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

IN THE MATTER OF THE PROTEST OF
JAMES A. AND TERRI L. HOLT **No. 01-18**
PROTEST OF DENIAL OF REFUND CLAIM

DECISION AND ORDER

A formal hearing on the above-referenced protest was held August 13, 2001, before Margaret B. Alcock, Hearing Officer. James A. and Terri L. Holt ("Taxpayers") represented themselves. The Taxation and Revenue Department ("Department") was represented by Monica M. Ontiveros, Special Assistant Attorney General. Based on the evidence and arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. On February 15, 2000, the Taxpayers filed their 1999 New Mexico personal income tax return ("PIT-1") with the Department.

2. On line 5 of the PIT-1, the Taxpayers reported zero federal adjusted gross income, as reported on line 33 of their 1999 federal income tax return, a copy of which was attached to the Taxpayers' New Mexico return.

3. Based on the reporting of zero federal adjusted gross income, the Taxpayers also reported zero New Mexico taxable income and zero New Mexico tax due.

4. On Line 16 of the PIT-1, the Taxpayers reported that $2,009.00 of New Mexico income tax had been withheld from them during 1999, and requested a refund in that amount.

5. A copy of the Taxpayers' 1999 W-2 forms were attached to the PIT-1. The W-2s showed that during 1999, James Holt earned "wages, tips, other compensation" of $47,561.03 from Public Service Company of New Mexico and Terri Holt earned "wages, tips, other comp." of

$15,281.28 from BGK Asset Management Corporation. The W-2s also indicated that the Taxpayers' employers withheld both federal and state income tax from their wages.

6. After reviewing the information submitted by the Taxpayers, the Department recalculated their 1999 New Mexico income tax by adding the wages shown on the Taxpayers' W-2s and using this as the amount that should have been reported as federal adjusted gross income on Line 5 of the PIT-1. The Department then subtracted the federal standard deduction and the federal exemptions to which the Taxpayers were entitled to arrive at taxable income of $50,142.00. Applying the rate table, the Department determined that the Taxpayers owed New Mexico personal income tax of $2,449.00. The Department then credited the Taxpayers with the $2,009.00 withheld from their wages, resulting in a net tax due of $440.00.

7. On April 7, 2000, the Department sent the Taxpayers a "New Mexico Personal Income Tax Recomputation Notice" which explained that the Department had recalculated the Taxpayers' 1999 New Mexico personal income tax and determined they were not entitled to the refund requested, but owed additional tax in the amount of $440.00.

8. By letter dated May 17, 2000, the Taxpayers filed a written protest to the Department's denial of their claim for refund of income taxes withheld from their wages.

9. On August 30, 2000, the Department acknowledged the Taxpayers' protest.

10. On March 27, 2001, Terri Holt sent the Department a letter inquiring as to the status of the Taxpayers' protest.

11. On April 25, 2001, the Department's attorney filed a Request for Hearing.

12. On April 27, 2001, the Department's hearing officer sent a letter to the Taxpayers scheduling a hearing on their protest for August 13, 2001.

DISCUSSION

The issue to be determined is whether the Department properly denied the Taxpayers' claim for refund of 1999 state income tax withheld by their employers in the amount of $2,009.00. The

Taxpayers have raised the following arguments in support of their protest: (1) the wages the Taxpayers earned from the performance of personal services are not subject to New Mexico income tax because those wages are not "income" for purposes of reporting federal income tax; (2) the State of New Mexico does not have authority to recalculate the federal adjusted gross income reported on the Taxpayers' federal income tax return and must accept the zero returns filed by the Taxpayers; (3) the Taxpayers' refund should be granted because the Department failed to set a prompt hearing on the Taxpayers' protest as required by Section 7-1-24 NMSA 1978.

(1) Taxation of Compensation for Personal Services. The Taxpayers argue that the wages they earned from their employment with PNM and BGK Asset Management Corporation during 1999 are not subject to New Mexico income tax because those wages are not "income" for purposes of reporting federal income tax. In order to understand the relationship between federal and state income taxation, a brief overview of New Mexico's personal income tax statutes and their operation is necessary.

New Mexico imposes income tax on the net income of "every resident individual". New Mexico is among the majority of states that "piggy-back" or use the federal income tax system as the basis for calculating state income taxes. The calculation of state income taxes begins with a determination of "base income" which is the taxpayer's "adjusted gross income" as defined in Section 62 of the Internal Revenue Code ("IRC"), plus net operating loss deductions which can be deducted for federal purposes but which New Mexico does not allow to be deducted in the same manner. *See,* Section 7-2-2(B) NMSA 1978. New Mexico then allows certain deductions, such as the federal standard or itemized deductions and deductions for income from federal obligations, to arrive at "net income" upon which income tax is imposed. *See*, Sections 7-2-2(N) and 7-2-3 NMSA 1978. Given the structure of New Mexico's income tax, the resolution of the Taxpayers' protest requires an examination of IRC provisions relating to the determination of federal adjusted gross income.

The IRC (26 U.S.C. Section 1 *et. seq*.) defines adjusted gross income as gross income, less certain deductions listed in IRC Section 62. Gross income is defined in Section 61:

> Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items*:*
>
> (1) Compensation for services, including fees, commissions, fringe benefits and similar items;
> (2) Gross income derived from business;
> (3) Gains derived from dealings in property;
> (4) Interest;
> (5) Rents;
> (6) Royalties;
> (7) Dividends;
> (8) Alimony and separate maintenance payments;
> (9) Annuities;
> (10) Income from life insurance and endowments contracts;
> (11) Pensions;
> (12) Income from discharge of indebtedness;
> (13) Distributive share of partnership gross income;
> (14) Income in respect of a decedent; and,
> (15) Income from an interest in an estate or trust.

This definition is quite broad, and certainly appears to include under the category of "compensation for services" the compensation the Taxpayers received from performing services for their employers in New Mexico. The Taxpayers nonetheless dispute the applicability of Section 61 to their wages.

First, the Taxpayers reference the definition of "gross income" in the 1939 version of the IRC to support their position that this term does not include wages under the 1954 version of the Code. The 1939 definition of gross income read, in pertinent part:

> "Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service (including personal service as an officer or employee of a State or political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing), of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever....

The Taxpayers point out that while the 1939 version of the IRC specifically included "wages, or compensation for personal service" within the definition of gross income, the 1954 version (which was

redesignated the "Internal Revenue Code of 1986" by Public Law 99-514, Sec. 2, Oct. 22, 1986) makes no mention of wages, but is limited to "compensation for services, including fees, commissions, fringe benefits and similar items." The Taxpayers argue that this change in the language defining gross income had the effect of excluding wages from federal income taxation.

The Taxpayers' argument might have some merit if the only change made to the statute had been the deletion of the phrase "income derived from salaries, wages, or compensation for personal service". In this case, however, the definition of gross income contained in the 1939 Code was completely restructured and rewritten in the 1954 Code. Under these circumstances, the change in the language of one portion of the statute has little significance. There are numerous court cases decided after enactment of the 1954 Code holding that wages are included in the definition of "gross income." *See e.g.*, *United States v. Gerads*, 999 F.2d 1255, 1256 (8th Cir. 1993), where the court held that "wages are within the definition of income under the Internal Revenue Code and the Sixteenth Amendment, and are subject to taxation." quoting *Denison v. Commissioner,* 751 F.2d 241, 242 (8th Cir.1984) (per curiam), *cert. denied*, 471 U.S. 1069 (1985). Similarly, in *Grimes v. Commissioner*, 806 F.2d 1451, 1453 (9th Cir. 1986), the court found that "Sections 1 and 61 of the Internal Revenue Code impose a tax on income, and wages are income." *See also*, the cases referenced on pages 7-9, *infra*. Given these decisions, there is no merit to the Taxpayers' contention that the 1954 change in the definition of gross income set out in Section 61 of the IRC had the effect of eliminating the income tax on wages.

The Taxpayers' next contention is that the income tax applies only to corporate profits and not to wages for personal services. The Taxpayers maintain the definition of "gross income" in IRC Section 61 is fatally flawed because it defines gross income by reference to the word "income", which is not separately defined in the IRC. Accordingly, the Taxpayers believe the determination of whether a particular type of income is subject to tax must be derived from case law. The Taxpayers rely on several

passages from early United States Supreme Court decisions to support their position that case law limits imposition of the income tax to corporate profits.

In *Doyle v. Mitchell Brothers Co*., 274 U.S. 179, 185 (1918), which concerned an action to recover taxes assessed under the Corporation Excise Tax Act of 1909, the Court stated:

> Whatever difficulty there may be about a precise and scientific definition of "income" it imports, as used here, something entirely distinct from principal or capital either as a subject of taxation or as a measure of the tax; conveying rather the idea of gain or increase arising from corporate activities....

Based on this language, the Taxpayers conclude that only profit from corporate activities is subject to income tax. But when the Court stated that the term income "as used here" meant gain or increase from corporate activities, the Court was referring solely to the matter at issue, *i.e.,* whether the gain Mitchell Brothers Co. realized on the sale of capital assets was subject to the corporation income tax. The decision has no application to the issue in this case, which is whether the Taxpayers' wages are subject to tax under the Income Tax Act.

In *Merchant's Loan & Trust Co. v. Smeitanka*, 255 U.S. 509 (1921), the Court held that the appreciation in the value of stock sold by the trustee of a decedent's estate was subject to the Income Tax Act of 1916. In reaching its decision, the Court found that the word "income" had the same meaning in the Income Tax Acts of 1913, 1916 and 1917 as it had in the Corporation Excise Tax Act of 1909:

> [T]here would seem to be no room to doubt that the word must be given the same meaning in all of the Income Tax Acts of Congress that was given to it in the Corporation Excise Tax Act, and that what that meaning is has now become definitely settled by decisions of this Court.

Id. at 519. The Taxpayers maintain that since the definition of "income" under the Income Tax Act is the same as that under the Corporation Excise Tax Act, the income tax is limited to corporate profits. This is too narrow a reading of the *Merchant's Loan* decision. The definition of income referenced by the Supreme Court appears in the Court's earlier decisions in *Stratton's Independence v. Howbert*, 231 U.S. 399, 415 (1913) and *Eisner v. Macomber*, 252 U.S. 189, 207 (1920), both of

which defined income as "gain derived from capital, from labor, or from both combined", with the Eisner case adding to the definition of income "profit gained through sale or conversion of capital assets". Based on this definition, corporations *and* individuals are subject to tax on gain realized from capital assets (such as stocks, bonds, and real estate) or from labor (such as construction, manufacturing, or personal services).

The Taxpayers do not believe the wages they earn from personal services represent taxable gain or profit. This argument has been raised by other taxpayers and has been soundly rejected by the courts. In *United States v. Buras*, 633 F.2d 1356, 1361 (9th Cir. 1980), the Ninth Circuit addressed the issue as follows:

> According to Buras...the wage earner exchanges his labor and personal time for its equivalent in money, he derives no gain and therefore cannot be taxed. Appellant's argument is refuted by one of the cases he cites. In *Stratton's Independence, Ltd. v. Howbert*, 231 U.S. 399, 415, 34 S.Ct. 136, 140, 58 L.Ed. 285 (1913), the Court did define income as gain derived from labor. The Court went on to explain, however, that "the earnings of the human brain and hand when unaided by capital" are commonly treated as income. *Id*.

There is a large body of federal case law upholding the imposition of federal income tax on wages. Quotations from just a few of those cases are set out below:

Coleman v. Commissioner, 791 F.2d 68, 70 (7th Cir. 1986): "Coleman says that wages may not be taxed because they come from his person, a depreciating asset. The personal depreciation offsets the wage, leaving no net income. Coleman thinks that only net income may be taxed under the Sixteenth Amendment—net income as Coleman defines it, not as Congress does.... These are tired arguments. The code imposes a tax on all income. See, 26 U.S.C. § 61. Wages are income, and the tax on wages is constitutional."

Casper v. Commissioner, 805 F.2d 902, 904-905 (10th Cir. 1986): "Appellant's contention that the amounts he received from his employers constituted an equal, nontaxable exchange of property rather than taxable income is clearly without merit. This court specifically rejected this argument in *United States v. Lawson*, 670 F.2d 923, 925 (10th Cir. 1982), as did the Tax Court in

Rowlee v. Commissioner, 80 T.C. 1111, 1119-22 (1983).... Value received in exchange for services constitutes taxable income pursuant to I.R.C. § 61(a)(1)."

Connor v. Commissioner, 770 F.2d 17, 20 (2d Cir. 1985): "The taxpayer next argues that wages are not income but an exchange of property. As money is property and labor is property, so his argument goes, his work for wages is a non-taxable exchange of property. Wrong again. Wages are income. *See, e.g., Schiff v. Commissioner*, 751 F.2d 116, 117 (2d Cir. 1984). The argument that they are not has been rejected so frequently that the very raising of it justifies the imposition of sanctions."

Olson v. United States, 760 F.2d 1003, 1005 (9th Cir. 1985): "Olson's attempts to escape tax by deducting his wages as 'cost of labor' and by claiming that he had obtained no privilege from a governmental agency illustrate the frivolous nature of his position. This court has repeatedly rejected the argument that wages are not income as frivolous, *see, e.g., Gattuso v. Pecorella*, 733 F.2d 709, 710 (9th Cir. 1984); *United States v. Romero*, 640 F.2d 1014, 1016 (9th Cir. 1981), and has also rejected the idea that a person is liable for tax only if he benefits from a governmental privilege."

United States v. Koliboski, 732 F.2d 1328, 1329 n.1 (7th Cir. 1984): "[T]he defendant's entire case at trial rested on his claim that he in good faith believed that wages are not income for taxation purposes. Whatever his mental state, he, of course, was wrong, as all of us already are aware. Nonetheless, the defendant still insists that no case holds that wages are income. Let us now put that to rest: WAGES ARE INCOME. Any reading of tax cases by would-be tax protesters now should preclude a claim of good-faith belief that wages—or salaries—are not taxable." (emphasis in original).

United States v. Lawson, 670 F.2d 923, 925 (10th Cir. 1982): "The defendant's wages for personal services are income under the Internal Revenue Code.... Notwithstanding Lawson's belief that his wages are not gains or profits but merely what he has received in an equal exchange for his services, the Internal Revenue Code clearly includes compensation of this nature within reportable gross income."

Peth v. Breitzmann, 611 F. Supp. 50, 53 (E.D.Wis. 1985): "[Peth] states that the income taxes are directed to taxable gain. Because he receives a paycheck for his labor, and because the paycheck is equal to the fair market value of his labor, he argues there is no gain. No court has ever accepted this argument for the purpose of determining taxable income. Indeed, it has always been rejected. For once and for all, wages are taxable income. *Granzow v. Commissioner of Internal Revenue*, 739 F.2d 265, 267 (7th Cir. 1984)."

In *Cheek v. United States*, 498 U.S. 192 (1991), the Supreme Court addressed the issue of whether a good faith misunderstanding of the law could be a defense to criminal charges of willfully failing to file a federal income tax return and willfully attempting to evade income taxes. The Court held that a good faith belief that one is not violating the law can negate willfulness, stating:

> In this case, if Cheek asserted that he truly believed that the Internal Revenue Code did not purport to treat wages as income, and the jury believed him, the Government would not have carried its burden to prove willfulness, *however unreasonable a court might deem such a belief*. Of course, in deciding whether to credit Cheek's good-faith belief claim, the jury would be free to consider any admissible evidence from any source showing that Cheek was aware of his duty to file a return and to treat wages as income, including...any contents of the personal income tax return forms and accompanying instructions that made it plain that wages should be returned as income. (emphasis added).

Id. at 202. Justice Blackmun, joined by Justice Marshall, dissented, finding Mr. Cheek's belief that wages are not income too unreasonable to be accepted as a defense:

> [I]t is incomprehensible to me how, in this day, more than 70 years after the institution of our present federal income tax system with the passage of the Revenue Act of 1913, 38 Stat. 166, any taxpayer of competent mentality can assert as his defense to charges of statutory willfulness the proposition that the wage he receives for his labor is not income, irrespective of a cult that says otherwise and advises the gullible to resist income tax collections.

Id. at 209-210.

The cases listed above are just a sample of the hundreds of cases addressing the taxability of wages. There really is no question that the Taxpayers' compensation for personal services performed in New Mexico come within the definition of "gross income" in IRC Section 61 and are subject to both

federal and state income tax. The Taxpayers appear to be intelligent people who are sincere in their beliefs. Nonetheless, those beliefs are clearly wrong. In conducting their research, they have misconstrued or taken out of context several passages from early Supreme Court cases that do not support their contentions. They have apparently failed to find—or refused to accept—more recent cases which are directly applicable to the arguments they raise. As Justice Blackmun noted in *Cheek*, *supra,* it is almost incomprehensible that the Taxpayers could believe their wages were not subject to federal income tax. This is particularly true given the large body of case law to the contrary and the fact that millions of other citizens routinely report and pay such income taxes every year.

Authority of the State to Recalculate Federal Adjusted Gross Income. The Taxpayers maintain the Department does not have authority to make an independent determination of their federal adjusted gross income when calculating income tax due to New Mexico. It is their position that until the Internal Revenue Service makes an adjustment to the Taxpayers' 1999 federal income tax return, the Department is bound to accept the zero federal adjusted gross reported on the Taxpayers' return.

The Taxpayers cite no legal authority to support their contentions. There is long-standing authority, however, to support the Department's position that New Mexico may impose and administer states taxes according to its own laws without oversight by the federal government. In *Michigan Central Railroad Co. v. Powers*, 201 U.S. 245, 292-293 (1906) the United States Supreme Court made the following observation:

> We have had frequent occasion to consider questions of state taxation in the light of the Federal Constitution, and the scope and limits of national interference are well settled. There is no general supervision on the part of the nation over state taxation, and, in respect to the latter, the state has, speaking generally, the freedom of a sovereign, both as to objects and methods.

Accordingly, the Taxpayers' challenge to the Department's authority to redetermine their federal adjusted gross income for purposes of calculating New Mexico state income tax must be resolved by reference to state law.

The Taxation and Revenue Department is established under the Taxation and Revenue Department Act, Sections 9-11-1 *et seq*. NMSA 1978. As stated in Section 9-11-3, the purpose of the Act "is to establish a single, unified department to administer all laws and exercise all functions relating to taxation, revenue and vehicles charged to the department." The Department's administration of most of the state's tax laws, including the Income Tax Act, is governed by the Tax Administration Act. *See*, Section 7-1-2(A)(1) NMSA 1978.

Section 7-1-4 NMSA 1978 of the Tax Administration Act gives the Department authority to investigate and determine tax liabilities. Subsection A of Section 7-1-4 specifically provides:

> A. For the purpose of establishing or determining the extent of the liability of any person for any tax, for the purpose of collecting any tax or for the purpose of enforcing any statute administered under the provisions of the Tax Administration Act, the secretary or the secretary's delegate is authorized to examine equipment and to examine and require the production of any pertinent records, books, information or evidence, to require the presence of any person and to require that person to testify under oath concerning the subject matter of the inquiry and to make a permanent record of the proceedings.

The statute gives the Secretary or his delegates authority to investigate and determine the extent of liability of any person for any tax. This language is sufficiently broad to authorize the Department to make its own, independent determination of the Taxpayers' income tax liability to the state.

The calculation of an individual's New Mexico income tax starts with adjusted gross income. This term is defined in Section 7-2-2(A) NMSA 1978 of the Income Tax Act to mean "adjusted gross income *as defined in Section 62 of the Internal Revenue Code*" (emphasis added). The statute does not limit the meaning of adjusted gross income to the income reported on a taxpayer's return. Although the Taxpayers in this matter maintain that only the Internal Revenue Service can determine a taxpayer's federal adjusted gross income, the fact is that tax preparers and professionals, as well as millions of individuals, make this determination every time they complete and file a federal income tax return. The Department has as much or more expertise than do the Taxpayers in determining whether a particular type of income comes within the definition of adjusted gross income set out in the IRC. Given the

investigative authority provided in Section 7-1-4 NMSA 1978, the Department was justified in changing the federal adjusted gross income reported on the Taxpayer's New Mexico income tax return to include their wages from performing services in New Mexico. The Taxpayers' belief that only the Internal Revenue Service can determine a taxpayer's federal adjusted gross income for purposes of calculating state income tax is incorrect.[1]

Delay in Setting a Hearing. Section 7-1-24(D) NMSA 1978 states: "Upon timely receipt of a protest, the department or hearing officer shall promptly set a date for hearing and on that date hear the protest or claim." The Taxpayers' protest of the Department's denial of their refund was filed on May 17, 2000. On March 27, 2001, Terri Holt sent the Department a letter asking about the status of the protest. On April 25, 2001, the Department's attorney filed a Request for Hearing, and on April 27, 2001, the Department's hearing officer scheduled a hearing for August 13, 2001. The Taxpayers maintain that the fifteen-month delay between the May 2000 protest and the August 2001 hearing violates the prompt hearing provision in Section 7-1-24 NMSA 1978 and requires the hearing officer to enter a decision granting the Taxpayers' refund.

The argument that a taxpayer who does not receive a prompt hearing is relieved of their tax obligations to the state has been considered—and rejected—by the courts. In *In re Ranchers-Tufco Limestone Project Joint Venture*, 100 N.M. 632, 635, 674 P.2d 522, 525 (Ct. App.), *cert. denied,* 100 N.M. 505, 672 P.2d 1136 (1983), the Court of Appeals addressed this issue as follows:

> Assuming, but not deciding, that the tax collector violated Section 7-1-24(D), how does a taxpayer benefit from the violation? The statute says nothing as to the consequence of a violation. The general rule is that tardiness of public officers in the performance of statutory duties is not a defense to an action by the state to enforce a public right or to protect public interests. *State, ex rel. Dept. of Human Services v. Davis*, 99 N.M. 138, 654 P.2d 1038 (1982). The general rule

[1] A more difficult issue would be posed if the Internal Revenue Service and the Department made conflicting determinations of the amount of a given taxpayer's federal adjusted gross income. That is not the case here. The Taxpayers have not received the refund requested on their 1999 federal income tax return. They testified that while they had not been served with any formal notices or assessments, they were having "discussions" with the Internal Revenue Service concerning their 1999 return.

> is applicable in these cases unless Section 7-1-24(D) makes it inapplicable. Section 7-1-24(D) does not make the general rule inapplicable.
>
> Even if the general rule did not apply, the taxpayers have not demonstrated that they have been harmed by the delay in deciding their protests. The taxpayers assert that the delay, in itself, was prejudicial because "we're uncertain as to what it's going to cost us in the future to produce uranium in the State of New Mexico, and how we can make a sales contract that will permit us to be competitive with other states and with other countries****" They also assert: "The recall of potential witnesses has been clouded by the passage of time." These items were insufficient to show prejudice....

In this case, the fifteen-month delay between the date of the protest and the date of the hearing is considerably shorter than the almost three-year delay addressed in *Ranchers-Tufco*. In addition, the Taxpayers did not introduce any evidence of prejudice, other than their natural desire to have this matter resolved. Based on existing New Mexico law, the Department's delay in setting a hearing on the Taxpayers' protest does not provide a basis for granting the Taxpayers' refund.

Summary. The Taxpayers are now on notice that there is no legal merit to the arguments on which they have relied in failing to report and pay personal income tax to the State of New Mexico. New Mexico makes it a felony to file false returns or to evade taxes, *see,* Sections 7-1-72 and 7-1-73 NMSA 1978, and imposes a 50% of tax civil penalty for the fraudulent failure to pay any tax required to be paid. Section 7-1-69(C) NMSA 1978. Unless this decision is reversed by the New Mexico Court of Appeals, the Taxpayers may be faced with such consequences if they continue to file returns in the same manner as they filed their 1999 state income tax return. As the court stated in *Coleman v. Commissioner,* 791 F.2d 68, 69 (7th Cir. 1986):

> Some people believe with great fervor preposterous things that just happen to coincide with their self-interest. "Tax protesters" have convinced themselves that wages are not income, that only gold is money, that the Sixteenth Amendment is unconstitutional, and so on. These beliefs all lead—so tax protesters think—to the elimination of their obligation to pay taxes. The government may not prohibit the holding of these beliefs, *but it may penalize people who act on them.* (emphasis added).

CONCLUSIONS OF LAW

1. The Taxpayers filed a timely, written protest pursuant to Sections 7-1-26 and 7-1-24 NMSA 1978 to the Department's denial of their claim for refund and jurisdiction lies over the parties and the subject matter of this protest.

2. The Taxpayers' compensation from their employment in New Mexico comes within the definition of "gross income" and "adjusted gross income" in the Internal Revenue Code.

3. The Taxpayers' compensation comes within the definitions of "base income" and "net income" in New Mexico's Income Tax Act.

4. The Taxpayers' 1999 wages were subject to New Mexico income tax, and the Taxpayers are not entitled to a refund of the income tax withheld from those wages.

5. The Department has the authority and responsibility to ensure that persons subject to tax in New Mexico properly report, calculate and pay their taxes to the Department. Pursuant to this authority, the Department may make its own determination, independently from the Internal Revenue Service, as to whether taxpayers are properly reporting and calculating income taxes due to the state.

6. The Department's delay in setting a hearing on Taxpayers' protest does not provide a basis for granting the Taxpayers' refund.

For the foregoing reasons, the Taxpayers' protest IS DENIED.

Dated August 22, 2001.