SAMUEL S. & LINDA W. MOODY P.O. BOX 1715 BAY MINETTE, AL 36507-1715,	§	STATE OF ALABAMA ALABAMA TAX TRIBUNAL
Taxpayers,	§	DOCKET NO. INC. 15-797
v.	§	
STATE OF ALABAMA DEPARTMENT OF REVENUE.	§	

FINAL ORDER

The Revenue Department assessed Samuel and Linda Moody ("Taxpayers") for 2013 Alabama income tax. The Taxpayers appealed to the Tax Tribunal pursuant to Code of Ala. 1975, §40-2A-7(b)(5)a. A hearing was conducted on February 11, 2016. CPA Mark Pawlowski represented the Taxpayers. Assistant Counsel Duncan Crow represented the Revenue Department.

The Taxpayers filed a 2013 Alabama income tax return on which they reported total Alabama adjusted gross income of $2,065.702 and non-Alabama adjusted gross income of $601,536. They also claimed a credit for 2013 Mississippi income tax paid of $29,439 based on taxable income of $594,772 reported to Mississippi in that year.

The Department reviewed the return, reduced the allowable credit to $18,145, and consequently entered the final assessment in issue.

Code of Ala. 1975, §40-18-21 allows an Alabama resident taxpayer a credit for income tax paid to another state on account of business transacted or property held in the other state. The credit is allowed in "the amount of income tax actually paid by such (Alabama) resident to" another state. Section 40-18-21(a)(1). The credit is also limited to the lower of the actual tax paid to the other state or the amount that "would be due on the

same (foreign state) income computed on the income tax rate in Alabama,. . . ." Section 40-18-21(a)(2).

Revenue Department Reg. 810-3-21-.03 addresses the credit for income tax paid to other jurisdictions. That regulation provides that in computing the allowable credit, the income tax paid to another state must be multiplied by a percentage, the numerator of which is total non-Alabama adjusted gross income and the denominator of which is total Alabama adjusted gross income. See, Reg. 810-3-21-.03(1) and (2). Paragraph (2)(a) of the regulation gives the following example:

> Example. Taxpayer reports $120,000 of adjusted gross income on his Alabama income tax return, of which $80,000 is attributable to another jurisdiction; his Alabama income tax liability before credits is $4,000. Taxpayer paid the other jurisdiction $4,000 of income tax on the $80,000 of income from the other jurisdiction.
>
> Because one-third ($1,333) of Taxpayer's liability is attributable to Alabama sources, it is not subject to the credit for tax paid to other jurisdictions. The maximum credit that Taxpayer may utilize is $2,667, which is the portion of his liability attributable to other jurisdictions.

The credit limitation set out in Reg. 810-3-21-.03(1) and (2) is contrary to §40-18-21, and is rejected.

As discussed, §40-18-21(a)(1) allows a credit against Alabama tax due for "the amount of income tax actually paid by such (Alabama) resident to any state or territory on account of business transacted or property held" in the foreign state or territory.

Paragraph (a)(2) limits the amount of the credit to only the amount of tax that would have been due on the same income computed using Alabama's tax rates. For example, if an Alabama resident had $10,000 in income in State B that had a tax rate of 7 percent, the resident would have paid $700 in income tax to State B. Pursuant to paragraph (a)(2), the

Alabama credit would be limited to only $500, or the amount that would have been paid on the same income pursuant to Alabama's 5 percent rate. Other than the paragraph (a)(2) limitation, however, there are no other limitations in §40-18-21; and specifically, §40-18-21 does not allow or impose the percentage limitation on the credit set out in Reg. 810-3-21-.03(1) and (2).

In *State v. Robinson Land & Lumber Co. of Alabama, Inc.*, 77 So.2d 641 (Ala. 1955), the Alabama Supreme Court addressed the income tax credit then allowed at Ala. Code Tit. §390 (1940), which is the predecessor to §40-18-21. In *Robinson Land*, the Revenue Department sought to impose the same percentage limitation now contained in Reg. 810-3-21-.03(1) and (2). Applying the plain language of the credit statute, the Court rejected the Department's argument, as follows:

> Subsection (b) of Section 390, supra, is the safeguard which prevents loss of income tax revenue by the State of Alabama on business transacted within Alabama by reason of credit under subdivision (a) of Section 390, supra, for payments actually paid to another state at a rate higher than our own on business transacted within such other state. For example, assume that an Alabama corporation has taxable income derived within Alabama of $ 10,000 and also taxable income of $ 10,000 on account of business transacted in another state in which the income tax rate is 6%; in the absence of subsection (b), supra, payment of $ 600 income tax to the other state would deprive Alabama of any income tax revenue on the $ 10,000 income of the corporation derived within the State of Alabama. This is the reason for subsection (b), Section 390, Title 51, Code of Alabama 1940. For emphasis, subsection (b), supra, is here quoted alone:
>
> > (b) In case the amount of tax actually paid by a resident of Alabama to another state or territory is in excess of the amount that would be due on the same income computed on the income tax rate in Alabama, then only such amount as would be due in this state on such taxable income shall be allowed as a credit.
>
> Reduced to words, the formula which the State Department of Revenue has used as an interpretation and application of subsection (b), Section 390,

supra, is:

> But such credit shall not exceed such proportion of the tax payable under this act as the gross income of the taxpayer derived in such other state or territory bears to his entire gross income derived from all sources both within and without Alabama.

The effect of the application of the State Department of Revenue's formula is to accomplish the very thing which Section 390, supra, was designed to avoid, namely, the imposition of two state income taxes upon one income. Section 390 of the income tax statute contains no such limitation.

It is not within the power of the State Department of Revenue to add or take from the statute by administrative construction. 42 Am.Jur. p. 400, § 80. Only the legislative branch of our state government is vested by the Constitution with lawmaking power.

Robinson Land, 77 So.2d at 647.

Section 40-18-21 is in substance identical to its predecessor §390. As in *Robinson Land*, the plain language of the statute must be followed. "Where language in a statute is unambiguous, the clearly expressed intent must be given effect, and there is no room for construction. The statute here is without any uncertainty of meaning, and appellee is entitled to the credit claimed." (cites omitted) *Robinson Land*, 77 So.2d at 641. Just as in *Robinson Land*, the percentage limitation imposed by the regulation is not in §40-18-21, and is accordingly rejected.

The Court in *Robinson Land* also opined that "the legislative purpose in the adoption of the credit provision in our statute, . . . was to relieve the taxpayer of the burden of double taxation." (cites omitted) *Robinson Land*, 77 So.2d at 646. Contrary to that intent, if the regulation's percentage limitation is applied, at least a part of an Alabama resident's foreign-sourced income would be taxed by both Alabama and the foreign jurisdiction in

which it was earned. Using the facts in the example in paragraph (2)(a) of Reg. 810-3-21-.03, the following computation shows the total State tax paid by the taxpayer.

Alabama Tax Computation	
Alabama sourced	$ 40,000
Non-Alabama sourced	$ 80,000
Total AGI	$120,000
Alabama deductions	$ 39,200
Alabama taxable income	$ 80,800
Alabama tax before credits	$ 4,000
Credit per Regulation 810-3-21-.03	$ 2,667
Alabama tax	$ 1,333

State Tax Rate	
Tax paid to non-resident state	$ 4,000
Tax paid to Alabama	$ 1,333
Total state tax paid	$ 5,333

Effective combined state tax rate

$5,333 ÷ 80,800 = 6.6%

To reiterate the Court's holding in *Robinson Land* – "The effect of the application of the State Department of Revenue's formula is to accomplish the very thing which (§40-18-21) was designed to avoid, namely, the imposition of two state income taxes upon one income. (Section 40-18-21) of the income tax statute contains no such limitation." *Robinson Land*, 77 So.2d at 647. The above calculation demonstrates that the Court was correct. By applying the percentage limitation in the regulation, the taxpayer in the

example would be paying an effective state tax rate of 6.6 percent, which can only mean that at least a portion of the income in issue is being taxed twice.

In summary, the intent of the credit provision is for an Alabama resident taxpayer with foreign-sourced income to pay to Alabama the amount that would have been owed to Alabama if the taxpayer had omitted the foreign-sourced income from the return.[1] The percentage limitation in Reg. 810-3-21-.03 thwarts that intent. Rather, the amount of income tax "actually paid" by the Taxpayers to the State of Mississippi in 2013 must be allowed pursuant to the plain language of §40-18-21.[2] The final assessment is accordingly voided.

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

Entered September 29, 2016.

Bill Thompson

BILL THOMPSON
Chief Tax Tribunal Judge

bt:dr
cc: Duncan R. Crow, Esq.
Mark A. Pawlowski, CPA

1 This assumes that the tax rate in the foreign jurisdiction is equal to or greater than the Alabama rate. If the rate in the foreign jurisdiction is lower than Alabama's rate, the taxpayer would pay some Alabama tax on the foreign sourced income.

2 There is no evidence that the State of Mississippi has a tax rate higher than Alabama's maximum five percent rate. Consequently, the limitation at §40-18-21(a)(2) is inapplicable.