

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 1997 by the)
Secretary of Revenue of North Carolina)
)
vs.) **FINAL DECISION**
) Docket No. 2001-84
)
[Taxpayers])

This matter was heard before the Acting Assistant Secretary of Administrative Hearings, Marilyn R. Mudge, in the city of Raleigh on April 17, 2001, upon an application for hearing by [Taxpayers, Husband and Wife], wherein they protested the proposed assessment of additional income tax and interest for the taxable year 1997. The hearing was held under the provisions of G.S. 105-260.1 and was attended by Taxpayers and Gregory B. Radford, Assistant Director of the Personal Taxes Division.

Pursuant to G.S. 105-159 and G.S. 104-241.1, a Notice of Individual Income Tax Assessment proposing an assessment of additional income tax and accrued interest for the taxable year 1997 was mailed to Taxpayers on October 3, 2000. The proposed assessment was based on a report obtained from the Internal Revenue Service reflecting adjustments to Taxpayers' 1997 federal income tax return. Taxpayers objected to the proposed assessment and timely 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 and interest proposed against Taxpayers for the taxable year 1997 lawful and proper?

EVIDENCE

The evidence presented by Gregory B. Radford, Assistant Director of the Personal Taxes Division, consisted of the following:

1. Memorandum from E. Norris Tolson, Secretary of Revenue, to Marilyn R. Mudge, Acting Assistant Secretary of Administrative Hearings, dated March 13, 2001, a copy of which is designated as Exhibit PT-1.
2. Taxpayers' North Carolina individual income tax return for the taxable year 1997, a copy of which is designated as Exhibit PT-2.
3. Notice of Individual Income Tax Assessment for the taxable year 1997 dated October 3, 2000, a copy of which is designated as Exhibit PT-3.
4. A paper extract of information provided to the Department of Revenue on magnetic tape by the Internal Revenue Service for the taxable year 1997, a copy of which is designated as Exhibit PT-4.
5. Letter from Husband to the Department of Revenue dated October 10, 2000, a copy of which is designated as Exhibit PT-5.
6. Letter from Gregory B. Radford to Taxpayers dated December 11, 2000, a copy of which is designated as Exhibit PT-6.
7. Letter from Husband to the Department of Revenue received by the Department on December 21, 2000, a copy of which is designated as Exhibit PT-7.
8. Letter from Muriel K. Offerman, former Secretary of Revenue, to Taxpayers dated February 12, 2001, a copy of which is designated as Exhibit PT-8.
9. Letter from Marilyn R. Mudge to Taxpayers dated March 2, 2001, a copy of which is designated as Exhibit PT-9.
10. Letter from Marilyn R. Mudge to Taxpayers dated March 30, 2001, a copy of which is designated as Exhibit PT-10.

FINDINGS OF FACT

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

1. Taxpayers are and at all material times were natural persons, sui juris, and citizens and residents of North Carolina.

2. Taxpayers timely filed their 1997 North Carolina individual income tax return. The return reflected federal taxable income of \$14,594.00 and North Carolina taxable income of \$16,794.00.
3. The Department of Revenue received information from the Internal Revenue Service indicating that Taxpayer's federal taxable income had been increased by \$5,362.00. The adjustment consisted of unreported interest income of \$11.00 from [an Insurance Company] and unreported pension income of \$5,351.00 from the New York State and Local Government Employees Retirement System.
4. Taxpayers did not notify the Department of Revenue of the adjustment to their federal income tax return.
5. Upon examination, the Department of Revenue increased Taxpayers' North Carolina taxable income to include the unreported income.
6. A Notice of Individual Income Tax Assessment reflecting additional tax and interest of \$403.35 for the taxable year 1997 was mailed to Taxpayers on October 3, 2000.
7. Taxpayers objected to the proposed assessment and timely requested a hearing.
8. Prior to moving to North Carolina in 1996, Taxpayers were residents of New York. Husband was employed by the State of New York or one of its local governments and was a member of the New York State and Local Government Employees Retirement System.
9. While still employed and a New York resident, Husband borrowed funds from the retirement system. Husband began repaying the borrowed funds through payroll deduction.
10. Husband subsequently left employment with New York and Taxpayers moved to and became residents of North Carolina.
11. Husband did not make any voluntary repayments of the borrowed funds after leaving employment and moving to North Carolina.
12. The New York State and Local Government Employees Retirement System cancelled the debt in 1997 and reported the cancellation to the Internal Revenue Service.
13. Taxpayers were residents of North Carolina at the time the debt was cancelled.

CONCLUSIONS OF LAW

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

1. For residents of this State, North Carolina taxable income is defined as federal taxable income, adjusted as statutorily required for differences in State and federal law. Residents

are taxed on income from whatever source derived, whether from sources within North Carolina or sources outside of North Carolina.

2. For federal income tax purposes, a taxpayer is required to include interest income and income from the discharge of indebtedness in gross income.
3. A cash-basis taxpayer reports income in the year it is actually or constructively received. Income from cancellation of debt is constructively received at the time the debt is cancelled.
4. Upon receipt of information reflecting adjustments to a taxpayer's federal income tax return by the Internal Revenue Service, all facts or evidence including any information shown on the federal report must be considered in proposing an assessment against the taxpayer. An assessment may be made within three years of receipt of the federal report unless the taxpayer files a return or amended return reporting the federal changes; in that case, an assessment must be made within one year of receiving the information from the taxpayer or three years of the date the original return was filed, whichever is later.
5. If a taxpayer does not provide adequate and reliable information upon which the Department can accurately compute his liability, an assessment may be made upon the basis of the best information available.

DECISION

Assessments are presumed to be correct and the burden is on the taxpayer to establish that the assessment is in error. Taxpayers have not furnished any information to show that the assessment is in error. Therefore, the assessment for additional tax and interest proposed under G.S. 105-159 and G.S. 105-241.1 was properly issued; is lawful in every respect; and is hereby sustained.

Made and entered this 3rd day of May, 2001.

Signature_____

Marilyn R. Mudge
Acting Assistant Secretary of Administrative Hearings