

# State and Local Tax Bulletin

April 7, 2011  
Alabama Edition



## Alabama Taxpayers' Bill of Rights II – House Version Introduced

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### Upcoming Seminars Involving Members Of Our SALT Practice Group

#### May 7, 2011

The American Bar Association Section of Taxation's annual meeting will be held in Washington, D.C. at the Grand Hyatt. The LLC's and LLP's Subcommittee will feature a panel presentation titled "State Tax Implications of the Proposed Series LLCs Regulations," with co-presenters Jimmy Long and Leigh Griffith of Waller Landen Dortch & Davis, LLP, Nashville. For more information, please visit [www.americanbar.org](http://www.americanbar.org).

#### May 10, 2011:

The Council On State Taxation (COST) Southeast Regional State Tax Update will be held in Birmingham at Regions Bank, Upper Lobby Auditorium. This half-day seminar will present an update on significant state tax issues for the Southeast states, and includes both industry and Alabama Department of Revenue speakers. The best view of the seminar is located on the COST calendar for May; click the date of May 10, and all of the necessary information will be available. The COST website: [www.cost.org](http://www.cost.org).

This bulletin summarizes the landmark legislation – **House Bill 427** – that was introduced last Thursday by Representative Paul DeMarco, and will be handled in the Senate by Ben Brooks of Mobile (SB 347), which reflects the work of members of the Alabama State Bar Tax Section, in cooperation with the Alabama Department of Revenue ("ADOR") and members of the Alabama Society of CPAs ("ASCPA"), over the past several years. The bill incorporates the provisions of the proposed Alabama Tax Appeals Commission Act, which has been endorsed by several business groups in previous years. To date, the Alabama State Bar, the Business Association Tax Coalition, the Business Council of Alabama, the Alabama Retail Association, the ASCPA, the Birmingham Business Alliance, and the Council On State Taxation ("COST") have endorsed this bill. The Legislative Fiscal Office has scored the bill as revenue neutral.

- Creates the Alabama Tax Appeals Commission ("ATAC") by abolishing the current Administrative Law Division of the ADOR and transferring both the personnel and equipment to a newly-formed state agency, under the executive branch. Alabama is now in the distinct minority of states that lack an independent tax appeals tribunal and we continually receive a "D" on the annual State Tax Due Process Scorecard issued by COST, primarily for this reason. The ATAC provisions essentially track the American Bar Association's Model State Tax Tribunal Act, which the National Conference of State Legislatures, the American Legislative Exchange Council (ALEC), the National Taxpayers Union, and COST have endorsed, except that appeals from the ATAC will continue to be filed with the circuit courts.

Four important features that differ from earlier versions of the ATAC bill are:

- » Taxpayers may appeal final assessments of sales, use, rental and lodgings taxes from *self-administered cities and counties (and their private auditing firms)* to the ATAC, unless the governing body of the city or county opts-out.
- » No filing fees will be imposed by ATAC;
- » An ATAC judge may be removed from office by the Judicial Inquiry Commission for neglect of duty, inability to perform duties, malfeasance in office, or other good cause; and
- » One of the 7 members of the nominating committee for the next ATAC judge(s) will be the Commissioner of Revenue, as the ADOR requested.

Allowing taxpayers to appeal final assessments from self-administered cities and counties is a *major* step toward addressing the frustration of the business community and tax advisers with the differing interpretations and appeals procedures of many self-administered localities or their contract auditing firms.

- Extends the period in which the taxpayer can appeal both a preliminary and final

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assessment from 30 days to 60 days after issuance of the assessment. The ADOR's Legal Division is also given 60 days in which to file their answer with the ATAC, plus a 30 day extension if so requested within the initial 60 day period.

- Amends the statute imposing a minimum \$50 penalty when the taxpayer does not file a return by the due date. The ADOR assesses the penalty now even if no tax is due on the return and even if a refund is due. The revised penalty would not apply to any individual income taxpayer who is owed a refund on the delinquent tax return. Additionally, for all other returns in which the taxpayer does not owe any additional tax (i.e., a zero sales tax return), the \$50 penalty would only apply if the taxpayer fails to file the delinquent return within 30 days after written notification from the ADOR. This change is strongly advocated by the ASCPA.

- Clarifies that the failure to pay penalty, which was expanded in 2009 (in the film incentives bill) to apply to the "correct" amount of tax required to be shown on a return, only begins to accrue 30 days after the first *written* notice and demand, and only applies to the "net" amount of underpaid tax. Additionally, the bill clarifies that neither failure-to-pay penalty will apply to estimated tax payments, consistent with federal law.

- Clarifies that filing an amended tax return with a refund claim does not extend or create a new three year statute of limitations period, consistent with federal case law, thus overruling the ALD's (incorrect) 2000 decision in *Dupree v. ADOR*.

- At the request of the ADOR, allows them up to six months in which to review a refund claim and, if necessary, to enter a preliminary assessment but limited to the adjustments at issue in the refund claim, when the statute of limitations is about to expire. Conversely, we added an exception to the time limits on filing a refund claim to allow taxpayers to request a refund in their petition for review of a preliminary assessment, but if filed after the normal statute of limitations has run, the claim is limited to the issues in the preliminary assessment.

- Creates an expedited revenue ruling procedure by which a taxpayer can receive a ruling within 30 days if they pay a \$3,000 filing fee, and in all events requires the ADOR's Legal Division to contact the taxpayer or its authorized representative – if they so request – to discuss their ruling request, prior to the ADOR issuing the ruling.

- At the request of the ADOR, increases the penalties amounts for negligence, fraud, and frivolous tax returns and frivolous appeals to the ATAC to conform to current federal law. The current system of penalties apparently is not deterring tax protesters.

- At the request of the ADOR, adds a substantial understatement penalty, similar to federal law, and adds penalties for failure to file partnership/S corporation information returns or failure to pay tax by EFT when required by law (also consistent with federal law). However, after input from COST and other business groups, the threshold for "substantial understatement" was increased to the greater of \$5,000 or 20% of the tax required to be shown on the return.

- Extends from two years to three years the statute of limitations on filing a refund claim for income tax withheld from a taxpayer-employee's wages that is later determined to have been overpaid, consistent with federal law.

- Requires that the ADOR attach not only to the *preliminary* assessment but to the *final* assessment a written description of the basis for the assessment and any penalties (currently, a "bare" final assessment can be issued, without any explanation as to the calculation of or legal basis for the assessment/penalties).

- At the suggestion of the ADOR, authorizes the ADOR to issue revenue procedures, similar to those issued by the IRS, that constitute their interpretation of the law as applied to a particular industry, but only if requested by an organization representing the industry or a trade association.

- Clarifies that the circuit courts have jurisdiction to hear, and if appropriate, to grant a motion to quash a subpoena issued by the ADOR to the extent the subpoena is overbroad or seeks privileged information.

- At the request of the ADOR, and because our income tax law generally piggybacks federal income tax law, amends the "RAR" statute requiring taxpayers to report IRS audit changes to the ADOR or allowing taxpayers to file a refund claim if the IRS granted a refund to them for the same tax period and same issues. The statute of limitations on assessment may not close until the taxpayer files an amended return and reports the IRS audit adjustment, which the taxpayer would be required to file within 6 months after a final determination of their federal tax liability (one year under current law). However, the taxpayer will continue to have one year after the grant of an IRS refund in which to file an equivalent refund claim with the ADOR.

- Conforms to two intervening changes to the "innocent spouse" rules under the Internal Revenue Code to expand the scope of this defense for Alabama spouses.

- Automatically nullifies any preliminary assessment that has been outstanding more than five years as of October 1, 2011 (i.e., issued prior to October 1, 2006), unless it is withdrawn before that date or a final assessment issued thereon or the parties agree to extend the time period. Under current law, the issuance of a preliminary assessment—which was intended to allow the parties to resolve their differences administratively—suspends the statute of limitations on assessments *indefinitely*. There have been reported instances where the ADOR or a self-administered local government or its contract auditing firm decided to simply sit on a preliminary assessment when they concluded that it was probably erroneous but they wished to wait for the law to become more favorable to them (e.g., new case or a change in the interstate or intra-state nexus rules). In the meantime, the taxpayer had no appeal rights.

- For any other preliminary assessment not described above that is issued by either the ADOR or a self-administered city or county, but then lies dormant for three years, the taxpayer has the *option* to appeal the preliminary assessment to the ATAC or appropriate circuit

court. See above explanation.

- Requires the Taxpayer Advocate to contact the taxpayer or his/her representative before issuing a denial of their request for an interest abatement or waiver of penalties. Under current law, the TA need not even contact the taxpayers or CPA/attorney to learn their side of the story or discuss his concerns about their request. If requested by the ATAC judge, allows the Taxpayer Advocate to review and correct a final order if there is newly-discovered evidence that shows the taxpayer was incorrectly assessed.
- Allows the Taxpayer Advocate to (a) reinstate the merchant's discount for retailers who file a sales tax return after its due date due to "reasonable cause" (e.g., death of the owner or natural disaster), and (b) waive late filing/payment penalties for areas of the State affected by a natural disaster. Currently, only the Commissioner has that power.
- Grants the ADOR and local governments the statutory authority--in conformity with federal law (see IRC §§ 7405 and 6602)--to recover an erroneously-issued tax refund, within two years of issuance.
- Clarifies that taxpayers have the option to appeal to the ATAC any proposed adjustments by the ADOR to their net operating loss deductions or carryovers, even though the proposed adjustment does not result in an assessment of tax or a denied refund claim.
- Makes several technical corrections to current law and clarifies the powers of the ATAC with respect to denied refund claims in order to allow the judge to consider any arguments or issues that may be raised by the taxpayer, even if the taxpayer did not raise the argument or issue earlier in the appeal process. This would override the 2009 Court of Civil Appeals ruling in *Rheem Manufacturing Company vs. ADOR*.
- At the request of the ADOR, allows them to suspend an automobile dealer's access to ETAPs (electronic title application processing) if the dealer fails to file the required surety bond or qualifying license, upon electronic notice to the dealer through ETAPs.

We are pleased with the final product and believe that 2011 is the opportune time to pass this much-needed legislation, and would like to thank Representative DeMarco and Senator Brooks for their leadership.

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