

810-3-1.1-.01 Operating Rules.

(1) For purposes of Chapter 18 of Title 40, Code of Alabama 1975, when the legislature adopts a specified section or sections of Title 26, United States Code ("26 U.S.C." or "IRC") or a federal public law (Pub. L. or P.L.), references shall be to those specified sections as amended from time to time.

(2) When any gain, loss, income, basis, earnings and profits, or any other item is to be determined in accordance with the provisions of federal law (Title 26, United States Code or public law) which have been adopted, by reference or otherwise, into Alabama law, such computations shall be applied in the manner provided in the pertinent federal laws and regulations, but shall be applied to the amounts determined under Alabama law.

(3) For example, §40-18-15(10), Code of Alabama 1975, provides a deduction for contributions for corporations to the extent deductible for federal purposes under 26 U.S.C. §170. The federal provision limits the deduction to ten percent (10%) of taxable income. In computing the limitation for Alabama purposes, "taxable income" would be computed under Alabama law - not federal law.

(4) Adjustments to Federal Limitations. Alabama's income tax laws are tied to various federal income tax limitations. Certain fundamental differences in the calculation of federal taxable income and Alabama taxable income require that adjustments be made to the federal limitation before they can be used in the calculation of Alabama taxable income as described below.

(a) Federal limitations calculated at the corporate consolidated group level and used in the calculation of consolidated federal taxable income for the corporate group, must be adjusted to reflect the fact that Alabama corporate taxpayers, even those participating in the filing of a post 2001 Alabama consolidated return, must calculate Alabama taxable income on a separate-company basis. For this reason, federal limitations applicable in the calculation of Alabama corporate taxable income must be calculated on a separate-entity basis.

1. Example. Contributing Corporation C, a member of a federal affiliated group filing a consolidated federal corporate income tax return, contributes \$10 to the American Red Cross, which is a qualifying charitable contribution under IRC § 170(c) and is the group's only such charitable contribution that year. Contributing Corporation C has \$20 of separate company taxable income before the contribution deduction, but the group has \$200 of taxable income before the contribution deduction. Because the ten percent (10%) charitable contribution deduction limitation of IRC § 170(b)(2) is calculated at the group level for corporations filing federal consolidated returns, Contributing Corporation C's contribution deduction is not limited for federal purposes. However, because Alabama tax law requires separate company calculations, for purposes of calculating Contributing Corporation C's Alabama taxable income, only \$2

(\$20 x 10%) of the \$10 contribution is deductible. The remaining \$8 contribution may be carried forward under the federal carry-forward rules.

(b) Federal limitations are calculated without regard to allocation and apportionment, which are state income tax concepts that have no counterpart in the federal income tax system. Federal limitations must be adjusted to reflect the fact that Alabama multi-state taxpayers must calculate Alabama taxable income on a post-allocation and apportionment basis. For this reason, federal limitations applicable in the calculation of the Alabama taxable income of multi-state taxpayers must be calculated on a post-allocation and apportionment basis.

1. Example. Alabama's net operating loss (NOL) rules are tied to IRC § 382, a federal limitation to the utilization of NOLs. See Ala. Code § 40-18-35.1(6), (1975). When a loss corporation experiences an ownership change and the provisions of IRC § 382 apply, the Alabama apportionment factor of the loss corporation for the reporting period including the ownership change must be used to compute the IRC section 382 limitation applicable to Alabama multi-state taxpayers. For example, Loss Corporation L experiences an ownership change that triggers an IRC § 382 limitation. The annual federal limitation is \$10. For the reporting period including the ownership change Loss Corporation L's Alabama apportionment factor is twenty percent (20%). The federal limitation of \$10 must be apportioned to Alabama using Loss Corporation L's Alabama apportionment factor of 20%, creating an Alabama limitation of \$2.

Author: Joe Garrett, Commissioner's Office
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