

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

IN THE MATTER OF THE PROTEST OF
DON BASS
PROTEST TO DENIAL OF CLAIM FOR REFUND

NO. 97-33

DECISION AND ORDER

This matter came on for formal hearing before Gerald B. Richardson, Hearing Officer, on February 24, 1997. Don Bass represented himself at the hearing. The Taxation and Revenue Department, hereinafter, Department, was represented by Frank D. Katz, Chief Counsel. Following the hearing the Hearing Officer requested that Mr. Bass clarify the issues he was raising, and cite to facts of record and legal authority in support of his position on those issues. The Department responded to Mr. Bass' submission and Mr. Bass was given the opportunity to respond to the Department. The final submission was by Mr. Bass on July 24, 1997 and the matter was considered submitted for decision at that time.

Based upon the evidence and the arguments submitted, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. Mr. Bass was born in Heidelberg, Germany as a dependent of a family in the United States military service.
2. Mr. Bass is a citizen of the United States.
3. Mr. Bass has lived in Albuquerque, New Mexico since 1981 and is a citizen and resident of New Mexico.
4. During 1995, Mr. Bass was employed by Manana Gas, Inc. in their accounting department and was paid \$49,000 in wages.
5. Manana Gas, Inc. withheld \$2,127 in New Mexico income withholding tax from the wages it paid Mr. Bass in 1995.
6. On February 6, 1996, Mr. Bass filed a 1995 New Mexico personal income tax return with the Department which reported zero Federal adjusted gross income on line 7 of the return and requested a refund of the \$2,127 of New Mexico income tax withheld from his wages.
7. On April 4, 1996, the Department denied Mr. Bass' claim for refund.
8. On May 8, 1997 Mr. Bass filed a written protest to the Department's denial of his claim for refund.
9. Mr. Bass also filed a 1995 federal income tax return with the Internal Revenue Service which reported zero Federal adjusted gross income.
10. There has been no determination by the Internal Revenue Service for tax year 1995 with respect to Mr. Bass' claim that he had zero Federal adjusted gross income.

DISCUSSION

The determination of Mr. Bass' protest herein ultimately depends upon the determination of whether the wages paid Mr. Bass for services rendered as an employee of Manana Gas, Inc. are subject to New Mexico's personal income tax. Mr. Bass has raised a number of legal arguments as to why his wages are not subject to income taxation which will be addressed individually. Prior to such discussion, however, New Mexico's personal income tax system will be explained.

New Mexico imposes its income tax upon the net income of "every resident individual". New Mexico is among the majority of states which "piggy-back" or use the federal income tax system as the basis for calculating state income taxes. The calculation of personal income taxes in New Mexico begins with a determination of "base income" which is defined to be the taxpayer's "adjusted gross income" as defined in Section 62 of the Internal Revenue Code, plus certain net operating loss deductions which can be deducted for federal purposes in arriving at federal adjusted gross income but which New Mexico does not allow to be deducted in the same manner. *See*, NMSA 1978, § 7-2-2(B). 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*, NMSA 1978, 7-2-2(N) and 7-2-3. Because Mr. Bass' arguments are, in essence, directed at the legality of the federal income tax, and provisions of the Internal Revenue Code which provide the basis for calculating New Mexico's income tax, the Internal Revenue Code, and the federal authority interpreting it and the United States Constitution will be consulted to determine Mr. Bass' protest.

First, Mr. Bass argues that he is not subject to the jurisdiction of "the internal revenue service for reasons of my alienage to the State of the forum of United States Tax Laws." (Mr. Bass' submittal of May 11, 1997, p.7). By this, I understand Mr. Bass to argue that he is not

subject to the Internal Revenue Code. Mr. Bass bases this argument upon several premises. First, he argues that federal legislation applies only within the territorial jurisdiction of the United States, unless a contrary intent appears in the statute. This decision maker has no quarrel with this proposition and would direct Mr. Bass' attention to the Organic Act Establishing the Territory of New Mexico, (Sept. 9, 1850, 9 Stat. 446, ch. 49), which established the Territory of New Mexico; the joint resolution of Congress to admit the Territory of New Mexico into the union as a state, (Aug. 21, 1911, No. 8, 37 Stat. 39) and the presidential Proclamation Admitting New Mexico as a State Into the Union, (Jan. 6, 1912, 37 Stat. 1723). New Mexico is clearly within the territorial jurisdiction of the United States. Mr. Bass' second premise under this argument is that if federal legislation is restricted to the United States and its territories, that it does not apply to the citizens of the fifty states unless the legislation specifically states such applicability. Mr. Bass supports this argument, somehow, with the concept that the people of the United States, because we are a republican form of government, are sovereign. Mr. Bass then cites to *United States v. Fox*, 94 U.S. 315 (1876) for the following quote:

Since in common usage, the term person does not include the Sovereign, statutes not employing the phrase are ordinarily construed to exclude it.

I have researched the case and could not find the quoted material. What I did find was this:

The term "person" as here used applies to natural persons, and also to artificial persons, --bodies politic, deriving their existence and powers from legislation,--but cannot be so extended as to include within its meaning the Federal government.

94 U.S. at 321.

This case is clearly inapplicable because it dealt with a situation where the sovereign was the Federal government, not the people, and the terms were not being used synonymously as Mr. Bass does in his argument. When the terms are used synonymously, there is no need to iterate each synonym for the people of the United States to include them within the terms of the statute. It would merely be redundant. Thus, the failure of the Internal Revenue Code to refer to persons as sovereigns in no way restricts the Code from applying to persons who may also consider themselves as sovereign. Furthermore, while I do not quibble with the concept that the power of our form of government derives from the people, and that therefore, they can be called sovereign, in our form of government, the people exercise their power of government through their elected representatives to Congress, and under the Constitution, which was passed by the people, the power to enact laws to govern all of the people has been granted to Congress. United States Constitution, Article 1. In this regard, it is noteworthy that in Article 1, Section 8, the people explicitly granted Congress the power to "lay and collect Taxes, Duties, Imposts and Excises..." Although Mr. Bass claims that he is a United States citizen under the Constitution, he denies being a citizen under Article 1, Section 8 of the Constitution. I know of no authority which allows citizens to select the constitutional provisions to which they are subject. The Constitution was enacted as a whole, and amended from time to time, by the people. As such, it applies in whole to the citizens of this country.

Mr. Bass' next argument is premised upon his first. Since New Mexico's income tax is based upon the Internal Revenue Code and since Mr. Bass believes he is not subject to the Internal Revenue Code, he believes that New Mexico's Income Tax Act does not apply to him. As noted above, his argument that he is not subject to the Internal Revenue Code is without merit.

Next, Mr. Bass makes certain arguments with respect to the applicability of certain provisions of the Internal Revenue Code. Specifically, he argues that he has zero federal adjusted gross income. The Internal Revenue Code defines adjusted gross income to be gross income, less certain deductions which are listed in Section 62 of the Code. Gross income is defined in Section 61 of the Code as follows:

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.

26 U.S.C. § 61 (1997). This definition is quite broad and inclusive, and is certainly broad enough to include under the first listed category of compensation for services the wages or salary paid by Manana Gas, Inc. to Mr. Bass.

Mr. Bass' next argument is that he has zero "net income" as defined in New Mexico's income tax act. As noted above, New Mexico's definition of "net income" begins with the definition of "base income" which is defined as federal adjusted gross income, and then certain deductions are allowed. Since Mr. Bass' wages fall within the definition of adjusted gross income under the Internal Revenue Code, this argument is without merit.

Next, Mr. Bass argues that he is not a "taxpayer" as defined by Title 26 CFR. Mr. Bass quoted the definition at 26 CFR § 7701 as stating, "The term "taxpayer" means person subject to any internal revenue tax." The Internal Revenue Code imposes an income tax upon the taxable income of individuals. 26 U.S.C. §1. Taxable income is defined to mean gross income minus the deductions allowed in Chapter 1 of the Internal Revenue Code, which covers §§ 1-1398 of 26 U.S.C. As noted above, gross income clearly includes wages paid individuals. Since wages are taxable income, Mr. Bass meets the definition of a taxpayer.

Mr. Bass also argues that he is not a "taxpayer" as defined in New Mexico's Income Tax Act. "Taxpayer" is defined at § 7-2-2(Z) NMSA 1978 to mean, "any individual subject to the tax imposed by the Income Tax Act. Section 7-2-3 NMSA 1978 provides for the imposition of income tax. It provides that:

A tax is imposed at the rates specified in the Income Tax Act upon the net income of every resident individual and upon the net income of every nonresident individual employed or engaged in the transaction of business in, into or from this state, or deriving any income from any property or employment within this state.

Mr. Bass is a resident of New Mexico who derives income from employment in this state. This argument is also meritless.

Mr. Bass has cited to a number of old federal cases in support of his protest. In more than one instance, he has provided quotes from them which do not exist and in general, he has misconstrued their meaning. Before responding to his reliance upon these cases, they will be briefly summarized and explained to provide a context for the discussion of Mr. Bass' arguments.

The cases relied upon by Mr. Bass were part of the evolution of the law concerning the power of Congress to impose an income tax and turned upon the limitations on Congress' power to impose taxes contained in Article 1, §2, Cl. 3 and Article 1, §9, Cl. 4 of the Constitution. Article 1, §2, Cl. 3 of the United States Constitution provides that:

Representatives *and direct taxes* shall be apportioned among the several States which may be included in this Union,.... (emphasis added)

Additionally, Article 1, §9, Cl.4 provides that:

No Capitation or other direct, Tax shall be laid, unless in Proportion to the Census or Enumeration herein before directed to be taken. (emphasis added, capitalization in original)

These clauses became the basis of the Supreme Courts determination that the Income Tax Act of 1894 was unconstitutional. The Court held that the income tax was unconstitutional because it imposed a tax on income from real estate. The Court ruled that this was the equivalent of a direct tax on the real estate itself, and since the tax was not apportioned, it violated these clauses of the Constitution. *Pollock v. Farmers Loan and Trust Co.*, 157 U.S. 429 (1895). The ruling in this case effectively thwarted the imposition of an income tax in this country for some years thereafter.

In 1909, Congress passed a law imposing an excise tax on corporation of 1% of net income. This tax was challenged on the same grounds as the 1894 income tax. In *Flint, v. Stone Tracy Company*, 220 U.S. 107 (1911), however, the Supreme Court upheld that tax, ruling that the tax was an "excise tax" and therefore not a direct tax which would be unconstitutional because it was not apportioned. Thus, the determination of whether a tax was an "excise tax" or a "direct tax" became crucial to the constitutionality of a tax. This concern was eliminated, however, by the passage of the Sixteenth Amendment to the Constitution. It provides as follows:

The Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration.

The first case to be decided by the Supreme Court following the passage of the Sixteenth Amendment which challenged the constitutionality of the income tax was *Brushaber v. Union Pacific Railroad Co.*, 240 U.S. 1, 36 S. Ct. 236 (1916). In that case a stockholder of the Union Pacific brought an action to restrain the company from paying income tax on the grounds of the unconstitutionality of the income tax provisions of the Tariff Act of 1913. The income tax was held to be constitutional. In doing so, the Court reiterated the inherent power of Congress to impose an income tax under Article 1, §8, and found that the Sixteenth Amendment had merely removed the requirement that such taxes be apportioned among the states. Of particular interest in the Court's decision is its discussion of the power of Congress to tax under Article 1, §8:

That the authority conferred upon Congress by §8 of article 1 "to lay and collect taxes, duties, imposts and excises" is exhaustive and embraces every conceivable power of taxation has never been questioned, or, if it has, has been so often authoritatively declared as to render it necessary only to state the doctrine. And it has also never been questioned from the foundation, without stopping presently to determine under which of the separate headings the power was properly to be classed, that there was authority given, as

the part was included in the whole, to lay and collect income taxes.

240 U.S. at 12-13.

With this background, Mr. Bass' additional arguments will now be addressed. Mr. Bass argues that *Brushaber* held that the sixteenth amendment, as correctly interpreted, and the federal income tax are constitutional because they are restricted to the classification of indirect or excise taxes. As the above discussion about the development of the federal law with respect to income taxes makes clear, the Sixteenth Amendment did away with any need to examine whether a tax is a direct tax, which was required to be apportioned, or whether it was an indirect tax, to determine its constitutionality. With this limitation removed, what remained was Congress' inherent and "exhaustive" authority to impose taxes, including income taxes. *Brushaber, supra*.

Mr. Bass also cites to a number of cases which discuss the "right to labor" as a fundamental right protected by the Constitution. From this, he concludes that when a citizen is exercising his or her right to labor, the compensation received is not "income" subject to any income or other revenue tax. In support of this argument, Mr. Bass provides the following quotation from *Brushaber*, and provides a page reference that it can be found at page 241 of the Supreme Court Reporter volume in which the case is printed. The quotation provided was:

income has been taken to mean the same thing as used in the Corporate excise tax of 1909 (36 Stat. 112). The individual worker does not receive a profit or gain from his/hers labors--merely an equal exchange of funds for services."

I have searched the page referenced and can find no language resembling the above quotation. What I did find, however, was a discussion by the Court of its earlier *Pollock* case. With respect to an income tax on income from "professions, trades, employments, or vocations", the court

stated as follows:

...in the Pollock Case, in so far as the law taxed incomes from other classes of property than real estate and invested personal property, that is, income from "professions, trades, employments, or vocations" (159 U.S. 637), its validity was recognized; indeed, it was expressly declared that no dispute was made upon that subject, and attention was called to the fact that taxes on such income had been sustained as excise taxes in the past.

36 S.Ct. 236, 241. Thus, it can hardly be argued that *Brushaber* stands for the proposition that the Federal government may not tax income arising from an individual's exercise of his right to labor or that such income is not "income" within the meaning of the Internal Revenue Code. Referring back to the earlier quotation from *Brushaber* discussing Congress' power to impose taxes, which was described as "exhaustive" and as embracing "every conceivable power of taxation", Mr. Bass' argument that Congress may not tax income arising from the exercise of the fundamental right to labor is simply erroneous.

At the hearing in this matter I was struck with both Mr. Bass' intelligence and his sincerity in his belief that the Federal income tax, and thus, New Mexico's income tax which is based upon determining federal adjusted gross income, were illegally and improperly applied to his earnings from employment. I asked Mr. Bass about his education and he informed me that he was college educated, with a degree in engineering. Thus, Mr. Bass is clearly capable of reading and understanding the law, even as a layman. Yet, the authorities cited in his written submissions are often misconstrued and contain quotations which cannot be found in the cases themselves. From this, I can only conclude that Mr. Bass did not actually read the cases themselves and my hunch is that he has learned what he espouses from some indirect source. I am seeing more and more of the same arguments arise in the context of the administrative hearing process and the movement

which is propounding these arguments is called the tax protester or tax resister movement. The arguments propounded are often elaborately structured and rely upon quotations either misconstrued, taken out of context, or from cases which are no longer current law, such as cases decided prior to the adoption of the Sixteenth Amendment. Clearly, someone has taken great pains to construct such arguments and to research archaic law. Yet, my review of the law challenging the Federal income tax reveals numerous recent cases which directly address the many arguments propounded by the tax resister movement. Surely, these cases are as easily located and researched as the archaic ones. I would suggest to Mr. Bass that he has been sold a bill of goods and I would direct him to one case in particular, which addresses the standard tax resister arguments and cites to numerous federal cases upholding federal income taxes in the face of these arguments, and I would urge him to read it and the other cases cited therein. In *Coleman v. Commissioner of Internal Revenue*, 791 F.2d 68, the Seventh Circuit Court of Appeals addressed the consolidated cases of Mr. Norman Coleman and Mr. Gary Holder. Both of these individuals had argued that their wages were not subject to federal income taxation. The court had this to say about those arguments:

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. Holder, who styles himself a "private citizen," insists that wages may not be taxed because the Sixteenth Amendment authorizes only excise taxes, and in Holder's world excises may be imposed only on "government granted privileges." Because Holder believes that he is exercising no special privileges, he thinks he may not be taxed. ***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. See, among hundreds of other cases, United States v. Thomas, 788 F.2d 1250, 1253 (7th Cir. 1986);***

Lovell v. United States, 755 F.2d 517 (7th Cir. 1984); *Granzow v. CIR*, 739 F.2d 265, 267 (7th Cir. 1984); *United States v. Koliboski*, 732 F.2d 1328, 1329 & n. 1 (7th Cir. 1984). See also *Brushaber v. Union Pacific R.R.*, 240 U.S. 1, 12, 24-15, 36 S.Ct. 236, 239, 244-45, 60 L.Ed. 2d 493 (1916).

Id. at 70. As this case and the cases cited therein indicate, there is really no question that Mr. Bass' income from wages he earned in New Mexico are income for federal tax purposes, and as such, would be included in federal adjusted gross income for federal purposes, and by inference, for purposes of calculating New Mexico personal income taxes.

I would leave Mr. Bass with the following admonition:

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).

The federal caselaw contains hundreds of cases where tax protesters have been sent to prison for tax evasion or fined substantially for filing frivolous returns based upon the theories espoused by the tax protester movement. New Mexico also makes it a felony to file false returns or to evade taxes, *see*, NMSA 1978, §§ 7-1-72 and 7-1-73, and it imposes a 50% of tax civil penalty for the fraudulent failure to pay any tax required to be paid. NMSA 1978 § 7-1-69(B). Mr. Bass may be faced with such consequences if he should continue to file returns in the same manner as he filed his 1995 state and federal returns. This is especially so now that he has been informed of the law. He has the opportunity to rectify his error by filing amended returns with both New Mexico and the Internal Revenue Service. I would urge his to act on this opportunity.

CONCLUSIONS OF LAW

1. Mr. Bass filed a timely, written protest to the Department's denial of his claim for refund and jurisdiction lies over both the parties and the subject matter of this protest.

2. Mr. Bass' wages from Manana Gas, Inc. are included in both "gross income" and "adjusted gross income" as those terms are defined in the Internal Revenue Code.

3. Mr. Bass' wages from Manana Gas, Inc. are included in both "base income" and "net income" as those terms are defined in the Income Tax Act, Chapter 7, Article 2, NMSA 1978.

4. Mr. Bass is not entitled to a refund of the taxes withheld from his wages earned from Manana Gas, Inc. in 1995 because those wages were properly subject to the imposition of New Mexico's income tax.

For the foregoing reasons, the Taxpayer's protest IS HEREBY DENIED.

DONE, this 28th day of August, 1997.