

THOMAS C. ROBERTSON, JR. §
2600 Vaughn Lakes Boulevard, #1514
Montgomery, Alabama 36177, §

STATE OF ALABAMA
DEPARTMENT OF REVENUE
ADMINISTRATIVE LAW DIVISION

Taxpayer, §

DOCKET NO. INC. 95-458

v. §

STATE OF ALABAMA §
DEPARTMENT OF REVENUE.

FINAL ORDER

The Revenue Department assessed income tax against Thomas C. Robertson, Jr. ("Taxpayer") for the years 1992 and 1993. The Taxpayer appealed to the Administrative Law Division, and a hearing was conducted on February 27, 1996. The Taxpayer appeared at the hearing with his authorized representative, Aaron Holden of H & R Block. Assistant Counsel Jeff Patterson represented the Department.

This case involves depreciation recapture. The Taxpayer moved to Alabama in 1991, and subsequently sold three rental houses in Oklahoma which he had purchased in the early 1980s. The specific issue is whether the Taxpayer should be required, for Alabama income tax purposes, to recapture depreciation on the houses for the years prior to when he moved to Alabama and became subject to Alabama income tax.

The facts are undisputed.

The Taxpayer purchased three rental houses in Oklahoma in the early 1980s. He was living in Texas at the time, but subsequently moved to Hawaii, Missouri, and other states. The Taxpayer depreciated the houses every year for federal income tax purposes.

It is not known if he also depreciated the houses for state purposes.

The Taxpayer moved to Alabama in 1991. He subsequently sold the rental houses in 1992 and 1993. For federal tax purposes, he recaptured all of the depreciation that had been claimed on the houses. However, for Alabama tax purposes, he recaptured only that portion of the depreciation he had claimed since moving to Alabama.

The Department reviewed the Taxpayer's returns and required him to recapture depreciation for Alabama purposes to the same extent as required for federal purposes. The Taxpayer appealed the resulting final assessments to the Administrative Law Division.

This issue has never been addressed in Alabama.

All Alabama taxpayers are allowed a depreciation deduction for income producing property pursuant to Code of Ala. 1975, §40-18-15(a)(8). In computing any gain or loss from the subsequent sale of such property, the taxpayer's basis in the property shall be adjusted for depreciation "to the extent allowed (but not less than the amount allowable) under this chapter" Code of Ala. 1975, §40-18-6(b)(2). In other words, the taxpayer is required to recapture the depreciation by decreasing his tax basis in the property by the amount of depreciation previously claimed or allowed under Alabama law.

The Taxpayer argues that it would be patently unfair for him to be required to recapture and pay tax in Alabama on depreciation for which he was not allowed a benefit in Alabama in prior years.

The Department counters that Alabama law requires a taxpayer to recapture all depreciation "allowed" or "allowable" in prior years, even if such depreciation was not claimed on an Alabama return. I agree with the Taxpayer.

Section 40-18-6(b)(2) requires recapture of all depreciation allowed or allowable "under this chapter", which is Chapter 18 of Title 40. If a taxpayer is not domiciled in or otherwise subject to Alabama tax in a given year, then obviously depreciation is not allowed or allowable under Chapter 18 of Title 40 in that year, in which case the taxpayer is not required to recapture depreciation for that year when the property is subsequently sold.

The intent of the recapture rule is to put a taxpayer in the same position tax-wise as if depreciation had not been claimed in the first place. Pro-rata depreciation is allowed in each year, but the taxpayer must eventually recapture and in effect pay tax on the depreciation when the property is disposed of. But under the Department's position, a taxpayer would be required to recapture and pay tax on depreciation in Alabama without ever having benefited from a depreciation deduction in Alabama in prior years.

Such a result would be unfair to the taxpayer, and, importantly, is not required under Alabama law.

The above considered, the final assessments in issue are dismissed.

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

Entered April 26, 1996.

BILL THOMPSON
Chief Administrative Law Judge