

**STATE OF NORTH CAROLINA**  
**COUNTY OF WAKE**

**BEFORE THE**  
**SECRETARY OF REVENUE**

**IN THE MATTER OF:**

The Proposed Assessments of Additional )  
Income Tax for the Taxable Years 1997 )  
and 1998 by the Secretary of Revenue )  
of North Carolina )  
vs. )  
[Taxpayer] )

**FINAL DECISION**  
Docket No. 2002-209

This matter was heard before the Assistant Secretary for Administrative Tax Hearings, Eugene J. Cella, in the city of Raleigh on June 17, 2002, upon an application for hearing by [Taxpayer], wherein he protested the proposed assessments of additional income tax for the taxable years 1997 and 1998. The hearing was held by the Assistant Secretary under the provisions of G.S. 105-260.1 and was attended by Taxpayer; Nancy R. Pomeranz, Director of the Personal Taxes Division; and, with Taxpayer's permission and at his request, [a friend of Taxpayer].

Pursuant to G.S. 105-241.1, assessments proposing additional tax and penalties for the tax years 1997 and 1998 were mailed to Taxpayer on December 13, 2001. Taxpayer filed a timely protest to the proposed assessments and requested a hearing before the Secretary of Revenue.

**ISSUE**

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

Are the assessments for additional income tax proposed against Taxpayer for the taxable years 1997 and 1998 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. Notice of Individual Income Tax Assessment for the taxable year 1997 dated December 13, 2001, a copy of which is designated as Exhibit PT-2.
3. Notice of Individual Income Tax Assessment for the taxable year 1998 dated December 13, 2001, a copy of which is designated as Exhibit PT-3.
4. Internal Revenue Service Report of Income Tax Examination Changes dated January 12, 2001, a copy of which is designated as Exhibit PT-4.
5. Letter from J. P. Parker, Revenue Tax Auditor, to Taxpayer dated August 9, 2001, a copy of which is designated as Exhibit PT-5.
6. Letter from Taxpayer to J. P. Parker dated August 24, 2001, a copy of which is designated as Exhibit PT-6.
7. Letter from J. P. Parker to Taxpayer dated August 27, 2001, a copy of which is designated as Exhibit PT-7.
8. Letter from Taxpayer to J. P. Parker dated September 1, 2001, a copy of which is designated as Exhibit PT-8.
9. Letter from J. P. Parker to Taxpayer dated November 2, 2001, a copy of which is designated as Exhibit PT-9.
10. Letter from Taxpayer to J. P. Parker dated November 24, 2001, a copy of which is designated as Exhibit PT-10.
11. Letter from Taxpayer to E. Norris Tolson dated January 7, 2002, a copy of which is designated as Exhibit PT-11.
12. Letter from Patrick G. Penny, Administrative Officer in the Personal Taxes Division, to Taxpayer dated January 22, 2002, a copy of which is designated as Exhibit PT-12.
13. Letter from Taxpayer to Patrick G. Penny dated February 25, 2002, a copy of which is designated as Exhibit PT-13.
14. Letter from Eugene J. Cella to Taxpayer dated March 19, 2002, a copy of which is designated as Exhibit PT-14.
15. Letter from Taxpayer to Eugene J. Cella dated March 30, 2002, a copy of which is designated as Exhibit PT-15.
16. Letter from Eugene J. Cella to Taxpayer dated May 13, 2002, a copy of which is designated as Exhibit PT-16.
17. Letter from Taxpayer to Eugene J. Cella dated May 15, 2002, a copy of which is designated as Exhibit PT-17.
18. Letter from Eugene J. Cella to Taxpayer dated May 16, 2002, a copy of which is designated as Exhibit PT-18.

19. Letter from Patrick G. Penny to Taxpayer dated May 28, 2002, a copy of which is designated as Exhibit PT-19.

At the hearing, Taxpayer presented a document entitled Taxable Income, a copy of which is designated as Exhibit TP-1.

### **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 did not file North Carolina or federal individual income tax returns for the tax years 1997 and 1998.
3. The Department of Revenue received reports from the Internal Revenue Service indicating that the Internal Revenue Service had determined Taxpayer's federal taxable income to be \$24,522.00 for the tax year 1997 and \$25,560.00 for the tax year 1998. The federal taxable income amounts were determined by allowing the standard deduction for the filing status of single and one personal exemption.
4. Upon examination, the Department determined Taxpayer's North Carolina taxable income for the tax years 1997 and 1998 to be \$25,822.00 and \$27,010.00, respectively, by increasing Taxpayer's federal taxable income as reported by the Internal Revenue Service for the differences between the State and federal standard deduction and personal exemption allowances.
5. Taxpayer understated taxable income by twenty-five percent or more of gross income for both years.
6. Pursuant to G.S. 105-241.1, Notices of Individual Income Tax Assessment reflecting additional tax, penalties, and interest for the tax years 1997 and 1998 were mailed to Taxpayer on December 13, 2001. Taxpayer objected to the proposed assessments and timely requested a hearing before the Secretary of Revenue.
7. Taxpayer argues that (1) Taxpayer has no taxable income since he did not receive any income from the "sources" listed in 26 CFR 1.861-8(f)(1); and (2) as a "tax payer" (two words), Taxpayer is not liable for income tax.

### **CONCLUSIONS OF LAW**

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

1. The North Carolina General Statutes impose 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.

2. 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.
3. Federal taxable income is defined by 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 gross income derived from business. 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.
4. An individual is required to file a federal income tax return if his gross income for the year equals or exceeds the allowable exemption amount. A resident of this State is required 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 shall show the taxable income and adjustments to federal taxable income required by statute. For a calendar-year taxpayer, the return is due on or before the fifteenth of April of the calendar year following the tax year.
5. Additions to federal taxable income are required for the amount by which the taxpayer's standard deduction has been increased and the amount by which each of the taxpayer's personal exemptions has been increased for inflation under the Code. The increase in the personal exemption for inflation is reduced by \$500.00 if the taxpayer's federal adjusted gross income is below the threshold for the taxpayer's filing status. Additions of \$1,300.00 and \$1,450.00 were properly made for the tax years 1997 and 1998, respectively.
6. If a taxpayer does not provide adequate and reliable information upon which to compute his tax liability, an assessment may be made upon the basis of the best information available; and, in the absence of information to the contrary, such assessment is deemed to be correct.
7. Assessments must generally be proposed within three years of the date the return was filed or the date the return was due to be filed, whichever is the later. When a return has not been filed, there is no statute of limitations and an assessment can be proposed at any time.
8. A penalty is imposed for failure to file a return when due. The penalty is equal to five percent of the tax for each month, or fraction of a month, the return is late (minimum \$5.00, maximum twenty-five percent). Because Taxpayer did not file the returns, penalties of \$420.00 and \$441.00 for failure to file the returns when due were properly assessed for the years 1997 and 1998, respectively.
9. A penalty is imposed for failure to pay tax when due. The penalty is equal to ten percent of the tax (minimum \$5.00). Because Taxpayer did not pay the tax when due, penalties of \$168.00 and \$176.40 were properly assessed for the years 1997 and 1998, respectively.

10. A twenty-five percent negligence penalty is imposed 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. Penalties of \$420.00 and \$441.00 were properly assessed for the years 1997 and 1998, respectively because Taxpayer understated taxable income by 25 percent or more of gross income.
11. A penalty is imposed for underpayment of estimated income tax if the taxpayer does not pay estimated income tax of at least ninety percent of the tax shown on the current year's return, or if no return is filed, ninety percent of the tax for that year or one hundred percent of the tax shown due on the previous year's return, whichever is less. The penalty is not due if the tax due on the return, reduced by the North Carolina tax withheld and allowable tax credits, is less than \$1,000.00. A penalty of \$90.65 for underpayment of estimated income tax was properly assessed for the year 1998.
12. The Secretary of Revenue's duties include administering the laws enacted by the General Assembly relating to the assessment and collection of individual income taxes. As an official of the executive branch of the government, the Secretary lacks the authority to determine the constitutionality of legislative acts. The question of constitutionality of a statute is for the judicial branch.

### **DECISION**

Based on the foregoing evidence of record, findings of fact, and conclusions of law, the Assistant Secretary finds the proposed assessments for the tax years 1997 and 1998 to be lawful and proper and are hereby affirmed.

Taxpayer presents many arguments in defense of his position that the assessments are in error. These arguments have been made on many occasions both before the courts and in previous administrative tax hearings by individuals who object to the payment of income tax. The arguments have consistently and uniformly been found to be completely lacking in legal merit and patently frivolous. Taxpayer's arguments include (1) Taxpayer has no taxable income since he did not receive any income from the "sources" listed in 26 CFR 1.861-8(f)(1); and (2) as a "tax payer" (two words), Taxpayer is not liable for income tax.

Taxpayer correctly states that Internal Revenue Code ("Code") section 61 defines gross income as all income from whatever source derived. Taxpayer then attempts to define "source" and contends that Code section 861 and its accompanying statutes and regulations indicate that he is not subject to income tax because, as a citizen of the United States, he has no sources of

income for purposes of the income tax. According to Taxpayer's argument, the only sources of income subject to income tax are listed in 26 CFR 1.861-8(f)(1). Such is not the case. For a citizen of the United States, the source of income is irrelevant. In *Commissioner of Internal Revenue v. Glenshaw Glass Co.*, 348 U.S. 426; 99 L. Ed. 483 (1955), the court concluded that income tax is imposed on "undeniable accessions to wealth, clearly realized, and over which the taxpayers have complete dominion" with no restrictions as to "sources." 26 CFR 1.1-1(b) provides that "in general, all citizens of the United States, wherever resident, and all resident alien individuals, are liable to the income taxes imposed by the Code whether the income is received from sources within or without the United States." In addition, the term "from whatever source derived" in Code section 61 is not intended to be restrictive; instead, it is intended to be all encompassing. In *United States v. Buras*, 633 F.2d 1356, 1361 (9<sup>th</sup> Cir. 1980), the court stated "According to Buras, income must be derived from some source. ...[T]he Sixteenth Amendment is broad enough to grant Congress the power to collect an income tax regardless of the source of the taxpayer's income." In *Angstadt v. Internal Revenue Service*, 99-2 U.S. Tax Cas. (CCH) ¶150, 926; 84 A.F.T.R.2d (RIA) 6776, the court stated "By the terms of the Sixteenth Amendment and section 61(a), 'source' is not to be a limitation on taxable income. Rather, income is to be taxed regardless of its source."

Code section 861 itself provides that the income of most citizens is from sources within the United States. Section 861(a) lists items of gross income that are treated as income from sources within the United States. Item (3) is compensation for labor or personal services performed in the United States. 26 CFR 1.861-4(a)(1) states that "gross income from sources within the United States includes compensation for labor or personal services performed in the United States irrespective of the residence of the payer, the place in which the contract for service was made, or the place or time of payment..." In *Aiello v. Commissioner*, T.C. Memo 1995-40; 69 T.C.M. (CCH) 1765, the court stated "Apparently, petitioner believes that the only sources of income for purposes of section 61 are listed in section 861, that income from sources

within the United States is taxed only to nonresident aliens and foreign corporations...Under section 61(a)(1) and (4), petitioner clearly is required to include his wages, toles, and interest in gross income.”

Taxpayer contends that he is a “tax payer” (two words) rather than a “taxpayer” (one word); and therefore, he is not subject to the income tax since only “taxpayers” (one word) are held liable for the income tax. This contention is totally without arguable merit. Taxpayer is obviously a human being and, as a resident of North Carolina, he is subject to North Carolina income tax.

I find the Taxpayer’s arguments to be no more than trite contentions repeatedly rejected by the courts as having no merit whatsoever. Therefore, the proposed assessments for the tax years 1997 and 1998 are hereby sustained in their entireties and are determined to be final and collectible, together with interest as allowed by law.

Made and entered this 31<sup>st</sup> day of July, 2002.

Signature \_\_\_\_\_

Eugene J. Cella

Assistant Secretary for Administrative Tax Hearings  
North Carolina Department of Revenue