

STATE OF NORTH CAROLINA
COUNTY OF WAKE

BEFORE THE
SECRETARY OF REVENUE

IN THE MATTER OF:

The Proposed Assessment of Additional)
Income Tax for the Taxable Year 2000)
by the Secretary of Revenue of)
North Carolina)
vs.)
[Taxpayer])

FINAL DECISION
Docket No. 2001-664

This matter was heard before the Assistant Secretary for Administrative Tax Hearings, Eugene J. Cella, in the city of Raleigh on December 10, 2001, upon an application for hearing by [Taxpayer], wherein he protested the proposed assessment of additional income tax for the taxable year 2000. The hearing was held by the Assistant Secretary under the provisions of G.S. 105-260.1 and was attended by Taxpayer and Nancy R. Pomeranz, Director of the Personal Taxes Division.

Pursuant to G.S. 105-241.1, an assessment proposing additional tax, penalty, and accrued interest for the tax year 2000 was mailed to Taxpayer on August 25, 2001. Taxpayer filed a timely protest to the proposed assessment and requested a hearing before the Secretary of Revenue.

ISSUE

The issue to be decided in this matter is as follows:

Is the assessment for additional income tax proposed against Taxpayer for the taxable year 2000 lawful and proper?

EVIDENCE

The evidence presented by Nancy R. Pomeranz, Director of the Personal Taxes Division, consisted of the following:

1. Memorandum from E. Norris Tolson, Secretary of Revenue, to Eugene J. Cella, Assistant Secretary for Administrative Tax Hearings, dated May 16, 2001, a copy of which is designated as Exhibit PT-1.

2. Taxpayer's North Carolina individual income tax return for the taxable year 2000, a copy of which is designated as Exhibit PT-2.
3. Notice of Individual Income Tax Assessment for the taxable year 2000 dated August 25, 2001, a copy of which is designated as Exhibit PT-3.
4. Letter from Taxpayer to the North Carolina Department of Revenue dated September 4, 2001, a copy of which is designated as Exhibit PT-4.
5. Letter from Angela C. Quinn, Administrative Officer in the Personal Taxes Division, to Taxpayer dated September 27, 2001, a copy of which is designated as Exhibit PT-5.
6. Letter from Taxpayer to Angela C. Quinn dated October 2, 2001, a copy of which is designated as Exhibit PT-6.
7. Letter from Eugene J. Cella to Taxpayer dated November 8, 2001, a copy of which is designated as Exhibit PT-7.

At the hearing, Taxpayer presented the following evidence:

1. Administrative Procedure Act, G.S. 150B-1 and G.S. 150B-19, copies of which are designated as Exhibit TP-1.
2. North Carolina Administrative Code references, a copy of which is designated as Exhibit TP-2.
3. North Carolina State Constitution, Article 1, Declaration of Rights, a copy of which is designated as Exhibit TP-3.
4. Dictionary references, a copy of which is designated as Exhibit TP-4.
5. G.S. 105-136 (10a) and US Code Section 17, copies of which are designated as Exhibit TP-5.
6. Notice of Individual Income Tax Assessment for the taxable year 2000 dated August 25, 2001, a copy of which is designated as Exhibit TP-6
7. Taxpayer's North Carolina individual income tax return for the taxable year 2000, a copy of which is designated as Exhibit TP-7.
8. Taxpayer's federal income tax return for the taxable year 2000, a copy of which is designated as Exhibit TP-8.

FINDINGS OF FACT

Based on the foregoing evidence of record, the Assistant Secretary makes the following findings of fact:

1. Taxpayer is and at all material times was a natural person, sui juris, and a citizen and resident of North Carolina.

2. Taxpayer timely filed his North Carolina individual income tax return for the taxable year 2000.
3. The 2000 return reflected federal taxable income of zero and North Carolina income tax withheld of \$1,198.00. Taxpayer requested a refund of \$1,198.00.
4. Upon examination, the Department calculated Taxpayer's federal taxable income to be \$21,837.00. This amount was determined based on Taxpayer's wage and tax statements, which reflect wages of \$28,312.00. The standard deduction for a married individual filing separately and one personal exemption was allowed.
5. The Department calculated Taxpayer's North Carolina taxable income by increasing Taxpayer's corrected federal taxable income by the difference between the State and federal standard deduction and personal exemption allowance. North Carolina taxable income was determined to be \$23,312.00 for the tax year 2000.
6. A Notice of Individual Income Tax Assessment proposing an assessment of additional income tax; a twenty-five percent negligence penalty; and accrued interest totaling \$422.71 was mailed to Taxpayer on August 25, 2001.
7. Taxpayer objected to the proposed assessment and timely requested an administrative tax hearing before the Secretary of Revenue.
8. Taxpayer did not present any evidence at the hearing to show that his income, deductions, exemptions, or credits are other than those reflected in the assessment.

CONCLUSIONS OF LAW

Based on the foregoing findings of fact, the Assistant Secretary makes the following conclusions of law:

1. One of the duties of the North Carolina Department of Revenue is to collect taxes due to the State.
2. Division II of Article 4 in Chapter 105 of the North Carolina General Statutes imposes an individual income tax upon the taxable income of (1) every resident of this State and (2) every nonresident individual deriving income from North Carolina sources attributable to the ownership of any interest in real or tangible personal property in this State or deriving income from a business, trade, profession, or occupation carried on in this State.
3. "Taxpayer" is defined as an individual subject to the tax imposed by Division II of Article 4 in Chapter 105. "Individual" is defined as a human being.
4. A resident of North Carolina is an individual who is domiciled in this State at any time during the taxable year or who resides in this State during the taxable year for other than a temporary or transitory purpose. For residents of this State, "North Carolina taxable income" is defined as the taxpayer's taxable income as determined under the Internal Revenue Code, adjusted as statutorily provided for differences in State and federal law.

5. Federal taxable income is defined in the Internal Revenue Code as gross income less deductions and personal exemptions. Gross income is defined as all income from whatever source derived unless specifically excepted. Gross income includes compensation for services rendered and interest. Wages, salaries, commissions paid salesmen, compensation for services on the basis of a percentage of profits, tips, and bonuses are all includable in gross income. Gross income also includes amounts received as prizes and awards.
6. The Secretary of Revenue has the power to examine any books, papers, records, or other relevant data for the purpose of ascertaining the correctness of any return, making a return where none has been made, determining the tax liability of a person, or collecting any such tax. An assessment may be made if the Secretary discovers that any tax is due from a taxpayer. The Secretary must base a proposed assessment on the best information available.
7. A taxpayer who does not claim itemized deductions may claim a standard deduction. For a married person filing separate, the basic standard deduction is \$2,500.00. The basic federal standard deduction is increased each year for inflation. As a result, the federal standard deduction for a married person filing separate for the tax year 2000 is \$3,675.00.
8. A taxpayer may claim an exemption for himself and for each qualified dependent. The basic federal exemption amount is \$2,000.00. The basic exemption amount is increased each year for inflation. As a result, the federal personal exemption for an individual entitled to only one exemption for the tax year 2000 is \$2,800.00.
9. Additions to federal taxable income are required for the amount by which the taxpayer's standard deduction has been increased for inflation and the amount by which each of the taxpayer's personal exemptions has been increased for inflation under the Code. An addition of \$1,475.00 was properly made for the tax year 2000.
10. The twenty-five percent negligence penalty is imposed pursuant to G.S. 105-236(5)b for a large individual income tax deficiency. A large income tax deficiency exists when a taxpayer understates taxable income by an amount equal to twenty-five percent or more of gross income. A penalty of \$82.25 was properly assessed for the tax year 2000.

DECISION

Based on the foregoing evidence of record, the findings of fact, and the conclusions of law, the Assistant Secretary finds the proposed assessment for the tax year 2000 to be lawful and proper, and it is hereby affirmed.

Taxpayer contends that he is not required to file a North Carolina individual income tax return. A resident of this State is required under G.S. 105-152 to file a North Carolina individual income tax return if the individual is required to file a federal income tax return. The North

Carolina return must show the taxable income and adjustments to federal taxable income required by statute and shall be in the form prescribed by the Secretary. Form D-400 and Form D-400EZ are the forms prescribed by the Department of Revenue as the proper forms for individual income taxpayers to file (Title 17, NCAC, Chapter 6B, .0101). For a calendar-year taxpayer, the return is due on or before the fifteenth of April of the calendar year following the tax year. Pursuant to G.S. 105-157, tax payable as shown on the return must be paid to the Secretary within the time allowed for filing the return. Due to the difference in the gross “minimum” filing requirements for State and federal purposes (Title 17, NCAC, Chapter 6B, .0109), a taxpayer may be required to file a North Carolina return even though he is not required to file a federal return.

Taxpayer contends that North Carolina is in violation of the North Carolina Constitution because a taxpayer’s North Carolina taxable income means the taxpayer’s taxable income as determined under the Code. Section 2(1) of Article V of the Constitution provides in pertinent part that the “power of taxation...shall never be surrendered, suspended, or contracted away.” To adopt by reference future amendments to the Internal Revenue Code would likely be held to be an unconstitutional delegation of legislative power. Taxpayer’s argument fails, however, because the State’s reference to the Code does not automatically adopt future changes to the Code. G.S. 105-228.90 defines “Code” by referring to the Internal Revenue Code as of a specific date. The definition is revised as needed to reflect the General Assembly’s decision to adopt amendments to the Code. The General Assembly always uses a reference date equal to or prior to the date the legislation is enacted to ensure that it is not delegating its power to tax to the United States Congress.

Taxpayer contends that his wages are not subject to taxation. Both federal and State law impose the individual income tax on the “taxable income” of every individual (Code section 1, G.S. 105-134). The State’s definition of taxable income (G.S. 105-134.1(16)) refers to the definition of taxable income in Code section 63. Taxable income for federal purposes means

gross income less allowable deductions. Gross income is defined by Code section 61 as, except as otherwise provided, all income from whatever source derived, including compensation for services.

The courts have consistently held that wages and other forms of compensation for services rendered are income. (See *Lonsdale v. U.S.*, 919 F. 2d 1440, 90-2 T.C. ¶50,581 (10th Cir. 1990) and *Stelly v. Commissioner*, 761 F. 2d 1113, 85-1 T.C. ¶9436 (5th Cir. 1985). There are many other cases that could be cited. Every court that has addressed the issue of the constitutionality of the income tax on wages, 28 U.S.C. § 61(a), has held the statute valid.

Taxpayer contends that the U.S. Secretary has not authorized the State of North Carolina to assess federal taxes. The North Carolina Department of Revenue is responsible for collecting taxes due to the State. The assessment proposed by the Department reflects North Carolina tax due, not federal tax due, as determined from the best information available. G.S. 105-159 provides that the Secretary "shall determine from all available evidence the taxpayer's correct tax liability for the taxable year." Taxpayer has not established that the evidence upon which the assessment is based is incorrect.

I find the Taxpayer's arguments, repeatedly rejected by the courts, having no merit whatsoever. Therefore, the proposed assessment for the tax year 2000 is hereby sustained in its entirety and determined to be final and collectible, together with interest as allowed by law.

Made and entered this 15th day of February, 2002.

Signature _____

Eugene J. Cella

Assistant Secretary for Administrative Tax Hearings
North Carolina Department of Revenue