

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 1998)
and 1999 by the Secretary of Revenue)
of North Carolina)

vs.)

[Taxpayers])

FINAL DECISION

Docket No. 2001-555

This matter was heard before the Assistant Secretary for Administrative Tax Hearings, Eugene J. Cella, in the city of Raleigh on September 24, 2001, upon an application for hearing by [Taxpayers, Husband and Wife], wherein they protested the proposed assessments of additional income tax for the taxable years 1998 and 1999. The hearing was held by the Assistant Secretary under the provisions of G.S. 105-260.1 and was attended by Husband and Nancy R. Pomeranz, Director of the Personal Taxes Division.

Pursuant to G.S. 105-241.1, assessments proposing additional tax, penalties, and accrued interest for the tax years 1998 and 1999 were mailed to Taxpayers on June 12, 2001. Taxpayers 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 Taxpayers for the taxable years 1998 and 1999 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 1998 dated June 12, 2001, a copy of which is designated as Exhibit PT-2.
3. Notice of Individual Income Tax Assessment for the taxable year 1999 dated June 12, 2001, a copy of which is designated as Exhibit PT-3.
4. Taxpayers' North Carolina individual income tax return for the taxable year 1998, a copy of which is designated as Exhibit PT-4.
5. Taxpayers' North Carolina individual income tax return for the taxable year 1999, a copy of which is designated as Exhibit PT-5.
6. Letter from Husband to the North Carolina Department of Revenue dated June 26, 2001, a copy of which is designated as Exhibit PT-6.
7. Letter from Angela C. Quinn, Administrative Officer in the Personal Taxes Division, to Husband dated August 2, 2001, a copy of which is designated as Exhibit PT-7.
8. Letter from Husband to Angela C. Quinn dated August 29, 2001, a copy of which is designated as Exhibit PT-8.
9. Letter from Eugene J. Cella to Husband dated September 7, 2001, a copy of which is designated as Exhibit PT-9.

FINDINGS OF FACT

Based on the foregoing evidence of record, the Assistant Secretary 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 filed their North Carolina income tax returns for the taxable years 1998 and 1999. The 1998 return was received by the Department on April 12, 2001 and the 1999 return was received by the Department on April 15, 2001.
3. The 1998 return reflected tax due of \$82.00 and the 1999 return reflected tax due of \$1,216.00. Taxpayers did not pay the tax shown due on the returns.
4. Notices of Individual Income Tax Assessment proposing assessments of additional income tax, a twenty-five percent late filing penalty, a ten percent late payment penalty, and accrued interest for both tax years were mailed to Taxpayers on June 12, 2001.
5. Taxpayers objected to the proposed assessments and timely requested an administrative tax hearing before the Secretary of Revenue.

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. 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). Penalties of \$20.50 and \$304.00 were properly assessed for the tax years 1998 and 1999.
7. A penalty is imposed for failure to pay tax when due. The penalty is equal to ten percent of the tax (minimum \$5.00). Penalties of \$8.20 and \$121.60 were properly assessed for the tax years 1998 and 1999.
8. 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.

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 1998 and 1999 to be lawful and proper, and they are hereby affirmed.

Husband argues that he is not a taxpayer and that his wages are not subject to taxation. He alludes to an argument that the income tax cannot apply to wages because that would be a direct tax that must be apportioned in accordance with the Constitution. 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 *E. M. Lonsdale*, CA-10, 90-2 USTC ¶50,581, *H.H. McKinley*, DC Ohio, 92-2 USTC ¶50,509, *A. Ficalora*, CA-2, 85-1 USTC ¶9103, *C. Stelly*, CA-5, 85-2 USTC ¶9436, *Coleman v. Commissioner of Internal Revenue*, 791 F.2d 68 (7th Cir. 1986); *United States v. Collins*, 920 F.2d 619, 629 (10th Cir. 1990). 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. In *Ficalora*, the appellant was employed by the New York Telephone Company and his wages were determined to be taxable. In *Collins*, the individual was employed by CDI Corporation and his wages were held to be taxable.

In *Ficalora*, the Court held that Congress had the constitutional authority to impose an income tax on individuals. The court cited the United States Supreme Court's decision in *Pollock v. Farmers' Loan & Trust Co.*, 157 U.S. 429, 558 (1895), which explicitly stated that

taxes on income from employment were not direct taxes and were not subject to the necessity of apportionment. Furthermore, the Sixteenth Amendment granted Congress the power to lay and collect taxes on incomes, from whatever source derived, without apportionment. In *United States v. Gerads*, 999 F.2d 1255 (8th Cir. 1993), the Court stated “we have rejected on numerous occasions, the tax-protester argument that the federal income tax is an unconstitutional direct tax that must be apportioned.”

There is nothing in the Constitution that says that wages or income from labor cannot be taxed, or that a tax on wages or income is a “direct tax.” It has been the consistent opinion of the Supreme Court that the phrase “direct tax” only applies to a tax on the value of property.

I find the Husband’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 1998 and 1999 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 10th day of December, 2001.

Signature_____

Eugene J. Cella
Assistant Secretary for Administrative Tax Hearings