

State and Local Tax Bulletin

July 7, 2011

Alabama Edition



Are Members of an LLC Personally Liable for Their LLC's Sales and Payroll Taxes?



BRADLEY ARANT
BOULT CUMMINGS
LLP

Bruce P. Ely and James E. Long, Jr.

Chief Administrative Law Judge Bill Thompson recently affirmed his 2010 ruling that the individual members of a multi-member LLC are not personally liable for withholding (payroll) or sales taxes owed by the LLC, unless they qualify as "responsible persons" under the state's 100% penalty statute. That issue remains critically important to investors in LLCs that operate in Alabama. *Box Family Restaurants, LLC v. State Department of Revenue*, Admin. Law Div. Dkt. No. S. 11-375 (Prelim. Order on Taxpayer's Appl. for Reh'g June 28, 2011).

In this new ruling, Judge Thompson initially dismissed the appeal because the LLC member's notice of appeal was not filed within 30 days after entry of the final assessment. The member timely applied for rehearing and argued that he did not receive the final assessment until well after the mandatory 30 day appeal period had expired. He subsequently appealed within 30 days from his receipt of the final assessment, arguing that he had never been actively involved in his son's business. Judge Thompson ordered the Alabama Department of Revenue (the "Department") to notify the Administrative Law Division whether it properly mailed the final assessment at issue to the member's last known address (vs. the LLC's last known address) by certified mail.

Obviously, there could be a Due Process issue here. If the Department failed to notify the member properly, the Judge stated that the Administrative Law Division would reinstate the appeal on its docket but then hold the case in abeyance pending a final decision in *Nonna Rose Kingsley LLC*, which has been pending in Jefferson County Circuit Court for over 15 months now, with no trial date set.

Readers may recall that *Kingsley* – like *Box Family* – involved final assessments entered against both the restaurant LLC and its members, the amount of which was not contested. The only issue was whether a local physician, Dr. John Kingsley, was personally liable for the tax as a 25% and passive member. In *Bayside Tire & Exhaust, LLC v. State Department of Revenue*, Judge Thompson held that the individual members of a multi-member LLC that was taxed as a partnership for federal and Alabama income tax purposes were jointly and severally liable for the LLC's payroll withholding obligations, based on a provision in the Alabama LLC Act that conforms Alabama tax law to the federal entity classification rules. Admin. Law Div. Dkt. No. W. 98-272 (Oct. 13, 1998).

The taxpayer successfully argued in *Kingsley* that *Bayside* was incorrectly decided because of the different state law liability obligations imposed on members of an LLC versus general partners. Additionally, the taxpayer cited the Internal Revenue Service's position with respect to federal employment taxes that "if under state law the members of an LLC are not liable for the debts of the LLC, then absent fraudulent transfers or other special circumstances, the IRS may not collect the LLC's employment tax liability [directly] from the members..." Rev. Rul. 2004-41, 2004-18 I.R.B. 845.

Because the Alabama LLC Act provides that members of an LLC are not personally liable for the debts of the LLC, unlike general partners of a partnership, Judge Thompson agreed with the taxpayers in *Kingsley* and held that *Bayside* had been incorrectly decided. "[C]onsistent with the IRS' position on the issue, LLC members cannot be held personally liable for any [Alabama] taxes owned by the LLC," such as withholding, sales and use, and other non-income taxes. However, "as under federal law, the members may, under the appropriate circumstances, be held personally liable for any trust fund taxes under Alabama's [responsible person penalty statute]."

Judge Thompson's holdings in *Kingsley* and *Box Family* illustrate the well-established principle that when Alabama's taxing provisions are modeled after or adopted from federal provisions, such as the classification of LLCs for purposes of taxation, the IRS' guidelines with respect to that provision should also be followed. See Ala. Code § 40-18-1.1(b); *Ex parte Jones Mfg. Co., Inc.*, 589 So. 2d 208 (Ala. 1991).

The authors expect the Alabama Legislature to address this issue next Spring since Judge Thompson is holding a number of similar cases in abeyance pending the outcome of the *Kingsley* appeal, and the ADOR has not changed its position. The authors are members of a Task Force commissioned by the Alabama State Bar Tax Section to study this issue as well as several others involving the manner in which LLCs and other Subchapter K entities are taxed for purposes of sales, use, rental, property, excise, etc. taxes. For example, should a single member LLC be disregarded for purposes of all these taxes or solely for income and financial institution excise taxes? Jimmy Long was the principal author of an article published last year in *The Alabama Lawyer* on these issues. A copy of that article is available on our SALT Practice Group's website at <http://www.babc.com/files/Publication/dd85c2ce-7ea0-4a4e-b424-4a5cbe02dcb5/Presentation/PublicationAttachment/844ce9da-18e4-471b-8cac-387daf2fc81/AL%20Lawyer%20Article.pdf>.

U.S. News & World Report Ranking

Bradley Arant Boulton Cummings LLP has received the fourth highest number of top-tier rankings in the country in the inaugural U.S. News & World Report – Best Lawyers list of top U.S. law firms.

As it has done for many years for hospitals and colleges, this year U.S. News, working with the attorney ranking company Best Lawyers in America, ranked U.S. law firms based on a number of criteria, including client satisfaction. We are pleased to note that each member of our SALT Practice Group who is a partner in the firm was also included in Best Lawyers in America this year, and in many cases has been included for many years prior as well.



Bradley Arant Boulton Cummings LLP Office Locations:

ALABAMA

One Federal Place
1819 Fifth Avenue North
Birmingham, AL 35203
(205) 521-8000

200 Clinton Avenue West, Suite 900
Huntsville, AL 35801
(256) 517-5100

The Alabama Center for Commerce
401 Adams Avenue, Suite 780
Montgomery, AL 36104
(334) 956-7700

MISSISSIPPI

188 E. Capitol Street, Suite 400
Jackson, MS 39201
(601) 948-8000

NORTH CAROLINA

100 North Tryon Street, Suite 2690
Charlotte, NC 28202
(704) 332-8842

TENNESSEE

1600 Division Street, Suite 700
Nashville, TN 37203
(615) 244-2582

WASHINGTON, DC

1615 L Street, N.W., Suite 1350
Washington, DC 20036
(202) 393-7150

This newsletter is sent to our friends as a courtesy of Bradley Arant Boulton Cummings LLP. If you would prefer not to receive future emails of this type, please contact our practice group assistant Sherry Barber, at sbarber@babc.com.

This newsletter is a periodic publication of Bradley Arant Boulton Cummings LLP and should not be construed as legal advice or legal opinions on any specific facts or circumstances. The contents are intended for general information only, and you are urged to consult your own lawyer or other tax advisor concerning your own situation and any specific legal questions you may have. For further information about these contents, please contact your lawyer or any of the lawyers in our practice group.

The Alabama State Bar requires the following disclosure: "No representation is made that the quality of the legal services to be performed is greater than the quality of legal services performed by other lawyers."

©2011 Bradley Arant Boulton Cummings LLP

SALT Practice Group:

Bruce P. Ely, Chair
(205) 521-8366
bely@babc.com

Brett R. Carter
(615) 252-2383
br Carter@babc.com

Joseph W. Gibbs
(615) 252-2317
jj Gibbs@babc.com

W. Stanley Gregory
(334) 956-7604
sgregory@babc.com

Christopher R. Grissom
(205) 521-8514
cgrissom@babc.com

K. Wood Herren
(205) 521-8505
wherren@babc.com

Emil Hirsch
(202) 719-8211
ehirsch@babc.com

James E. Long, Jr.
(205) 521-8626
jelong@babc.com

Patricia Head Moskal
(615) 252-2369
pmoskal@babc.com

Brian S. Shelton
(615) 252-2313
bshelton@babc.com

William T. Thistle, II
(205) 521-8985
wthistle@babc.com

Robert D. Thorington
(334) 956-7609
rthorington@babc.com

Robert C. Walthall
(205) 521-8308
rwalthall@babc.com

Stephen M. Wilson
(601) 592-9957
swilson@babc.com



BRADLEY ARANT
BOULT CUMMINGS
LLP