STATE OF ALABAMA DEPARTMENT OF REVENUE,	§	STATE OF ALABAMA DEPARTMENT OF REVENUE ADMINISTRATIVE LAW DIVISION
v.	§	DOCKET NO. INC. 87-233
GREGORY & PENELOPE DESPINAKIS 3836 Spring Valley Road Birmingham, AL 35223,	§	
Taxpayer.	§	

ORDER

The Revenue Department assessed income tax against Gregory Despinakis ("Taxpayer") and his wife Penelope Despinakis for the year 1984. The Taxpayer appealed to the Administrative Law Division and a hearing was conducted on March 23, 1989. J. Michael Cooper, Esq. appeared for the Taxpayer. Assistant counsel Duncan Crow represented the Department. Based on the evidence presented in the case, the following findings of fact and conclusions of law are hereby entered.

FINDINGS OF FACT

The Taxpayer worked as a real estate broker from 1971 until 1981, and was last associated with the brokerage firm of Johnson-Rast and Hays Company, Inc. in Birmingham. As a broker, the Taxpayer acquired considerable skill and knowledge about real estate contracts and the development of commercial property. The Taxpayer left the real estate business in 1981 and purchased a restaurant in downtown Birmingham.

In early 1983, the Taxpayer was approached by Tom Rast and Robert Reed of Johnson-Rast and Hays concerning the

construction of an office complex on Block 60 in downtown Birmingham. Specifically, Rast and Reed asked the Taxpayer to contact Cameron Grammas concerning the project and to solicit Grammas' participation and cooperation. Grammas frequently dined at the Taxpayer's downtown restaurant and owned a large portion of Block 60 that was essential to the proposed project. Rast and Reed hoped that the Taxpayer, as an acquaintance of Grammas with a proven reputation in real estate development, would help convince Grammas to participate in the project.

The Taxpayer approached Grammas and his attorney, J. Gusty Yearout, with the plans. Grammas and Yearout were initially reluctant, but finally agreed to cooperate after several meetings and discussions involving the Taxpayer and others.

Agreement was reached that the project would proceed and that the company financing the project, The Equitable Life Assurance Society, would own 60% of the project, with the remaining 40% divided among the shareholders of a partnership as follows:

Grammas and Yearout	25%
Tom Rast	15%
Bob Reed	15%
Todd Sharley	15%
Bob Schleusner	15%
Greg Despinakis	15%
	100%

The agreement to include the Taxpayer in the partnership was set out in a letter from Reed to the Taxpayer dated June 6, 1983 (Taxpayer's Exhibit 1). Reed also wrote a letter dated September 30, 1983 to Yearout indicating that the Taxpayer would own a 15%

interest in the partnership (Taxpayer's Exhibit 5).

However, Grammas subsequently objected to the Taxpayer's participation in the project and refused to cooperate if the Taxpayer was given a partnership share. Consequently, the partnership was formed without the Taxpayer, and the Taxpayer was notified that he would have no interest in the project. The Taxpayer objected and demanded his original ownership share. The partners refused and offered to pay the Taxpayer $25,000.00 in settlement of his claim, which the Taxpayer rejected.

The partners subsequently filed a declaratory judgment action in Jefferson County Circuit Court in February, 1984, therein asking the Court to declare that the Taxpayer had no rights and interest in the partnership or project. The Taxpayer counterclaimed, alleging that he had been wrongfully excluded from the partnership. The counterclaim demanded an plus punitive damages.

The parties negotiated and finally agreed that the Taxpayer would receive $165,000.00 in return for a general release of all claims and interests in the project and partnership. The agreement was evidenced by an amended counterclaim filed on July 24, 1984 in which the Taxpayer sought $165,000.00 in damages. Also, a general release was signed by the Taxpayer on July 25, 1984 acknowledging receipt of the $165,000.00 and releasing all rights and interest in the project and partnership.

The Taxpayer excluded the $165,000.00 settlement from his 1984 Alabama income tax return, arguing that the amount constituted damages received for a personal injury. Personal injury damages are excluded from gross income by Code of Ala. 1975, §40-18-

14(2)(e).

The Department reviewed the return and included the amount as taxable income received for personal services rendered by the Taxpayer. The Department subsequently entered the preliminary assessment in issue, from which the Taxpayer appealed.

CONCLUSIONS OF LAW

Code of Ala. 1975, §40-18-14(2)(e) excludes from gross income any amounts received by an individual to the same extent as allowed under 26 U.S.C. §104. The scope of §104 was explained in Thralkeld v. C.I.R., 848 F.2d 81, as follows:

> Section 104(a)(2) provides an exception from gross income for "the amount of any damages received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of personal injuries or sickness." The regulations specify that "[t]he term 'damages received (whether by suit or agreement)' means an amount received (other than workmen's compensation) through prosecution of a legal suit or action based upon a tort or tort type rights, or through a settlement agreement entered into in lieu of such prosecution" 26 C.F.R. §1.104-1(c).

Damages received in a tort action for malicious prosecution the type excluded under §104(2)(e), see Threlkeld, supra, and Roemer v. Commissioner, 716 F.2d 693, respectively.

Conversely, a settlement compensating the plaintiff for loss of earnings did not arise from a personal injury and thus was not excludable under §104(2)(e), see Wolfson v. Commissioner 651 F.2d 1228.

In the present case, the Taxpayer's only claim to a partnership

interest in the project was based on services rendered in bringing Grammas and Yearout into the project. But for his activities as a middleman, the Taxpayer clearly would have had no basis for claiming a partnership share. The Taxpayer had performed a service and expected compensation. Accordingly, the amount received by the Taxpayer was clearly compensation based on or arising from personal services and was not the result of a personal injury. Any income arising from the partnership interest would have constituted taxable income. Thus, the settlement received in lieu of the partnership interest also constituted taxable income.

The above considered, the Department is hereby directed to make final the assessment in issue, with interest as required by statute.

Entered this 28th day of April, 1989.

BILL THOMPSON
Chief Administrative Law Judge