ATTORNEYS INS. MUTUAL OF THE SOUTH, INC., RISK RETENTION GROUP 200 INVERNESS PKWY. BIRMINGHAM, AL 35242-4813, Taxpayer, v. STATE OF ALABAMA DEPARTMENT OF REVENUE.	§ § § § § §	STATE OF ALABAMA ALABAMA TAX TRIBUNAL DOCKET NO. BPT. 15-860

FINAL ORDER

The Revenue Department assessed Attorneys Insurance Mutual of the South, Inc., Risk Prevention Group ("Taxpayer") for 2012 business privilege tax. The Taxpayer appealed to the Tax Tribunal pursuant to Code of Ala. 1975, §40-2A-7(b)(5)a. Because the facts are undisputed, the parties agreed that the Tribunal should decide the case on the pleadings. Charles Moses represented the Taxpayer. Assistant Counsel Craig Banks represented the Department.

The Taxpayer claimed a dividends received deduction of $3,510 on line 36a of its 2011 federal Form 1120-PC. It also claimed a net operating loss of $46,815 on line 36b of the return. The deduction and loss reduced the Taxpayer's federal taxable income on line 37 to $0. The Department recomputed the federal taxable income on the return by adding back the line 36a dividends received deduction of $3,510 and the line 36b loss of $46,815 to arrive at federal taxable income apportioned to Alabama of $50,312 ($50,325 x factor of 99.976 percent equals $50,312). The recomputation increased the Taxpayer's Alabama liability from $2,076 to $8,304, which resulted in the final assessment in issue.

The case turns on the correct interpretation of Department Reg. 810-2-8-.01. The Taxpayer is an insurance company. The above regulation is titled "Taxable Income for

Determining the Applicable Privilege Tax Rate." Paragraph (g) of the regulation reads as follows:

> (g) Insurance Companies. For U. S. Life Insurance Company filing Internal Revenue Service Form 1120-L, federal taxable income shall be total taxable income less the dividends received deduction and the operations loss deduction. For U. S. Property and Casualty Insurance Companies filing Internal Revenue Service Form 1120-PC, federal taxable income shall be taxable income less the dividend received deduction and the net operating loss deduction. This income shall be apportioned in accordance with Title 27, Code of Alabama 1975, relating to insurance companies.

The issue is how the word "less" should be interpreted in the phrase – "federal taxable income shall be total taxable income less the dividends received deduction and the net operating loss deduction."

The Taxpayer argues that a plain reading of the regulation requires that federal taxable income must be taxable income after taking the dividends received deduction and any net operating loss. The Taxpayer's Response to Department Answer at 1, reads in part as follows:

> The plain language of the Rule contemplates the final number to be treated as "taxable income" is "less" those described deductions. If the Rule had defined "Taxable Income" as the amount on line 37 of Form 1120-PC, without taking into account the deduction for dividends received or net operating loss, then the ADOR would be correct. But that is not the way the Rule reads for this type of entity. Interestingly in all other sections of the Rule, (a) through (h), it is clear that the "taxable income used to compute the tax rate for the Business Privilege Tax shall be" determined without permitting these or similar deductions from "taxable income" in determining the tax rate. For example, *Rule 810-2-8-.01(1)(1) C Corporations* reads:
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>> 1. "The taxable income used to determine the tax rate for the privilege tax shall be the federal taxable income **before** net operating loss and special deductions". . .
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> Thus, the Rule applicable to taxpayer requires that taxable income be the federal taxable income after the deductions for dividends received and net operating loss are deducted. It is just a tortured reading of the Rule to

> suggest that there is any basis for adding those items back to the amount on line 37 when the Rule could have used the exact same language as that for corporations.
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> Taxpayer's net income that is taxable after the aforementioned authorized deduction is zero, thus entitling Taxpayer to apply the minimum tax rate.

The Department contends that the word "less," as used in paragraph (g) of the regulation, should be construed as "without." "The phrase 'less the dividends received deduction and the net operating loss deduction' in the regulation is properly read as 'without the dividends received deduction and the net operation loss deduction.'" Department Brief at 2.

Federal taxable income on line 37 of the federal return is determined by deducting any dividends received and any net operating losses. Those deductions and losses are thus included in the computation of federal taxable income. I agree that use of the word "less" in paragraph (g) is awkward, but the clear intend of the phrase in issue is that federal taxable income should be total income without or less the dividends received deduction and the net operating loss deduction that was initially included in the computation of federal taxable income.

I agree with the following from the Department's Brief at 3, as follows:

> The Department's interpretation of Rule 810-2-8-.01 is clearly a reasonable interpretation. This is especially true considering the structure of IRS Form 1120-PC and the lack of any reason to grant the Taxpayer a deduction for an amount that is already present in the computation of taxable income on Form 1120-PC. Such a double deduction would be the natural result of the reading of the regulation that is advanced by the Taxpayer, wherein it suggests that its taxable income from Form 1120-PC should be reduced by the amounts of the dividends received deduction and the net operating loss deduction. Indeed, the only reason to address the dividends received deduction or the net operating loss deduction in the regulation is to modify the taxable income from Form 1120-PC to remove the two deductions for purposes of BPT computation.

In summary, the dividends received deduction and any net operating losses are deducted in arriving at federal taxable income. That is, federal taxable income already includes the dividends received and net operating loss deductions. The clear intent of paragraph (g) of the regulation is to remove those deductions from the computation. The inartful drafting of a regulation should not defeat the purpose and intent of the regulation.

The final assessment in issue is affirmed. Judgment is entered against the Taxpayer for $6,810.79. Additional interest is also due from the date the final assessment was entered, May 19, 2015.

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

Entered May 10, 2016.

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BILL THOMPSON
Chief Tax Tribunal Judge

bt:dr
cc: Craig A. Banks, Esq.
Charles H. Moses, III, Esq.