

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

IN THE MATTER OF THE PROTEST OF
CATHLEEN TOMLINSON,
ID. NO. 02-315014-00 9, PROTEST TO
ASSESSMENT NOS. 2045130, 2056017,
2056018, 2056019 AND 2056020

NO. 98-13

DECISION AND ORDER

This matter came on for formal hearing before Gerald B. Richardson, Hearing Officer, on March 9, 1998. Cathleen Tomlinson, hereinafter, "Taxpayer", or "Ms. Tomlinson" represented herself at the hearing. The Taxation and Revenue Department, hereinafter, "Department", was represented by Mónica M. Ontiveros, Special Assistant Attorney General. Based upon the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. Commencing in 1993, the Taxpayer began providing private counseling and tutoring of children with learning disabilities or behavioral disorders who were enrolled in the Taos Municipal Schools. The Taxpayer received compensation for providing these services from the parents of the students she tutored or counseled.
2. Prior to providing private counseling and tutoring, the Taxpayer had been employed by the Taos Municipal Schools as a special education teacher.
3. Because it never occurred to the Taxpayer that she was "in business", or engaging in business as a private counselor or tutor, she did not understand that she was required to report and pay gross receipts tax upon her receipts from providing counseling or tutoring services.

Consequently, she did not report or pay gross receipts tax upon her receipts from providing those services.

4. The Taxpayer engaged H&R Block to prepare her income tax returns during all relevant periods. H&R Block prepared Federal Schedule C forms for the 1993 and subsequent tax years, reporting the Taxpayer's receipts from tutoring and counseling as income from a business or profession for federal income tax purposes.

5. The Taxpayer never asked H&R Block whether any taxes other than state and federal income taxes applied to her receipts from tutoring and counseling, and H&R Block never informed the Taxpayer that she was liable for New Mexico gross receipts tax upon her receipts from tutoring and counseling.

6. Pursuant to an information sharing agreement with the Internal Revenue Service, the Department receives information with respect to New Mexico taxpayers.

7. As a result of information received from the Internal Revenue Service, the Department issued various assessments to the Taxpayer, assessing gross receipts tax, penalty and interest on the Taxpayer's receipts from performing tutoring and counseling services. Those assessments are as follows:

<u>Assmt. No.</u>	<u>Date</u>	<u>Reporting Paid</u>	<u>Tax</u>	<u>Penalty</u>	<u>Interest</u>
2045130	6-14-96	7/93-12/93	\$813.04	\$81.30	\$294.73
2056020	7-12-96	1/94-6/94	\$453.30	\$45.33	\$135.99
2056019	7-12-96	7/94-12/94	\$453.37	\$45.34	\$102.01
2056018	7-12-96	1/95-6/95	\$510.26	\$51.03	\$76.54
2056017	7-12-96	7/95-12/95	\$471.49	\$47.15	\$35.36

8. The Department granted the Taxpayer a retroactive extension of time in which to file a protest to Assessment No. 2045130.

9. On August 12, 1996, the Taxpayer filed timely, written protests to the Department's assessments referenced above.

DISCUSSION

The Taxpayer does not dispute that she is liable for gross receipts tax upon her receipts from performing counseling and tutoring services for parents of children with special needs who are enrolled in the Taos Municipal Schools. The Taxpayer has paid the tax portion of the assessments in protest and has protested only the assessment of penalty and interest.

The Taxpayer disputes the imposition of penalty and interest primarily because of the hardship it would cause to pay it and because of her belief that the imposition of the tax itself, under the circumstances of her work, is inequitable.

Ms. Tomlinson is a single mother with two children, who, although well-educated, is not sophisticated about tax matters. She had worked as an employee of the Taos Municipal Schools prior to 1993 as a special education teacher. In 1993, she obtained another credential as a certified Academic Language Therapist and instead of working as an employee of the Taos Municipal Schools, the schools referred students with special needs to her for individual tutoring and counseling and she began her private counseling and tutoring business. The Taos Municipal Schools continued to make the school premises available to her to meet with her student clients for the convenience of the students. It simply never occurred to Ms. Tomlinson that private teaching was a taxable business and that in addition to income taxes, that there might be other taxes applicable to her receipts from performing her work. Because of this perception, Ms. Tomlinson did not inquire of the Department about any tax consequences to her change in the way she was teaching. Additionally, Ms. Tomlinson, not being sophisticated about tax matters, had relied upon her income tax preparer, H&R Block, to prepare her taxes and to advise her about tax matters. H&R Block had prepared Federal Schedule C forms for inclusion with her federal return for the tax years at issue, so clearly they knew she was doing business as a private

tutor, but they never informed her about New Mexico's gross receipts taxes and never inquired of her why she had no deductions from income for such taxes.

Ms. Tomlinson also objects to the tax itself as inequitable because the cost of the tax falls upon the parents of her clients, many of who are low income and many of whom already pay taxes to support our public schools. She does not think that the provision educational services such as those she provides should be subject to tax. Ms. Tomlinson understands, however, that there is no statutory exemption or exception for the types of educational services she provides and that she will need to look to the legislature for relief from the inequity of the imposition of this tax, itself. Nonetheless, she hopes that this will also be taken into consideration in this matter in the hope that the totality of the circumstances of this case will be cause for leniency with regard to the imposition of penalty and interest in this matter.

While I have great respect for Ms. Tomlinson and the work that she does and I have no doubt that she has made a real difference in the lives of the children who she has helped, nonetheless, I must be guided by the statutes and the interpretation of those statutes given by our courts in determining the legal issues presented.

Section 7-1-67(A) NMSA 1978 addresses the imposition of interest on tax deficiencies and provides as follows:

- A. 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. (emphasis added)

It is a well settled rule of statutory construction that the use of the word "shall" in a statute indicates that the provisions are intended to be mandatory rather than discretionary, unless a contrary legislative intent is clearly demonstrated. *State v. Lujan*, 90 N.M. 103, 560 P.2d 167 (1977). Applying this rule to Section 7-1-67, the statute requires that interest be paid to the state any time

that taxes are not paid when they are due and no exceptions to the imposition of interest are countenanced by the statute. Thus, it doesn't matter why taxes were unpaid. Interest is imposed for the period of time that they are unpaid.

There is an aspect of Ms. Tomlinson's argument which conceives of interest as a penalty imposed to punish a taxpayer for the late payment of taxes. This argument misapprehends the nature of the assessment of interest. Interest is imposed to compensate the state for the lost value of having tax revenues at the time they are required to be paid. Those tax revenues could have been invested by the state and interest earned upon those revenues, until the state needed to use the money to meet its obligations. Unfortunately, the rate of interest chosen by the Legislature, being at this time a fair amount more than market rates of interest, does little to dispel the Taxpayer's conception that the imposition of interest is intended to punish the late payment of tax. Nonetheless, while one may disagree with the rate of interest set by statute, that is a matter within the sound discretion of the Legislature, and the Department is without authority to substitute its own judgment for that of the Legislature in setting the rate of interest to be imposed. In this case, because there is no dispute that Ms. Tomlinson did not pay gross receipts taxes at the time they were originally due, the assessment of interest must stand.

The imposition of penalty is governed by the provisions of NMSA 1978, Section 7-1-69(A)(1995 Repl. Pamp.), which imposes a penalty of two percent per month, up to a maximum of ten percent:

In the case of failure, due to negligence or disregard of rules and regulations, but without intent to defraud, to pay when due any amount of tax required to be paid or to file by the date required a return regardless of whether any tax is due,....

This statute imposes penalty based upon negligence (as opposed to a willful or fraudulent intent) for failure to timely pay tax. Thus, there is no contention that the failure to report and pay taxes was based upon any conscious attempt by Ms. Tomlinson to underreport taxes. In fact, I have no doubt

that she would have reported and paid these taxes at the time they were due, had she known of her responsibility for them. What remains to be determined, however, is whether Ms. Tomlinson was negligent in failing to report her taxes properly. Taxpayer "negligence" for purposes of assessing penalty is defined in Regulation 3 NMAC 1.11.10 (formerly TA 69:3) as:

- 1) failure to exercise that degree of ordinary business care and prudence which reasonable taxpayers would exercise under like circumstances;
- 2) inaction by taxpayers where action is required;
- 3) inadvertence, indifference, thoughtlessness, carelessness, erroneous belief or inattention.

In this case the Taxpayer's failure to report and pay taxes was based upon Ms. Tomlinson's lack of knowledge about New Mexico gross receipts taxes. New Mexico has a self-reporting tax system which requires that taxpayers voluntarily report and pay their tax liabilities to the state. Because of this, the case law is well settled that every person is charged with the reasonable duty to ascertain the possible tax consequences of his actions, and the failure to do so has been held to amount to negligence for purposes of the imposition of penalty pursuant to Section 7-1-69 NMSA 1978. *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).

The fact that Ms. Tomlinson relied upon H&R Block to advise her about tax matters is a circumstance which should be considered in determining whether she was negligent in failing to pay taxes in a timely manner. Regulation 3 NMAC 1.11.11 (formerly regulation TA 69:4) provides a listing of situations which may indicate that a taxpayer was not negligent. Pertinent to Ms. Tomlinson's reliance on H&R Block is the fourth example, which provides in pertinent part:

the taxpayer proves that the failure to pay tax or to file a return was caused by reasonable reliance *on the advice of competent tax counsel or accountant* as to the taxpayer's liability after full disclosure of all relevant facts;....(emphasis added).

In this case, there are several ways in which Ms. Tomlinson fails to qualify under this regulation. Primarily, it is because Ms. Tomlinson was never advised by H&R Block about her gross receipts taxes. The regulation is intended to protect taxpayers who sought advice and were given erroneous advice by their tax advisors. Ms. Tomlinson admitted that she never inquired of them about any taxes other than the income taxes for which they prepared returns, and she admitted that she was never advised whatsoever about the New Mexico gross receipts taxes which applied to her. Admittedly, this is a bit of a catch-22, because Ms. Tomlinson did not know to ask about gross receipts taxes, and she had fully disclosed her income and its source in order for them to prepare her income taxes. It must also be conceded that, H&R Block does its clients a great disservice when it fails to advise them about New Mexico's gross receipts tax when its clients file a Federal Schedule C to report business income and losses and they find no evidence of an expense for payment of such taxes. It is a situation which, unfortunately, I have encountered all too often. Nonetheless, one must also consider that H&R Block holds itself out as an income tax preparation service and not a full scale tax adviser. That fact also ties into the language in the Department's regulation which requires that the advice be given by a "competent tax counsel or accountant". H&R Block is neither. They are income tax preparers, but they are not tax attorneys or accountants¹. Because of the foregoing, Ms. Tomlinson does not meet the criteria of Regulation 3 NMAC 1.11.11. Additionally, the facts of this case fall under the category of "erroneous belief" in Regulation 3 NMAC 1.11.10 defining taxpayer negligence and Ms. Tomlinson was also negligent under the standards of the *Tiffany Construction Company* case, *supra.*, and for these reasons, the imposition of penalty is upheld.

¹ Based upon this and other matters which have come before me, I also have substantial reason to question the competency of H&R Block, but that is not relied upon as a grounds for finding the pertinent regulation inapplicable in this case.

Although the imposition of penalty will pose a hardship for Ms. Tomlinson in this case, I hope that she can recognize the sound policy reasons behind the imposition of penalty. A self-reporting tax system relies upon taxpayers accurately reporting their tax liabilities to the government. There are insufficient government resources to audit every taxpayer periodically to otherwise assure tax compliance. The imposition of penalty provides taxpayers with an incentive to make inquiry so as to understand the tax consequences of their actions to ensure the accurate and timely payment of taxes.

CONCLUSIONS OF LAW

1. The Taxpayer filed timely, written protests to Assessment Nos. 2045130, and 2056017 through 2056020 and jurisdiction lies over both the parties and the subject matter of this protest.
2. Because the Taxpayer did not pay tax when it was due, interest was properly assessed.
3. The Taxpayer was negligent in failing to timely report and pay gross receipts taxes, and penalty was properly assessed.

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

DONE, this 11th day of March, 1998.