

STATE OF ALABAMA
DEPARTMENT OF REVENUE,

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STATE OF ALABAMA
DEPARTMENT OF REVENUE
ADMINISTRATIVE LAW DIVISION

§

v.

§

DOCKET NO. INC. 91-107

DUNCAN P. & MARGARET LILES
3565 Bankhead Avenue
Montgomery, AL 36111,

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Taxpayer.

§

FINAL ORDER

Duncan P. Liles, Jr. & Margaret Liles (Taxpayers) incurred a loss in 1989 and attempted to carry the loss back for refunds to 1984 and 1986. The Department disallowed the carryback and the Taxpayers appealed to the Administrative Law Division. A hearing was conducted on June 25, 1991. Attorney D. Kyle Johnson and CPA James B. Billingsley appeared for the Taxpayers. Assistant counsel Dan Schmaeling represented the Department. This order is based on the facts and arguments presented by the parties contained in the transcript of the hearing along with exhibits and the Recommended Order of the Administrative Law Judge.

FINDINGS OF FACT

The Taxpayers executed a waiver on March 5, 1990 allowing the Revenue Department until April 15, 1991 to assess additional income tax for the years 1984 and 1986. The Department subsequently entered final assessments for both years on October 17, 1990.

Duncan Liles (Taxpayer) telephoned the Department concerning the assessments on or about November 13, 1990. The Taxpayer concluded from the call that he did not have to appeal the

assessments but instead would be allowed to carry a loss in 1989 back to offset the tax due for 1984 and 1986. However, the Department employee that talked to the Taxpayer understood only that the Taxpayer wanted to use the 1989 refund to pay off the final assessments for 1984 and 1986. The employee would have voided the assessments if she had known that the Taxpayer intended to carry the 1989 loss back to 1984 or 1986. See transcript at pages 17-22.

In any case, the Taxpayers failed to appeal the final assessments within thirty days as required by Code of Ala. 1975, 40-2-22. Instead, the Taxpayers filed their 1989 return on November 20, 1990 and claimed NOL carrybacks to 1984 and 1986.

The Department denied the carrybacks because of the final assessments for 1984 and 1986. The Department's position is that a final assessment unappealed from is conclusive and cannot be reopened.

The Taxpayers also filed a 1989 S corporation return for Liles, Inc. on November 20, 1990 and attempted to pass a loss by the corporation through to their individual return. Liles, Inc. had filed as an Alabama S corporation for the four years preceding 1989. The Department disallowed S corporation status because the return was filed after the corporation's September 15th filing deadline. The Department's position is based on Reg. 810-3-160-.01, which requires a corporation to elect S status

by the timely filing of an S corporation return in each year.

CONCLUSIONS OF LAW

The primary issue is whether a NOL can be carried back to reopen a tax year that has been finally assessed and not appealed.

A NOL can be carried back to release a contingent obligation only. Alabama Ed. Ass'n. v. Grayson, 382 So.2d 501. The Supreme Court reiterated in Grayson that a final assessment unappealed from is fixed and cannot be reopened.¹ See

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In Grayson, the Supreme Court held that an income tax liability becomes fixed either (1) upon entry of a final assessment, or (2) three years after the return is filed. However, there are other circumstances which may cause the tax liability to remain open or contingent beyond three years. For example, income tax may be assessed within five years if the taxpayer omits more than 25% of his income, see §40-18-45(a), or at any time if no return or a fraudulent return is filed, see §40-18-46(a). Also, tax paid

also, Lambert v. State, Department of Revenue, 414 So.2d 983. Consequently, the final assessment for 1984 and 1986, not having been timely appealed as required by §40-2-22, are fixed and the Taxpayers cannot carry back their 1989 loss to those years. In any case the loss could not be carried back to 1984 because that year

through mistake may be refunded within three years after the tax is paid, see, §40-18-43. In many instances income tax is not paid until long after the return is filed. In short, an income tax liability is not necessarily fixed three years from when a return is filed. Rather, in my opinion a tax liability is fixed when the taxpayer can no longer amend or appeal the amount due or receive a refund of an amount already paid. As noted, under prevailing case law a final assessment unappealed from cannot be changed and therefore constitutes a final liability under the above definition.

is outside of the three year statute.

However, the Taxpayers should be allowed to carry the 1989 loss in full back or forward to any other year or years within the statute that are not barred by a final assessment. See, State v. First National Bank of Auburn, 141 So.2d 196.²

The Taxpayer also argues that he was misled by the Department into not appealing the final assessments. However, the Department employee did not intentionally mislead the Taxpayer and would have set the assessments aside if the Taxpayer had told her that he intended an NOL carryback to 1984 and 1986. In any case, the jurisdictional requirements of §40-2-22 cannot be waived because

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In the First National Bank of Auburn case, the Department denied a loss carryback to a year that had been finally assessed and also tried to reduce the loss available for carryforward by the amount that could have been carried back but for the final assessment. The Supreme Court disagreed and held that if the loss could not be carried back, then at the least it could be carried forward in full, without reduction. Although the Court looked on the denial of the carryback with disfavor, it did not rule that a NOL can be carried back to reopen a year that has been finally assessed.

the Taxpayer misunderstood or was misinformed concerning his appeal rights. See, Maddox Tractor and Equipment Company, Inc. v. State, 69 So.2d 426.

The second issue is whether Liles, Inc. should be recognized as an Alabama S corporation for 1989.

Section 40-18-160(1) provided in 1989 that the "election to be an Alabama S corporation shall be made or terminated in accordance with said 26 U.S.C. §1362 and (Department) regulations". The problem is that §1362 and Department Reg. 810-3-160-.01 are conflicting. Section §1362 provides that after a corporation elects S status it automatically continues as an S corporation in each subsequent year until the election is terminated by the shareholders. However, Reg. 810-3-160-.01 requires that a corporation must annually elect S treatment by timely filing an S corporation return in each year.

In my opinion the intent of §40-18-160(1) was to make §1362 controlling. Neither §40-18-160 nor §1362 requires a corporation to elect S corporation status each year by the timely filing of a return. The only timely filing requirement in §40-18-160 relates to nonresidents who must file a consent to be taxed by the due date of the return, see subparagraph (2). That requirement does not apply in this case because the Taxpayers are Alabama residents. Thus, Reg. 810-3-160-.01, insofar as it conflicts with §1362 by requiring a timely filing of each year's return, is invalid.

Liles, Inc. elected to file as an Alabama S corporation in the years preceeding 1989 and therefore should also be allowed S corporation treatment in 1989.³

This Final Order may be appealed in accordance with Code of Ala. 1975, §41-22-20.

Entered on December 4, 1991.

JAMES M. SIZEMORE, Commissioner

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Section 40-18-160 was amended effective January 1, 1990 so that any corporation that qualifies as a federal S corporation will also automatically be recognized as an Alabama S corporation.