

STEVEN D. & REBECCA B. NAPPIER§
Post Office Box 1281
Alexander City, Alabama 35010,§

STATE OF ALABAMA
DEPARTMENT OF REVENUE
ADMINISTRATIVE LAW DIVISION

Taxpayers, §

DOCKET NO. INC. 95-366

v. §

STATE OF ALABAMA §
DEPARTMENT OF REVENUE.

FINAL ORDER

The Revenue Department assessed income tax against Steven D. and Rebecca B. Nappier ("Taxpayers") for the years 1990, 1991, and 1992. The Taxpayers appealed to the Administrative Law Division, and a hearing was conducted on December 18, 1995. The Taxpayer's representative, Thomas L. Roberson, was unable to attend the hearing due to bad weather. He later submitted the Taxpayers' arguments in writing. Assistant Counsel David Avery represented the Department.

The issue in this case is whether the Department properly assessed the tax in issue within the special six year 25% omission statute of limitations set out at Code of Ala. 1975, §40-2A-7(b)(2)b.

The Taxpayers timely filed their 1990, 1991, and 1992 Alabama income tax returns. The Department audited the returns and denied certain automobile expenses claimed by the Taxpayers. Based thereon, the Department entered preliminary assessments for additional tax due on June 14, 1995. The tax was assessed outside of the normal three year statute of limitations for assessing tax set out at §40-2A-7(b)(2)a., but within the special six year 25%

omission statute at §40-2A-7(b)(2)b. Final assessments were entered on August 31, 1995. The Taxpayers timely appealed.

The Taxpayers initially argued that the denied automobile expenses should be allowed. They now concede that they do not have adequate records to verify those expenses. Rather, they argue that the tax was not timely assessed. Specifically, they argue that the six year statute can be applied only if income is omitted from a return, and that they did not omit income from their returns.

The Taxpayers' argument is correct under the statute as it now reads. But unfortunately for the Taxpayers, the tax was timely assessed under the statute as it read when the assessments were entered.

Prior to October 1992, the statute of limitations for assessing income tax was found at Code of Ala. 1975, §40-18-45. That section contained a general three year statute, but the Department was allowed five years if a taxpayer "omits from the gross income reported on said return . . ." more than 25% of the gross income reported on the return. That section, and its reference to "gross income," was similar in substance to the federal 25% omission statute at 26 U.S.C.A. §6501(e)(1)(A).

Section 40-18-45 was repealed by the Uniform Revenue Procedures Act ("URPA"), effective October 1992. URPA included a comprehensive statute of limitations provision applicable to all taxes administered by the Department. See, §§40-2A-7(b)(2)a-j. Subsection (b)(2)b. also included a new version of the 25% omission

statute. However, to make the statute apply to all taxes, not just income tax, the term "gross income" was not used. Instead, the statute allowed the Department six years to assess tax "if such return omits more than 25% of the correct amount of tax required to be shown" on the return. It is that language that was in effect when the Taxpayers were assessed in June 1995. After the unverified automobile expenses are disallowed, the tax reported on the Taxpayers' returns is underreported by more than 25%.

Subsection (b)(2)b. was amended by Act 95-607, effective July 31, 1995, to again conform closely to the federal income tax 25% omission statute.¹ The amendment also included a provision, again modeled after federal law, that the six year statute does not apply if the taxpayer's return includes sufficient information to notify the Department of the nature and the amount of the omitted item. See, §40-2A-7(b)(2)b.(ii).

Clearly, if Act 95-607 had been in effect when the tax in issue was assessed, the special six year statute would not apply because the Taxpayers did not omit gross income from their returns.

Their returns also contained sufficient information to notify the Department of the omitted (disallowed) items. However, as stated, the tax was assessed in June 1995, prior to the July 31, 1995 effective date of Act 95-607. Consequently, because the Taxpayers' returns, as adjusted, omitted more than 25% of the correct tax due, the six year statute was applicable. The assessments were thus

¹Act 95-607 used the term "taxable base", which is defined to include "gross income", and other items.

timely entered.

The Taxpayers' representatives points out that the Department's 1995 Form 40 instruction booklet, at page 16, refers to omitted income, not omitted taxes, as follows:

Keep records of income, deductions, and credits shown on your return, as well as any worksheets used to figure them, until the statute of limitations runs out for that return. Usually this is 3 years from the date the return was filed. If income that should have been reported was not reported and the income omitted is in excess of 25% of the stated income, the period of limitation does not expire until six (6) years after the due date of the return or six (6) years after the date the return was filed, whichever is later. There is no period of limitation when a return is false or fraudulent, or when no return is filed. (Emphasis added).

The 1994 instruction booklet also uses the same language. However, the 1992 and 1993 instruction booklets refer to omitted tax, as follows:

Keep records of income, deductions, and credits shown on your return, as well as any worksheets used to figure them, until the statute of limitations runs out for that return. Usually this is 3 years from the date the return was filed. If an amount of tax that should have been reported was not reported, and it is more than 25 percent of the correct tax required to be shown on the return, the period of limitation does not expire until six (6) years after the due date of the return or six (6) years after the date the return was filed, whichever is later. There is no period of limitation when a return is false or fraudulent, or when no return is filed.

I have no idea why the 1994 and 1995 instruction booklets refer to omitted "income", whereas the 1992 and 1993 booklets refer to omitted "tax". However, the statute, as amended from time to time, must control, not the instruction booklets. In any case, the 1994 and 1995 booklets are not applicable, and the Taxpayers cannot

claim reliance, because the years in issue were 1990 through 1992.

I also note that to my knowledge, the Taxpayers have never argued that they had adequate records to support the automobile expenses, but threw them away because they believed that the three year assessment period had expired.

I sympathize with the Taxpayers in this case. But, the statute of limitations in effect when the assessments were entered must be applied. The final assessments are accordingly affirmed, and judgment is entered against the Taxpayers for 1990 income tax in the amount of \$1,383.56, 1991 income tax in the amount of \$1,633.43, and 1992 income tax in the amount of \$1,900.30.

This Final Order may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, §40-2A-9(g).

Entered February 13, 1996.

BILL THOMPSON
Chief Administrative Law Judge