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

IN THE MATTER OF THE PROTEST
OF JAMES BROWN **No. 01-08**
ID NO. 02-432277-00 6
ASSESSMENT NO. 25511986

DECISION AND ORDER

A formal hearing on the above-referenced protest was held June 13, 2001, before Margaret B. Alcock, Hearing Officer. James Brown ("Taxpayer") represented himself. The Taxation and Revenue Department ("Department") was represented by Lewis J. Terr, Special Assistant Attorney General. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. On July 12, 2000, the Department issued Assessment No. 25511986 to the Taxpayer, assessing $553.32 in gross receipts tax, $55.32 in penalty and $328.54 in interest for reporting periods January through December 1996.

2. The Department's assessment was based on information provided to the Department by the Internal Revenue Service ("IRS") pursuant to an information sharing agreement between the Department and the IRS. The Department's "tape-match program" compares the amount of business income reported on federal income tax returns filed by New Mexico residents to the amount of business income those residents reported to New Mexico for gross receipts tax purposes.

3. For tax year 1996, the Department determined that the Taxpayer reported business income in the amount of $10,500 on his federal income tax return but did not file corresponding gross receipts tax reports with New Mexico. This discrepancy led to the issuance of Assessment No. 25511986.

4. On August 7, 2000, the Taxpayer filed a written protest to the assessment.

5. From 1962 until mid-November 1996, the Taxpayer taught political science at Southern Methodist University in Texas. During those 34 years, the Taxpayer was a resident of Texas.

6. In addition to his teaching career, the Taxpayer provided consulting services to various businesses and government agencies. None of the Taxpayer's consulting work was performed in New Mexico.

7. In mid-November 1996, the Taxpayer retired from teaching and moved from Texas to New Mexico to take a position with Sandia National Laboratories in Albuquerque.

8. The Taxpayer has worked as an employee of Sandia National Laboratories since November 1996 and has not performed any outside consulting work during this period.

DISCUSSION

The sole issue to be determined in this protest is whether the business income the Taxpayer reported on his 1996 federal income tax return was subject to New Mexico gross receipts tax. "Gross receipts" is defined at Section 7-9-3(F) NMSA 1978 to mean:

> the total amount of money or the value of other consideration received from selling property in New Mexico, from leasing property employed in New Mexico, from selling services performed outside New Mexico the product of which is initially used in New Mexico or from performing services in New Mexico.

At the June 13, 2001 hearing, the Taxpayer testified that he did not move to New Mexico until mid-November 1996 when he accepted employment with Sandia National Laboratories and that none of his business income was attributable to services performed in New Mexico. Although the Department had no evidence to dispute this testimony, it was unwilling to accept the Taxpayer's assertions without corroborating documentary evidence. The Taxpayer explained that after conducting a diligent search, he was unable to find a Form 1099 relating to the business income reported on his 1996 federal income tax return. He also stated that he could not remember which company or agency he did consulting work for during 1996. The Taxpayer was unequivocal, however, in his testimony that none of his consulting work was performed in New Mexico.

Although taxpayers are expected to retain tax records in case of audit, it must be noted that the Department's assessment was not issued until more than three years after the due date of the Taxpayer's 1996 federal income tax return and four years after the work at issue was performed. In addition, assuming the Taxpayer's work was performed outside New Mexico while he was a resident of Texas, the Taxpayer was not subject to the record keeping requirements set out in New Mexico's Tax Administration Act and Gross Receipts & Compensating Tax Act. Given these circumstances, the absence of records—by itself—is not sufficient to establish that the Taxpayer's testimony is untruthful.

Prior to the hearing, the Department's only contact with the Taxpayer was by letter. The protest auditor said he did not attempt to speak with the Taxpayer personally because the tape-match auditor's notes indicated the Taxpayer's telephone number was unlisted. The Taxpayer disputed this, and Department counsel acknowledged that when he tried to reach the Taxpayer

the day before the hearing, he had no trouble obtaining a telephone number from information. Had someone from the Department tried to call the Taxpayer earlier, the Department might have been able to make its own determination of the Taxpayer's credibility. Instead, the Department chose to rely on the statutory presumption of correctness that attaches to Department assessments and require the Taxpayer to come to hearing to present his case to the hearing officer.

The presumption of correctness set out in Section 7-1-17(C) NMSA 1978 is not equivalent to a presumption that all taxpayers are untruthful. Before rejecting a taxpayer's statements out-of-hand, the Department should make every effort to confirm—or disprove—those statements through independent investigation. Aside from requesting documents from the Taxpayer, the Department made no effort to verify the Taxpayer's statements concerning his 1996 income. The Department's own records would have provided some evidence concerning the timing of the Taxpayer's change of residence from Texas to New Mexico. Nonetheless, the protest auditor assigned to the case never checked the Department's tax records to see whether the Taxpayer had filed a New Mexico income tax return prior to 1996 or checked the Department's motor vehicle records to determine when the Taxpayer first obtained a New Mexico driver's license or registered his automobile in this state. Nor did the Department make any effort to contact Sandia National Laboratories to confirm when the Taxpayer's employment commenced or whether the Taxpayer performed any consulting services for Sandia prior to his employment.

The Department's failure to uncover any evidence to dispute the Taxpayer's testimony concerning his move to New Mexico is important because residency is the key factor supporting the assessment. Referred to as a "limited scope audit", the Department's tape match program

does not encompass any audit field work or examination of taxpayer records. The program relies solely on information received from the IRS and is based on the assumption that a New Mexico resident who reports business income on his federal income tax return is likely to have earned that income in New Mexico. Once a taxpayer provides evidence that he was not a resident of New Mexico during the period at issue, the underlying rationale for the assessment disappears. While it is certainly possible that an out-of-state resident could have income from New Mexico sources, that fact cannot be assumed. Clearly, the Department would not be justified in issuing gross receipts tax assessments to self-employed residents of bordering states based on the mere possibility that some of their income was derived from business activities in New Mexico.

In this case, the presumption of correctness of the Department's assessment against the Taxpayer was rebutted by the Taxpayer's testimony that he lived and worked in Texas for 10½ of the 12 months covered by the assessment and that none of his consulting work was performed in New Mexico. At that point, the burden shifted to the Department to come forward with evidence to show (1) that the Taxpayer was, in fact, a resident of New Mexico during the assessment period; (2) that part or all of the Taxpayer's business income was derived from services performed in New Mexico; or (3) that the Taxpayer's testimony was inherently unbelievable or otherwise untrustworthy. The Department failed to meet this burden of proof. As the Taxpayer noted in his protest letter and reiterated at the hearing, when he offered the Department's tape-match auditor proof of the Taxpayer's Texas residency, the auditor "never indicated he was interested in having this information, nor required it." Similarly, the protest auditor never felt it was important to verify whether the Taxpayer was a Texas or a New Mexico resident during

1996, although it would have been easy enough to do so through Department records or an inquiry to the Taxpayer's employer.

The root of the problem in this case appears to be the belief among Department personnel that testimony is not reliable evidence and that only the hearing officer can determine credibility. Although auditors are trained to rely on books of account and other taxpayer records, they must recognize that once a matter reaches the protest stage, a taxpayer's sworn testimony carries weight equal to that of documentary evidence. And while the hearing officer is ultimately responsible for determining the facts of matters taken to hearing, the Department's hearing officers should not be the only Department employees capable of making determinations of credibility for purposes of resolving protests. The Department's Protest Office and its Legal Services Bureau also should be capable of making such determinations as part of the protest resolution process. When a taxpayer has provided testimony in defense to his liability for an assessment, and when the Department has no information or evidence to dispute that testimony or the credibility of the taxpayer, it should be possible to resolve the matter without expending the resources involved in conducting a full-blown evidentiary hearing.

In this case, the Taxpayer provided testimony that he lived and worked in Texas until mid-November 1996 and that none of the business income he earned during 1996 was attributable to services performed in New Mexico. Department counsel affirmatively stated that the Department had no evidence to dispute the Taxpayer's testimony. Based on the evidence presented, the Taxpayer's 1996 business income is not subject to New Mexico gross receipts tax.

CONCLUSIONS OF LAW

1. The Taxpayer filed a timely, written protest to Assessment No. 25511986, and jurisdiction lies over the parties and the subject matter of this protest.

2. The Taxpayer had no gross receipts subject to New Mexico gross receipts tax during calendar year 1996.

For the foregoing reasons, the Taxpayer's protest IS GRANTED and the Department is ordered to abate Assessment No. 25511986 in full.

DATED June 14, 2001.