hereinafter, Taxpayer, represented himself at the hearing. The Taxation and Revenue Department, hereinafter, Department, was represented by Bridget A. Jacober, Special Assistant Attorney General. Based upon the evidence and arguments presented, it is decided and ordered as follows:

FINDINGS OF FACT

1. The Taxpayer is a consultant. With the advice of his accountant and in an effort to lower his tax liability, the taxpayer gave 50% of the stock in his consulting company to each of his two children. This resulted in a distribution of the income from the corporation to his children rather than the Taxpayer and tax savings occurred because the children were in a lower tax bracket than the Taxpayer.

2. For the tax years 1990 and 1991, the Taxpayer reported and paid income tax to the IRS and the Department excluding the income reported to those entities by his children.

3. The Taxpayer was audited by the IRS for the 1990 and 1991 tax years. The IRS disallowed the deductions from income caused by the transfer of income to the Taxpayer's children, resulting in an increase in the Taxpayer's taxable income.

4. The IRS determination occurred in approximately February of 1994. As a result of this determination, the Taxpayer paid the additional taxes he owed to the IRS, and the Taxpayer's children filed amended returns and obtained a refund of overpaid taxes from the IRS.

5. Pursuant to its reciprocal agreement on the exchange of taxpayer information with the IRS, the Department received a revenue agents report from the IRS showing the IRS adjustments to the Taxpayer's taxable income for tax years 1990 and 1991.

6. Based upon the information the Department received from the IRS, on April 13, 1994 the Department issued to the Taxpayer Assessment No. 568744 in the total amount of \$8,172.61, representing taxes in the amount of \$5,272.66 in taxes, \$527.26 penalty and \$2,372.69 in interest, for the 1990 tax year. Additionally, on the same date the Department issued to the Taxpayer Assessment No. 568745 for the 1991 tax year, assessing \$1534 in tax, \$153.40 in penalty and \$460.20 in interest.

7. On April 15, 1994 the Taxpayer paid the Department the taxes assessed by the two aforementioned assessments and filed a written protest to the penalty and interest assessed.

8. The Department has abated the penalty assessed on the grounds that the Taxpayer was relying upon the advice of his accountant concerning the handling of his taxes for 1990 and 1991.

9. Although the Taxpayer's children applied for and received a refund from the Department of the taxes which they overpaid for the 1991 and 1990 tax years, the Department refunded no interest on such claims for refund which would compensate the Taxpayer's children for the time-value of having those overpaid taxes in the state's possession for the years prior to the refund claim.

10. The Department's interest assessment represents interest at a rate of 15% per annum or 1.25% per month, computed from the date the taxes were originally due, to the date the taxes were actually paid.

DISCUSSION

The sole issue to be determined herein is whether interest was properly assessed against the Taxpayer. The Taxpayer's arguments are, essentially, that interest at the rate of 15% per annum is excessive to compensate the state for the value of the money which the state forewent in not having

the taxes paid properly when they were originally due, since it is far higher than prevailing interest rates during the relevant time periods. Additionally, in this case, the state had at least part of the tax money in its possession, representing the taxes which it was ultimately determined were overpaid by the Taxpayer's children. Finally, the Taxpayer argues that the taxes were not actually due until the Department assessed the taxes, and so interest should only run from the date of the Department's assessment.

Interest on tax deficiencies is imposed pursuant to Section 7-1-67(A) NMSA 1978, which provides in pertinent part:

If any tax imposed is not paid on or before the day on which it becomes due, interest shall be paid to the state on such 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.

Pursuant to subsection B of Section 7-1-67, interest is imposed at the rate of 15% per year, computed at the rate of one and one-fourth percent per month or fraction of a month.

The Department acknowledged that charging interest at the rate of 15% per annum represented higher than market interest rates during the relevant time period. The Department even acknowledged that it had, on more than one occasion, sought legislation tying the interest rate to some measure by which the interest rate would be adjusted automatically and be more representative of market rates. The legislature, however, never enacted such legislation. Unfortunately for the Taxpayer, this is not an area where the Department has the discretion to make adjustments to the rate of interest. It is a legislative prerogative, and the Department (and this Taxpayer) are bound to follow the mandates of the statute. The relief the Taxpayer seeks can only be granted in a legislative forum. Thus, the rate of interest is no defense to the present assessment of interest.

The Taxpayer next argues that the Department or the state was already compensated for some part of the interest due to the fact that the Taxpayer's children had erroneously paid taxes which were not actually owing. The problem with this argument is that we are dealing with three separate

taxpayers here, even if they do happen to be related. The children filed under their own taxpayer identification number. A payment of taxes by one taxpayer, even if it is later determined to be erroneous, does not amount to a payment of taxes by another taxpayer. There is simply no statutory authority which would allow the Department to offset one taxpayer's liability with a tax payment made by a separate taxpayer.

The Taxpayer's final argument, that interest should only be computed from the date of the assessment, finds no support in the statutes. As noted above, Section 7-1-67 imposes interest upon the amount due "from the first day following the day on which the tax becomes due". Section 7-2-12 NMSA 1978 addresses when income taxes are due and provides in pertinent part:

...The return required and the tax imposed on individuals under the Income Tax Act are due and payment is required on or before the fifteenth day of the month following the end of the taxable year. (emphasis added).

In the case of individuals such as the Taxpayer who file on a calendar year basis, income taxes are due on or before April 15th of the following year. Thus, the Taxpayer's taxes were due, respectively upon April 15, 1991 and April 15, 1992, and the interest on any tax deficiency runs from those dates until the full amount of tax is paid.

Finally, I would like to address the Taxpayer's perception that he is somehow being punished for wrongdoing by the imposition of what he believes to be an exorbitant amount of interest. In this case, the Taxpayer has not been accused of knowingly claiming an improper deduction from income. There is a 50% of the tax liability penalty for such actions. *See*, Section 7-1-69(B) NMSA 1978. In fact, even the negligence penalty of 10% of the tax was abated by the Department when the Taxpayer demonstrated that his actions had been based upon the advice of his accountant. While the Taxpayer does have some basis to be concerned with the interest rate, which is much higher than market rates, this is something that can only be addressed by the ultimate policy maker on this issue, the legislature.

Actually, the most significant factor in the amount of interest due is the fact that two to three years passed from when the Taxpayer filed its original returns claiming the improper deductions from

income to the date when the deductions were disallowed by the taxing authorities. Although the Taxpayer can quibble with the interest rate imposed, nonetheless, the taxing agencies were entitled to receive the proper amount of taxes on the original due dates for the 1990 and 1991 income tax returns.

It is for this, that interest is imposed and no injustice has been done to the Taxpayer in this instance by the imposition of interest from the date the proper amount of taxes were due.

CONCLUSIONS OF LAW

1. The Taxpayer filed a timely written protest to the assessments at issue and jurisdiction lies over both the parties and the subject matter of this protest.

2. The Department has no authority to offset a tax payment by one taxpayer against a tax deficiency of another taxpayer in order to abate the accrual of interest on the tax deficiency.

3. Taxes are due by the due date established by statute, not the date that the Department issues an assessment for such taxes.

4. The Department has no authority to impose interest at a rate or in any manner that does not conform to the rate and manner required Section 7-1-67 NMSA 1978.

For the foregoing reasons, the Taxpayer's protest is hereby denied.

Done, this 22nd day of December, 1994.