

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. INC. 87-132

DONALD L. & BARBARA A. COOK  
1245 Vista Lane  
Birmingham, AL 35216,

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§

Taxpayers.

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ORDER

The Taxpayers, Donald L. and Barbara A. Cook, requested a refund of 1982 income tax based on a net operating loss ("NOL") carryback from 1985. The Department partially denied the refund and the Taxpayers appealed to the Administrative Law Division. The Administrative Law Division entered a Recommended Order advising the Department to issue the additional refund as computed by the Taxpayers. Based on a review of the administrative record, the following order is hereby entered.

FINDINGS OF FACT

The Taxpayers reported a negative income of (\$117,793.00) on their 1985 Alabama income tax return. In conjunction therewith, the Taxpayers also filed an amended 1982 return and accompanying forms NOL-NL (net operating loss computation) and NOL-N2 (application for net operating loss carryback). The Taxpayers claimed a 1985 NOL carryback of \$74,103.00, which resulted in a 1982 refund claim of \$3,705.00. The Department examined the amended return and NOL forms and issued a partial refund of \$1,675.15, excluding interest.

Thereafter, the Taxpayers filed amended forms NOL-NL and NOL-N2 claiming a 1985 NOL carryback of \$104,053.00 and a total 1982 refund of \$5,202.55. The amended refund claim was based on the Taxpayers' treatment of a gain of \$70,544.00 from the sale of stock as "non-business income" on the amended form NOL-NL.

The Taxpayers computed the NOL loss on amended form NOL-N1 by deducting from the 1985 loss the personal exemption and credit for dependents (as required by Code of Ala. 1975, §40-18-15(a)(16)(f)(2)) and the excess of non-business deductions over non-business income (as required by Code of Ala. 1975, §40-18-15(a)(16)(f)(3)). A summary of the Taxpayers' amended NOL-NL computations is set out below:

1985 loss.....	(\$117,793.00)
Personal exemption and credit for Dependents..	\$ 3,300.00
Non-business deductions.....	\$105,037.00
Non-business income.....	94,597.00
Excess of non-business deductions.....	\$ 10,440.00
Total modifications.....	<u>\$13,740.00</u>
Net Operating Loss.....	(\$104,053.00)

The non-business income as claimed by the Taxpayers included a gain of \$70,544.00 on the sale of stock from the Taxpayers' personal portfolio. The Department reviewed the Taxpayers' computations and determined that the stock gain should not be included as non-business income on the NOL-NL. The exclusion substantially reduced the Taxpayers' NOL, and the Department consequently denied the Taxpayers' claim for additional refund. The amended NOL-NL as recomputed by the Department is as follows:

1985 loss.....	(\$117,793.00)
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Personal exemption and credit for Dependents..	\$ 3,300.00
Non-business deductions.....	\$105,037.00
Non-business income.....	24,053.00
Excess of non-business deductions.....	\$ 80,984.00
Total modifications.....	<u>\$84,284.00</u>
Net Operating Loss.....	(\$33,509.00)

The issue in dispute is whether the gain received by the Taxpayers from the sale of stock should be included on the NOL-N1 as non-business income.

CONCLUSIONS OF LAW

Code of Ala. 1975, §40-18-15(a)(16)(e) defines "net operating loss" as "the excess of the deductions allowed by this chapter over the gross income", with certain modifications. one of the modifications is set out in subparagraph (f)(3), which provides that the "deductions allowable by this chapter which are not attributable to a taxpayer's trade or business . . . shall be allowed only to the extent of the amount of the gross income not derived from such trade or business". That is, the NOL should not include (must be reduced by) the excess of non-business deductions over non-business income.

The gain from the sale of stock in the instant case was not attributable to the Taxpayers' business, i.e. the gain constituted non-business income, in that Taxpayers were not in the business of trading and selling stock. However, the Department argues that the gain should not be included as non-business income on the form NOL-NL because, unlike federal law, any loss from the sale of stock can be used in computing an Alabama NOL. The Department argues in brief as follows:

Although the sale of stock is not a normal business activity of the Taxpayers in the usual sense, loss from the sale of stock could be used in creating a net. operating loss for Alabama income tax purposes. For this reason, in determining the limitations for "non-business deductions" in computing an Alabama net operating loss, the resulting gain or loss from the sale of stock should be treated as "business income or deductions" rather than "non-business income or deductions".

The Department is partially correct in arguing that a stock loss is allowed in computing an Alabama NOL. A stock loss constitutes a non-business deduction (Code of Ala. 1975, §40-18-15(a)(5)) and thus would be allowed only to the extent of non-business income.

For example, if a taxpayer incurred a loss on the sale of stock, but had no additional non-business income, then the entire stock loss deduction would be disallowed (subtracted) in computing the NOL on form NOL-N1.

In any case, the plain language of the statute must control. Quick v. Utotem of Alabama, 365 So.2d 1245. The subsection (f)(3) modification clearly requires the use of non-business income in computing the net excess of non-business deductions over non-business income. The stock gain in issue is admittedly non-business income and thus must be used in the computation.

The above considered, it is hereby ordered that the Department issue the additional refund as computed by the Taxpayers in the amount of \$3,527.40 along with interest. This Order is the final order of the purposes of judicial review under Code §41-22-20.

Done this 9th day of August, 1988.