WILSON INVESTMENT COMPANY, LLC 2660 EASTCHASE LANE, SUITE 100 MONTGOMERY, AL 36117-7024,	§	STATE OF ALABAMA ALABAMA TAX TRIBUNAL
Taxpayer,	§	DOCKET NO. BPT. 16-541
v.	§	
STATE OF ALABAMA DEPARTMENT OF REVENUE.	§	

FINAL ORDER

This appeal involves the Revenue Department's denial of 2009, 2012, and 2014 Alabama Business Privilege tax ("BPT") refunds requested by Wilson Investment Company, LLC ("Taxpayer"). The Taxpayer elected treatment as a Family Limited Liability Entity ("Family LLE") on its tax year 2009, 2012 and 2014 BPT returns. The Department determined that the Taxpayer did not qualify for the Family LLE election in those years, and denied the refunds in issue. The Taxpayer appealed to the Tax Tribunal pursuant to Code of Ala. 1975, §40-2A-7(c)(5)a.

Procedural History

The Taxpayer filed its tax year 2009 BPT return claiming a Family LLE election and reported and paid tax in the amount of $500, the maximum amount of tax due by an entity qualifying for and claiming the Family LLE election pursuant to Code of Ala. 1975, §40-14A-22(d)(2). The Department determined that the Taxpayer did not qualify for Family LLE treatment and entered an assessment against the Taxpayer on December 18, 2014 in the amount of $13,959.63. The Taxpayer appealed the assessment to the Tribunal pursuant to Code of Ala. 1975, §40-2A-7(b)(5)a, on January 6, 2015. On August 3, 2015, the Taxpayer informed the Tribunal that it intended to pay the assessment in full. Consequently, the appeal was dismissed.

The Taxpayer also claimed the Family LLE election on its tax year 2012 and 2014 BPT returns and reported and paid tax in the amount of $500 in each year. The Department again determined that the Taxpayer did not qualify for Family LLE treatment in those years and entered assessments against the Taxpayer on August 20, 2015 in the amounts of $15,955.20 and $15,086.37, respectively. On September 11, 2015, the Taxpayer paid the 2009, 2012 and 2014 assessments in full and any additional interest that accrued.

On November 4, 2015, the Taxpayer filed a petition for refund with the Department claiming it was entitled to the Family LLE election in tax years 2009, 2012 and 2014, and requesting a refund in the amount it paid to satisfy the final assessments entered for those years. The Department did not grant or deny the petition within six months from the date it was filed. Thus, the petition was deemed denied by operation of law pursuant to Code of Ala. 1975, 40-2A-7(c)(3). The Taxpayer timely appealed to the Tribunal on May 6, 2015.

Issues in Dispute

In its appeal, the Taxpayer asserts that it qualifies for treatment as a Family LLE in tax years 2009, 2012 and 2014. As such entity, the Taxpayer argues that its tax liability for those years should be limited to $500 pursuant to §40-14A-22(d)(2). Specifically, the Taxpayer states that in each of the years at issue, the Taxpayer was directly or constructively owned by Wynonna W. Wilson ("WWW") and her four children: James W. Wilson, III, William B. Wilson, Elizabeth W. Hunter, and Winston Wilson Reese (collectively, the "Wilson children"). As such, it argues that it meets the requirements for treatment as a Family LLE because it is directly and constructively owned by an individual

and members of the individual's family pursuant to §40-14A-1(h)(4). The Department argues that 40-14A-1(h)(4) attributes constructive ownership of the Taxpayer to WWW, solely, and therefore, the Taxpayer cannot qualify as a Family LLE for purposes of the Family LLE Election.

The Taxpayer also argues, alternatively, that the Taxpayer qualifies for the Family LLE election because §40-14A-1(h) permits a limited liability entity owned eighty percent (80%) or more by only one individual to qualify for the Family LLE election.

Analysis

The BPT is an annual privilege tax levied in §40-14A-22 on every corporation, limited liability entity and disregarded entity doing business in Alabama. The amount of the tax levied on a taxpayer each tax year is determined by multiplying the taxpayer's net worth in Alabama by a schedule of rates that are based on the taxpayer's taxable income. The amount of tax due is limited for any electing Family LLE and shall not exceed $500.

An "Electing Family LLE" is defined at Code of Ala. 1975, §40-14A-1(h) as a limited liability entity whose profits and capital interests are eighty percent (80%) or more directly or constructively owned by an individual and the members of the individual's family, and who elects annually to be taxed as such entity. The statute further defines "members of the individual's family" as including the individual's spouse, grandparents, and the lineal descendants of the grandparents and their spouses. §40-14A-1(h)(4). To determine constructive ownership, the statute provides that "whether interests are constructively owned shall be determined using the attribution rules set forth in 26 U.S.C. §318 as if the

profits and capital interests for the [Family LLE] were stock and without regard to the fifty percent limitations contained in 26 U.S.C. § 318(a)(2)(C) and 26 U.S.C. §318(a)(3)(C)." Id.

The relevant attribution rules found in §318 ("the attribution rules") provide the following:

> §318(a)(2)(B)(i) provides that stock owned, directly or indirectly, by or for a trust shall be considered as owned by its beneficiaries in proportion to the actuarial interest of such beneficiaries in such trust.
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> §318(a)(2)(B)(ii) provides that stock owned, directly or indirectly, by or for any portion of a trust of which a person is considered the owner under subpart E of part 1 of subchapter J (relating to grantors and others treated as substantial owners) shall be considered as owned by such person.

In 2006, James W. Wilson, Jr. ("JWW, Jr.") died testate. Relevant to the issues presented in this appeal regarding the 2009 tax year, his will established two trusts: the JWW, Jr. Marital Trust ("the Marital Trust") for the benefit of WWW; and the JWW, Jr. Residual Trust ("the Residual Trust") for the benefit of WWW and the Wilson children. It is undisputed that in the 2009 tax year, the Taxpayer was owned one percent (1%) by WWW and ninety-nine percent (99%) by the Estate of James W. Wilson, Jr. ("the Estate"). It is also undisputed that the Estate's beneficiaries in 2009 were WWW, the Marital Trust and the Residual Trust.

It is undisputed that in the 2012 and 2014 tax years, the Taxpayer was owned one percent (1%) by the Marital Trust and ninety-nine percent (99%) by the Wynona W. Wilson 2008 Irrevocable Trust ("the 2008 Trust"). It is also undisputed that the 2008 Trust is a grantor trust for federal tax purposes.

Relevant to the 2009 tax year, the Department argues that the attribution rules attribute ownership of the Taxpayer to WWW, solely. Specifically, the Department argues

that because the Wilson children are not beneficiaries of the Marital Trust and are merely contingent beneficiaries of the Residual Trust, they have no present interest equating to actual ownership in the Estate in the 2009 tax year. Put another way, the Department argues that the trusts' only primary beneficiary is WWW, and therefore, only WWW has a present interest in the trusts. Consequently, the attribution rules attribute sole ownership of the trusts – and thus, the Estate – to WWW. It concludes that because WWW directly owns one percent (1%) of the Taxpayer and constructively owns the remaining ninety-nine percent (99%) of the Taxpayer, that the Taxpayer is not owned by WWW *and* individual members of her family – a requirement necessary to qualify for the Family LLE election. I disagree.

For the reasons set forth below, I find that the Wilson children are primary beneficiaries with a present ownership interest in the Residuary Trust. As such, they have an actual ownership interest in the Residuary Trust – and thus the Estate – in tax year 2009 pursuant to the attribution rules. Therefore, the Taxpayer was directly owned by WWW and constructively owned by both WWW and the Wilson children in 2009. Consequently, the Taxpayer qualifies for the Family LLE election in that year.

Relevant to the 2012 and 2014 years, the Department argues that the attribution rules, specifically the rule found at §318(a)(2)B)(ii), dictate that the grantor of the 2008 Trust is the owner of any interests owned by the 2008 Trust. The Department argues, that because WWW is the only primary beneficiary of the Marital Trust, one percent (1%) of the Taxpayer is owned constructively by WWW, and as the grantor of the 2008 Trust, the remaining ninety-nine percent (99%) ownership of the Taxpayer is treated as constructively owned by WWW. It concludes that because WWW constructively owns one hundred

percent (100%) of the Taxpayer, that the Taxpayer is not owned by WWW *and* individual members of her family – a requirement necessary to qualify for the Family LLE election. I agree.

For the reasons set forth below, I find that the attribution rules are clear that WWW, solely, is the constructive owner of the Martial Trust and the 2008 Trust. As such, the Taxpayer is constructively owned by WWW, solely. Consequently, the Taxpayer does not qualify for the Family LLE election in tax years 2012 and 2014.

Tax Year 2009

It is undisputed that the Taxpayer was owned one percent (1%) by WWW and ninety-nine percent (99%) by the Estate in the 2009 tax year. The beneficiaries of the Estate in tax year 2009 were WWW, the Marital Trust and the Residual Trust.

The Marital Trust of the James W. Wilson, Jr. Trust dated December 5, 2003

The relevant provisions of the Marital Trust are as follows:

> A.) The net income shall be paid to [WWW] during her life at least quarter-annually.
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> B.) In addition, if Trustee in Trustee's sole discretion considers it advisable, Trustee may from time to time make payments from principal in such amounts as Trustee may deem appropriate for the benefit of [WWW].
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> C.) Upon my said wife's death, Trustee shall pay the remaining principal to or in trust for such one or more of [the Wilson children], *in such amounts or proportions as [WWW] may appoint by Will consisting specific reference to this power of appointment.* [emphasis added.]

The Taxpayer argues that the Wilson children have contingent rights with vested interests, and therefore should be treated as having a present ownership interest. The Taxpayer's argument is incorrect. Beneficiaries cannot be vested if their right to receive a

future interest in the trust is unknown. Here, WWW has the power to appoint, *or choose not to appoint,* any one of or all the Wilson children. Thus, the Wilson children's interest in the trust is entirely contingent on WWW's actions. Further, the Wilson children have no present interest in the trust because they are not currently entitled to a benefit from the trust. The Wilson children only receive a benefit from the trust upon the death of WWW. Because the Wilson children are not entitled to a current benefit from the trust and because their future benefit is uncertain, the children are contingent remainder beneficiaries. For purposes of the Family LLE, the Wilson children's contingent remainder interests are not present ownership interests. Consequently, they do not have actual ownership interests in the Marital Trust pursuant to the attribution rules.

The Residual Trust of James W. Wilson, Jr. Trust dated December 5, 2003

The relevant provisions of the Residual Trust are as follows:

A.) If [WWW] survives [JWW, Jr.], during her lifetime:

> 1. The net income shall in the discretion of Trustee either be accumulated, in whole or part, and added to principal at the end of the annual accounting period *or paid in such amounts as Trustee may deem appropriate for the health, support, maintenance and education of [WWW] and [the Wilson children].* [emphasis added.]
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> *2.* In addition, if Trustee in Trustee's sole discretion considers it advisable, *Trustee may from time to time make payments from principal in such amounts as Trustee may deem appropriate for the health, support, maintenance and education of [WWW] and [Wilson children].* [emphasis added.]
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> 3. Upon [WWW's] death, the remaining principal shall be paid to or in trust for such one or more of my issue, in such amounts or proportions as [WWW] may appoint by Will containing specific reference to this power of appointment.

In the Residual Trust, the trustee has the sole discretion to distribute income or principal to WWW and the Wilson children. WWW and the Wilson children are discretionary beneficiaries because payments are made at the discretion of the trustee. However, they have an immediate interest in the trust income and principal because they can receive a benefit from trust income and principal currently – they do not have to wait on a certain event to trigger their right to payments. Thus, they are primary beneficiaries of a discretionary trust, not contingent remainder beneficiaries as the Department argues. The fact that the benefit is paid to WWW and the Wilson children at the discretion of the Trustee does not change the fact that all are primary beneficiaries. As such, they had a present interest in the trust in 2012 and 2014. Consequently, they have actual ownership interests in the Residual Trust pursuant to the attribution rules.

The relevant attribution rule of §318 provides that stock owned, directly or indirectly, by or for a trust shall be considered as owned by its beneficiaries in proportion to the actuarial interest of such beneficiaries in such trust. §318(a)(2)(B)(i). For purposes of the Family LLE, the Wilson children's primary interests are actual present ownership interests in the Residual Trust. Because the Taxpayer was directly owned by WWW and constructively owned by WWW and the Wilson children in the 2009 tax year, the Taxpayer qualified for the Family LLE election in that year.

Tax Years 2012 and 2014

It is undisputed that the Taxpayer was owned one percent (1%) by the Marital Trust and ninety-nine percent (99%) by the 2008 Trust. It is undisputed that the 2008 Trust is a grantor trust for federal tax purposes. The Taxpayer asks the Tribunal to ignore that fact, and hold that the Wilson children have constructive ownership interest sufficient to qualify

as owners of the trust for purposes of the Family LLE election in tax years 2012 and 2014. In essence, the Taxpayer argues that the trust operates to bestow a vested benefit on the Wilson children, and that it is the language of the trust, and not the attribution rules, that should control. I disagree.

The plain language of §40-14A-1(h) provides "whether interests are constructively owned shall be determined using the attribution rules set forth in [§318]." The language of the statute is clear that there is no other test or method for establishing constructive ownership for purposes of determining whether an entity qualifies for the Family LLE election. Principles of statutory construction direct the Tribunal to interpret the plain language of a statute "to mean exactly what it says and to engage in judicial construction only if the language in the statute is ambiguous." *Ex parte Pratt*, 815 So. 2d 532, 535 (Ala. 2001).

The 2008 Trust is a grantor trust for federal tax purposes. The relevant attribution rule of §318 attributes ownership of a grantor trust solely to the grantor. §318(a)(2)(B)(ii). Specifically, the rule provides that that stock owned, directly or indirectly, by or for any portion of a trust which a person is considered the owner under subpart E of part 1 of subchapter J (relating to grantors and others treated as substantial owners) shall be considered as owned by such person. Id.

As grantor of the 2008 Trust, §40-14A-1(h) provides that WWW is the sole owner of the 2008 Trust, and therefore the sole constructive owner of the 2008 Trust's ninety-nine percent (99%) interest in the Taxpayer. As aforementioned, WWW is the only primary beneficiary of the Marital Trust. For purposes of the Family LLE election, she is the only constructive owner of the Martial Trust (and therefore the sole constructive owner of the

Marital Trust's one percent (1%) interest in the Taxpayer), as the Wilson children's contingent remainder interests are not present ownership interests. Consequently, because the Taxpayer was constructively owned solely by WWW in the 2012 and 2014 tax years, the Taxpayer does not qualify for the Family LLE election in those years.

The Taxpayer's Alternative Argument

In the alternative, should the Tribunal hold that the Taxpayer is constructively owned solely by WWW in any of the 2009, 2012 and 2014 years, the Taxpayer argues for the first time in its post hearing brief that §40-14A-1(h) permits an entity to qualify for the Family LLE Election if eighty percent (80%) or more of the profits and capital interests of the entity are owned by an individual. In essence, the Taxpayer argues that the Family LLE election is available for entities that are *either* individually owned *or* owned by an individual and the individual's family. In support of its argument, the Taxpayer asks the Tribunal to interpret the word "and" as an "or".

An "Electing Family LLE" is defined as a limited liability entity whose profits and capital interests are eighty percent (80%) or more directly or constructively owned by an individual *and* the members of the individual's family . . . ". (emphasis added.) The Taxpayer argues that "and" means that if other individuals own an interest in an entity, they must be in the same family. I disagree.

The Taxpayer's argument is illogical in that it asks the Tribunal to construe the word "and" as an "or" in one context and the same "and" as an "and" in another. Specifically, the Taxpayer asks the Tribunal to interpret the "and" as a disjunctive to determine that the statute does not require that eighty percent (80%) or more of a taxpayer be owned by an

individual and members of the family, but that as long as one individual owns at least eighty percent (80%) of a taxpayer the entity qualifies for the election. The Taxpayer then argues that the same "and" is only interpreted as a conjunctive when other individuals own an interest in the taxpayer – i.e., that only then is it a requirement that the other individuals all be members of the same family. I agree with the Department that this argument does not comport with the language of the statute or the generally understood rules of statutory construction. Perhaps the most practical reason is that the statute creating the election created it for a "Family" LLE.

The Department correctly stated in its Post Hearing Brief on pages 5 and 6 that reading the "and" as an "or" leaves the term "individual" without any field of operation in certain situations and leads to nonsensical results.

> Such a reading, however, leaves the term "individual" without any field of operation in certain situations and, in addition, leads to nonsensical results.
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> > """There is a presumption that every word, sentence, or provision [of a statute] was intended for some useful purpose, has some force and effect, and that some effect is to be given to each, and also that no superfluous words or provisions were used."'" Ex parte Children's Hosp. of Alabama, 721 So. 2d 184, 191 (Ala. 1998) (quoting Sheffield v. State, 708 So. 2d 899, 909 (Ala. Crim. App. 1997), quoting in turn 82 C.J.S. Statutes § 316 (1953)). Moreover, "[c]ourts will attempt to give meaning to a legislative enactment and it is presumed that the Legislature did not do a vain and useless thing," Alidor v. Mobile County Comm'n, 291 Ala. 552, 558, 284 So. 2d 257, 261 (1973).
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> City of Montgomery v. Town of Pike Road, 35 So. 3d 575, 584 (Ala. 2009).
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> The reading of the statute advocated by the Taxpayer means that not only would every single-member LLC owned solely by one "individual" qualify as a family LLE, but also an LLC owned entirely by "members of the individual's family," without any ownership by "the individual." However, there is no need to define the ownership of an LLC by reference to the

> "members of the individual's family" if the individual is not also an owner. The phrase "members of the individual's family" has no meaning without reference to the identity of the individual, and if the individual is not an owner of the LLC, there is no reason to define the LLC's ownership in terms of persons who are members of that individual's family – the statute becomes absurd.
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> > "It is a 'well established principle of statutory interpretation that the law favors rational and sensible construction.' " King v. State, 674 So. 2d at 1383 (quoting 2A Norman J. Singer, Sutherland Statutory Construction § 45.12 (5th ed.1992)). Moreover, "'[t]he courts will not ascribe to the legislature an intent to create an absurd or harsh consequence, and so an interpretation avoiding absurdity is always to be preferred.' " Daugherty v. Town of Silverhill, 672 So. 2d 813, 816 (Ala. Cr. App. 1995) (quoting 1A C. Sands, Sutherland Statutory Construction § 23.06 (4th ed.1972)).
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> Goodwin v. State, 728 So. 2d 662, 668 (1998).

The language of §40-14A-1(h) is clear and unambiguous that the entity must be owned not only by an individual, but by an individual and members of that individual's family. Principles of statutory construction direct the Tribunal to interpret the plain language of a statute "to mean exactly what it says and to engage in judicial construction only if the language in the statute is ambiguous." *Ex parte Pratt*, 815 So. 2d at 535. An entity does not qualify for the Family LLE election unless eighty percent (80%) of the profits and capital interests are owned by an individual and members of that individual's family.

The Taxpayer's request for refund of 2009 BPT, and any associated penalties and interest, is hereby granted. The Department's denial of the Taxpayer's request for a refund of 2012 and 2014 BPT, and any associated penalties and interest, is hereby affirmed.

This Final Order may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, §40-2B-2(m).

Entered June 16, 2017.

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CHRISTY O. EDWARDS
Associate Tax Tribunal Judge

cc: Craig A. Banks, Esq.
Riley W. Roby, Esq.