STATE OF ALABAMA DEPARTMENT OF REVENUE,	§	STATE OF ALABAMA DEPARTMENT OF REVENUE
	§	ADMINISTRATIVE LAW DIVISION
v.	§	DOCKET NO. INC. 86-132
CHRISTINE P. ELLISON Hurtsboro, AL 36860,	§	
Taxpayer.	§	

ORDER

This case concerns a preliminary assessment of income tax entered by the Revenue Department against Christine P. Ellison(Taxpayer) for the calendar year 1984. A hearing was conducted in the matter by the Administrative Law Division on November 25, 1986. The Taxpayer was represented at said hearing by CPA James W. Wilson, Sr. Assistant counsel Mark Griffin was present and represented the Department. Based on the undisputed evidence submitted at the hearing, the following findings of fact and conclusions of law are hereby made and entered.

FINDINGS OF FACT

The issue in this case concerns the deductibility of $7,051.05 paid by the Taxpayer in 1984 as part of the settlement of the state of her husband. The Taxpayer was administratrix of the estate, and, along with her children, was also a beneficiary.

The deceased husband's estate consisted of various assets, including two pieces of rental property. Under the terms of the will, the beneficiary children were to receive a specific amount of money. However, due to operating losses incurred on the rental property during the administration of the estate, the estate had insufficient cash to pay the full amounts due the children. Consequently, in lieu of selling the rental properties to get the necessary cash, the Taxpayer paid to the children a total of $7,051.05 in settlement of the children's claims against the estate.

On her original 1984 return, the Taxpayer claimed the amount paid as an estate loss on Schedule E. The Department audited the Taxpayer and disallowed the claimed loss on the basis that an estate loss cannot be passed through to the estate's beneficiaries, citing Department Reg. 810-3-25-.08 and related regulations. Thereafter, the Taxpayer filed an amended return and thereon claimed the $7,051.05 as an expense relating to the production, maintenance or receipt of income and/or income producing property under Code of Alabama 1975, §§40-18-15(5) and (6). The Department again disallowed the deduction and based thereon entered the preliminary assessment in issue.

CONCLUSIONS OF LAW

On her original return, the Taxpayer claimed the $7,051.05 as an estate loss passthrough. However, after the loss was disallowed by the Department, an amended return was filed by the Taxpayer in which the payment was claimed as a deduction under §40-18-15(5) and corresponding Department Reg. 810-3-15-.09(1). Thus, although the Taxpayer disagrees with the Department's regulations which disallow a passthrough of a loss from an estate of a beneficiary, that question is not in issue. Rather, the determinative issue is whether the payments are deductible as ordinary and necessary expenses for the production or collection of income, or for the management, conservation or maintenance of property held for the production of income.

Code of Alabama 1975, §§40-18-15(5) and (6) provide in substance for a deduction for losses incurred "in any transaction entered into for profit" (subsection (5)), or sustained "of property not connected with the trade or business" (subsection (6)). Department Reg. 810-3-15-.09(1), entitled "Deduction of Nontrade or Nonbusiness Expenses", provides as follows:

> In computing net income, the taxpayers may deduct all ordinary and necessary expenses for the production or collection of income, or for the management, conservation, or maintenance of property held for the production of income . . .

Succinctly stated, the payments in question were made by the Taxpayer so as to maintain her percentage interest in the estate's rental property, and to avoid a sale of said property that would have otherwise been necessary to obtain the money due the other beneficiaries. The transaction (payments) was not entered into for profit, nor were the payments made for the production or collection of income or the maintenance of property held for the production of income. Rather, they were made, at the option of the Taxpayer, as an alternative to selling the rental properties and paying the amounts due the children from the sales proceeds. By paying the other beneficiaries from her own funds, the Taxpayer simply maintained her percentage ownership in the rental properties and avoided a forced sale of the properties to get the needed cash. The payments may have also facilitated a distribution of the estate assets, but upon distribution the Taxpayer was in effect reimbursed for prior payments by the retention of her full ownership in the properties. In any case, it cannot be said that the receipt of estate assets is a transaction entered into for profit, nor are payments made to facilitate the receipt of said assets expenses relating to the production or receipt of income or the maintenance of income producing property.

Based on the above, it is hereby determined that the $7,051.05 paid by the Taxpayer in 1984 was not a deductible expense, and accordingly, the preliminary assessment in issue is correct as entered, and should be made final with applicable interest as required by law.

Done this 7th day of January, 1987.

BILL THOMPSON
Chief Administrative Law Judge