

STATE OF ALABAMA  
DEPARTMENT OF REVENUE,

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STATE OF ALABAMA  
DEPARTMENT OF REVENUE  
ADMINISTRATIVE LAW DIVISION

§

v.

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DOCKET NO. F. 88-120

FBK INTERNATIONAL CORP.  
280-14 Snow Drive  
Birmingham, AL 35209,

§

§

Taxpayer.

§

ORDER

The Revenue Department entered a preliminary assessment of domestic corporation franchise tax against FBK International Corporation ("Taxpayer") for the years 1986 and 1987. The Taxpayer appealed to the Administrative Law Division and a hearing was conducted on August 9, 1988. Don B. Long, Jr., Esq. appeared on behalf of the Taxpayer. Assistant counsel Ron Bowden was present and represented the Department. Based on the evidence presented by the parties, the following findings of fact and conclusions of law are hereby made and entered.

FINDINGS OF FACT

The relevant facts are undisputed.

The Taxpayer's board of directors adopted a resolution on March 27, 1986 which provided that 2,833,334 shares of the Taxpayer's preferred stock "shall be cancelled on the records of the corporation and shall no longer be deemed issued and outstanding".

Said shares were surrendered to the Taxpayer and were cancelled on the records of the corporation effective April 1, 1986.

The Taxpayer filed a statement of cancellation with the

Jefferson County Probate Court concerning the shares in issue on March 4, 1988. The statement of cancellation was filed pursuant to the provisions of Code of Ala. 1975, §10-2A-120.

The Taxpayer's 1987 Alabama franchise tax return omitted the 2,833,334 shares as capital stock for purposes of computing the Alabama franchise tax. The Department included the shares as capital stock and accordingly assessed additional tax due for the years 1986 and 1987. The Taxpayer paid the tax for 1986, leaving only a contested balance due of \$3,016.55 for 1987.

#### CONCLUSIONS OF LAW

Code of Ala. 1975, §40-14-40 levies an annual franchise tax based on a corporation's capital stock. The issue in dispute is whether the shares of capital stock in question were cancelled (1) upon the effective date of the corporate resolution, or (2) upon the filing of the statement of cancellation with the probate court.

Code of Ala. 1975, §10-2A-120 reads in pertinent part as follows:

(a) A corporation may at any time, by resolution of its board of directors, cancel all or any part of the shares of the corporation . . . I and in such event a statement of cancellation shall be filed as provided in this section.

(c) Such statement of cancellation shall be delivered to the probate judge.

(d) Upon the filing of such statement of cancellation, the stated capital of the corporation shall be deemed to be reduced by that part of the stated capital which was,

at the time of such cancellation, represented by the shares so cancelled, and the shares so cancelled shall be restored to the status of authorized but unissued shares.

(e) Nothing contained in this section shall be construed to forbid a cancellation of shares or a reduction of stated capital in any other manner permitted by this chapter.

The Taxpayer contends that subsection (a) controls and that the shares were cancelled upon passage of the resolution by the board of directors effective April 1, 1986. Conversely, the Department contends that subsection (d) controls and thus that the subject shares were not effectively cancelled until the statement of cancellation was filed with the Jefferson County Probate Court on May 4, 1988.

Section 120 is unclear and does not specify when the shares are effectively cancelled. Thus, related §§119 and 121 should be considered. While §120 provides that shares can be cancelled by corporation resolution, §119 provides for cancellation by redemption or purchase. Section 119 specifically sets out that "the redemption or purchase shall effect a cancellation of such shares". The section further provides that the corporation shall file a statement of cancellation, which when delivered to the probate court shall effect a reduction in the stated capital of the corporation. In short, §119 provides that the shares are cancelled when redeemed or purchased, and that stated capital is reduced upon the later filing of a statement with the probate court. That is, the reduction in stated capital is separate and apart from the

cancellation of the shares.

Section 121 concerns the reduction in stated capital when not accompanied by a cancellation of shares. The section sets forth various requirements which must be met, culminating with the filing of a statement with the probate court. As with §§119 and 120, the reduction is effectuated upon filing with the probate court.

Reading sections 119, 120 and 121 together, it is clear that the cancellation of stock and the reduction in stated capital, while sometimes related, are two distinct and separate events which occur at different times. Section 121 illustrates that a reduction in stated capital can occur without a cancellation of stock.

Stock can be cancelled either by redemption or purchase (§119) or by corporate resolution (§120). Section 119 specifies that the shares are cancelled when redeemed or purchased. Section 120 has no similar specific provision designating when the shares are cancelled. However, a reasonable interpretation is that the shares are cancelled on the effective date of the corporate resolution specifying that the shares are thereby cancelled. The Legislature apparently considered that no additional and specific explanation as the effective date of cancellation was necessary, as was included in §119.

In fairness to the Department, the language of §120(d) does provide a reasonable argument that cancellation is effective upon filing with the probate court. The last phrase of (d) reads ". .

. and the shares so cancelled shall be restored to the status of authorized but unissued shares." But the section is unclear as to whether "at the time of such cancellation" relates back to the effective date of the corporate resolution or the filing of a statement of cancellation with the probate court.

Similar language is found in §119. However, §119 provides that the shares are "restored to the status of authorized but unissued shares" when the statement of cancellation is filed with the probate court, which occurs after the shares have been effectively cancelled. Thus, restoration of the shares as authorized but unissued does not trigger cancellation of the shares, as argued by the Department.

If a tax statute is unclear, the section must be construed in favor of the taxpayer and against the Department. Where two reasonable interpretations are possible, the one most favorable to the taxpayer must be adopted. Alabama Farm Bureau Mut. Ins. Co., Inc. v. City of Hartselle, 460 So.2d 1219.

The above considered, a reasonable interpretation of §120 is that the cancellation of shares, i.e., a reduction in capital stock, occurs on the effective date of the resolution of the board of directors. Consequently, the shares in issue were cancelled effective April 1, 1986, and thus should not be included in the measure of the Taxpayer's franchise tax for the year 1987. Accordingly, the Department is hereby directed to reduce and make

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final the assessment for 1987 showing no additional tax due.

Done this 31st day of August, 1988.

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BILL THOMPSON  
Chief Administrative Law Judge