HERBERT L. RABURN, Executor as Co-Executor of the Estate of James H. Neely 1208 Cedardale Lane Birmingham, AL 35216,	'	STATE OF ALABAMA DEPARTMENT OF REVENUE ADMINISTRATIVE LAW DIVISION
Taxpayer,	'	DOCKET NO. INC. 99-313
v.	'	
STATE OF ALABAMA DEPARTMENT OF REVENUE.	'	

FINAL ORDER

The Revenue Department assessed estate tax against Herbert L. Raburn (ATaxpayer@), as Executor of the Estate of James H. Neely. The Taxpayer appealed to the Administrative Law Division pursuant to Code of Ala. 1975, '40-2A-7(b)(5)a. A hearing was conducted on February 23, 2000. Robert Walthall represented the Taxpayer. Assistant Counsel David Avery represented the Department.

ISSUE

The issue in this case is whether the Taxpayer is personally liable for the Alabama estate tax owed by the Estate of James H. Neely.

FACTS

James H. Neely (ANeely@) died in December 1982. His will named three co-executors, the Taxpayer and Neely=s son and wife. The Taxpayer is a CPA and was Neely=s longtime friend. The Taxpayer=s CPA firm prepared the estate tax return for Neely=s estate.

The estate tax return reported an estate value of $6,328,000. (The dollar amounts stated herein are rounded for ease of reference.) Eighty five percent of that value was a

49 percent ownership interest in Mitchell & Neely, Inc. (Acorporation@) valued at $5,390,000. The corporation was engaged in the coal mining business in Alabama, and also owned undeveloped property in Louisiana valued at $3,536,000.

The return also reported $130,000 in life insurance and $266,000 in jointly owned property (a certificate of deposit, miscellaneous stocks, etc.). The Estate had other miscellaneous properties valued at $495,000. The most valuable of those included a $277,000 partnership interest in an oil and gas exploration partnership. The return also showed miscellaneous Estate debts of $337,000. The Estate owed $557,000 in federal estate tax.

The Estate owed Alabama estate tax of $87,800. The Estate petitioned the Department to allow it to pay in ten annual installments, as allowed by Code of Ala. 1975, '40-15-4. The Department agreed. Neely=s widow paid three annual installments totaling $35,000. She stopped paying because, according to the Taxpayer, the Estate became insolvent.

The Department assessed the Taxpayer individually for the unpaid estate tax.[1] The

[1]The Department indicated at the February 23 hearing that it may also assess the other two co-executors for the unpaid tax. It has not done so to date.

Taxpayer appealed.[2]

The Department contends that the Taxpayer should be held personally liable because he wasted or allowed to be wasted the assets of the Estate, and that but for the Taxpayer=s negligence, the Estate would have had sufficient assets to pay the Alabama estate tax. The Taxpayer contends that his CPA firm prepared the Estate=s estate tax return, but that he had nothing to do with managing the Estate=s assets. He argues that even if he had been actively involved, he could not have prevented the Estate from becoming insolvent. A review of what happened to the Estate=s assets is thus necessary.

The corporation=s coal mining business relied primarily on its contracts with Alabama Power Company. Alabama Power Company failed to renew those contracts shortly after Neely=s death. The corporation began losing money as a result, and Mitchell and Neely=s widow, together, contributed almost $1,000,000 to keep the business viable. The business eventually failed. Central Bank subsequently foreclosed on its loans to the corporation and sold the corporation=s equipment in September 1991. The Bank later foreclosed on and sold the corporation=s coal mining-related real property in December

[2]The Department filed a motion to dismiss because the appeal was not filed in the Taxpayer=s name, but rather in the name of the Estate of James H. Neely. That motion was denied by Preliminary Order dated November 3, 1999.

1994. None of the sale proceeds went to the corporation.

The corporation discovered when it attempted to sell the undeveloped property in Louisiana that the property contained wetlands. Consequently, the property decreased drastically in value, and was subsequently sold for only $1,210,000. Most of those proceeds went to pay the corporation=s debts. However, the corporation did eventually receive $320,000 from the sale. Some of that amount was used to pay more of the corporation=s debt, but a balance of $230,000 is currently in a certificate of deposit at Central Bank. Against that amount are outstanding liens against the corporation of over $460,000, plus $500,000 in reclamation bonds.

The life insurance and jointly owned property went to Neely=s widow outside of the Estate. The oil exploration partnership that was the primary miscellaneous asset of the Estate failed to discover oil or gas, and turned out to be worthless. A second undeveloped parcel of land in Louisiana owned by the Neelys was sold to pay an outstanding federal tax debt. The Estate received nothing from that sale.

ANALYSIS

The Alabama estate tax is levied on all net estates passing in Alabama. Code of Ala. 1975, '40-15-2. The executor of an estate is required to file a copy of the federal estate tax return with the Department. The Department is then required to compute the Alabama estate tax due and Ashall assess against said estate@ the Alabama tax due. Code of Ala. 1975, '40-15-3.

The estate tax return is due and the personal representative of the estate is

required to pay the tax within nine months of the decedent=s death. The Department may, however, extend the payment period for a period not to exceed ten years. Code of Ala. 1975, '40-15-4.[3]

In this case, the Department allowed the Estate to pay in ten annual installments. Section 40-15-4 also allows the Department to obtain security to ensure that the deferred payments are made. The Department did not require the Estate to post security in this case.

Code of Ala. 1975, '40-15-18 provides that all estate taxes shall be paid by the executor Aout of the estate property and shall be a charge against the residue@ of the estate.

[3]This provision is similar to 26 U.S.C. '6166, which allows an estate to elect to pay its federal estate tax in installments, not to exceed ten years. However, the Department has sole discretion to grant an extension to pay under '40-15-4.

The above statutes are clear that the Alabama estate tax is on the estate. Unlike federal law, there is no Alabama statute making an executor personally liable for estate tax if the estate fails to pay or is without sufficient funds to pay the tax.[4] Code of Ala. 1975, '40-15-7(e) provides that a legal representative may be liable to the extent that estate assets come into his hands. But that statute applies only to non-resident decedent estates. In any case, as discussed below, sufficient estate assets were not available to the Taxpayer from which he could have paid the annual installments.

There are also no Alabama cases or other authority holding an executor personally liable for unpaid estate taxes.[5] But even assuming that an executor can be held personally liable for estate taxes because of waste, negligence, or mismanaging of the estate assets,

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[4]An executor may under certain circumstances be personally liable for federal estate tax. 26 U.S.C. '3713. That section applies, however, only if the executor distributes the assets of the estate knowing that the estate is insolvent and that the estate taxes of the estate have not been paid. U.S. v. Coppola, 85 F.3d 1015 (1996) (Executor liable because he knew of federal estate tax liability, yet depleted estate by distributing assets to himself and his family, thereby preventing payment of estate taxes.) See also, U.S. v. Estate of Kime, 950 F.Supp. 950 (1996); Schwartz v. C.I.R., 560 F.2d 311 (1977).

[5]The one Alabama case cited by the Department, Carter v. Carter, 24 So.2d 759 (1946), does not involve an executor=s liability for unpaid estate tax, and is otherwise

that did not occur in this case.

The Estate=s primary asset was its minority interest in Mitchell & Neely, Inc. That interest was valued at $5,350,000 for estate tax purposes. However, in fact, and through no fault of the Taxpayer, the true value of the corporation was substantially less.

The corporation began losing money when it lost the Alabama Power Company coal contracts shortly after Neely died. Considering the outstanding loans and debts owed by the corporation, its coal mining operation was in substance worthless at that time. Mitchell and Neely=s widow infused almost $1,000,000 into the business to try and make it viable. That effort failed, and the coal mining assets were eventually sold to pay creditors. The corporation received nothing from the sale of those assets.

The corporation=s undeveloped Louisiana land appraised for $3,536,000 when Neely died. However, the value of the property was substantially reduced when wetlands were discovered on the property. There was obviously nothing the Taxpayer could have done to Apreserve@ the value of that property. A small portion of the sale proceeds ($230,000) are currently on deposit at Central Bank. But against those proceeds are outstanding liens totaling $460,000 that pre-date the estate tax liability.

In summary, the value of the corporation substantially decreased through no fault of the Taxpayer when the corporation lost the Alabama Power Company contracts and

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inapplicable to this case.

wetlands were discovered on the Louisiana property. In effect, the primary asset of the Estate valued at $5,390,000 became worthless. I know of no action the Taxpayer could have taken to save the business, especially considering that the Estate held only a minority interest in the corporation.

There is also no evidence that the Taxpayer mismanaged or wasted the other assets of the Estate. The life insurance proceeds and the jointly held property valued together at $396,000 went to Neely=s widow outside of the Estate. Of the Estate=s miscellaneous properties valued at $495,000, the oil and gas partnership interest valued at $277,000 was worthless. The balance of the assets ($218,000) was subject to priority debts of $337,000. The Estate also owed federal estate tax of $557,000.

The above illustrates that the Estate became insolvent through events not under the Taxpayer=s control. The Department argues that the Taxpayer should have immediately sold the stock in Mitchell & Neely, Inc. after Neely died. At that time, however, the corporation=s equipment and real property were pledged as security for various loans, and with the loss of the Alabama Power Company contracts, the corporation was losing money. It is thus unlikely that the closely-held corporation could have been sold for a profit. That conclusion is supported by the fact that Neely=s widow and Mitchell, individually, put almost $1,000,000 into the corporation in a futile attempt to keep it viable.

The final assessment in issue is dismissed.[6]

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[6]The Department claims that the Estate still has assets sufficient to pay the estate taxes. Department=s ABrief of Issues,@ at 3. Those assets were not identified, but if such assets are available, the Department should execute against those assets through normal procedures. In hindsight, the Department should also perhaps require a bond or other security when it allows an estate to pay in installments to ensure that the full tax is

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

Entered June 16, 2000.

BILL THOMPSON
Chief Administrative Law Judge

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eventually paid. (The Department currently has no regulation governing estate tax installment payments under '40-15-4.)