

810-3-164-.01 Adjustments to Basis of Stock and Indebtedness.

(1) Basis Adjustments - Shareholder's Stock in an Alabama S Corporation.

(a) The shareholder's basis in the Alabama S Corporation stock is increased by:

1. Any separately stated income attributed to Alabama as computed under § 40-18-162(a)(1), Code of Alabama 1975, to the extent included in the shareholder's return, as amended or adjusted.

2. Any nonseparately stated income attributed to Alabama as computed under §40-18-162(a)(2), to the extent included in the shareholder's return, as amended or adjusted.

3. Any oil and gas depletion deduction attributed to Alabama in excess of the basis of the wells being depleted.

(b) The shareholder's basis in the Alabama S Corporation stock is decreased by:

1. Any distributions which constitute a return of capital under §40-18-165.

2. Any separately stated loss and deductions attributed to Alabama computed under §40-18-162(a)(1); such as charitable contributions.

3. Any nonseparately stated loss and deductions attributed to Alabama computed under §40-18-162(a)(2).

4. Any losses or expenses attributed to Alabama not deductible by the corporation or chargeable to its capital account.

5. Any depletion deduction attributed to Alabama on oil and gas property to the extent such deduction does not exceed the proportionate share of the adjusted basis of such property allocated to the shareholder.

(c) Basis Not Reduced Below Zero. The basis of the stock, as adjusted in the manner provided in paragraph (1) above, will not be reduced below zero. Any amount that would reduce the basis of the stock below zero will be used to adjust the shareholder's basis (but not below zero) in any indebtedness due to the shareholder from the corporation, as provided in paragraph (2) below.

(d) Multistate Operations. For tax years beginning after December 31, 1996:

1. The increases under subparagraph (a) and the decreases under subparagraph (b) will include the entire amount, without allocation and apportionment under Chapter 27, Title 40, Code of Alabama 1975, of the shareholder's pro rata share of such increases and decreases during the taxable year.

2. If an item of income is subject to allocation and apportionment, the basis increases under subparagraphs (1)(a)1, (1)(a)2 and (1)(d)1 will be allowed only in proportion to the income reported on the taxpayer's return that bears to the amount of income allocated and apportioned to Alabama and required to be included in the shareholder's return.

(2) Basis of Shareholder Loans to the Corporation. The shareholder's basis in any indebtedness due to the shareholder from the corporation will be:

(a) The basis (determined as provided in §40-18-6) of the debt, less

(b) Any excess basis adjustments to the shareholder's stock as provided in subparagraph (1)(c) above, but

(c) Not less than zero.

(3) See Rule 810-3-162-.01 for carryover of excess amounts which would reduce the basis of debt or stock below zero except for the provisions of this regulation.

(4) Restoration of the Shareholder's Basis in Indebtedness and Stock. Positive adjustments to the shareholder's basis in future years will be first applied to increase the shareholder's basis in any indebtedness due to the shareholder from the corporation, and then applied to increase the shareholder's stock basis.

(5) If the stock of the Alabama S corporation becomes worthless, the amount of loss to be deducted by the shareholder will be determined after making the basis adjustments set out in paragraph (1) above.

(6) For nonresident shareholders, the investment in Alabama S corporation stock and debt will be considered to be attributed to the shareholder's state of domicile. For resident shareholders, the investment in Alabama S corporation stock and debt will be considered to be attributed to Alabama in full.

(7) Examples. The following examples will serve to illustrate the operation of this regulation:

(a) Able, an Alabama resident, is the 100% owner of Sussex Corporation, an Alabama S corporation with all its activities attributed to Alabama. Able's basis for his Sussex Corporation stock at the beginning of 1985 is \$1,000. In addition, Able has a basis of \$500 in a loan from him to the corporation.

1. On its tax return for the year ended December 31, 1985, Sussex reports the following:

Non-separately stated loss	\$1,200
Charitable contributions	

2. Able's basis in his Sussex stock and in the debt of the corporation at December 31, 1985 is computed as follows:

	<u>Basis in Stock</u>	<u>Basis in Debt</u>
Basis at January 1, 1985	\$1,000	\$ 500
Non-separately stated loss and charitable contributions reduce stock basis (but not below zero)	<u>(1,000)</u>	<u>(300)</u>
Basis at December 31, 1985	<u>\$ -0-</u>	<u>\$ 200</u>

(b) In the year ended December 31, 1986, Sussex Corporation reports the following:

Net income	\$2,500
Charitable contributions	300

1. Able's basis in his Sussex Corporation stock and the debt owed to him from the corporation at December 31, 1986 is computed as follows:

	<u>Basis in Stock</u>	<u>Basis in Debt</u>
Basis at January 1, 1986 (see above)	-0-	\$ 200
Net income increases basis of debt to extent of prior reduction		300
Balance of net income and separately stated items increases		

basis in stock	<u>1,900</u>	
Basis at December 31, 1986	<u>\$1,900</u>	<u>\$ 500</u>

(c) The situation is the same as in (a) and (b) above except (1) the tax periods are 1997 and 1998 and (2) the corporation has only 50% of its activities attributed to Alabama.

1. Able reports his 100% share of the income attributed to Alabama.

2. Able's basis in his Sussex Corporation stock and in the debt to him from the corporation will be the same as computed in (a) and (b) above. For tax periods beginning after December 31, 1996, the shareholder's basis is adjusted by his share of the total Alabama S corporation income (loss).

(d) The situation is the same as in (c) above except Able (100% shareholder) reports on his 1998 tax return only 95% of the nonseparately computed income attributed to Alabama. Able's basis should increase by only 95 % of the nonseparately computed income.

1. Able's basis in his Sussex Corporation stock and in debt to him from the corporation at December 31, 1998 is computed as follows:

	<u>Basis in Stock</u>	<u>Basis in Debt</u>
Basis at January 1, 1998 (see above)	\$-0-	\$200
Net income increases basis of debt to extent of prior reduction		300
Balance of net income (2375-300) and separately stated items (-300) increases basis in stock	<u>1775</u>	
Basis at December 31, 1998	<u>\$1775</u>	<u>\$500</u>

(8) Inherited Stock of an Alabama S Corporation.

(a) If any person acquires stock in an Alabama S corporation by reason of the death of a decedent or by bequest, devise, or inheritance, then the treatment of any item of income of the S corporation shall be determined in accordance with 26 U.S.C. § 691, concerning recipients of income in respect of a decedents, which shall be applied as if the decedent had held directly his or her pro rata share of such item. For interpretation of federal statutes adopted by the Alabama legislature, see Rule 810-3-1.1-.01, Operating Rules.

(b) The basis of any stock in an Alabama S corporation which is determined under § 40-18-6 shall be reduced by the portion of the value of the stock that is attributable to items constituting income in respect of a decedent.

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