

ALABAMA DEPARTMENT OF REVENUE
REVENUE RULING 97-007

This document may not be used or cited as precedent. Code of Alabama 1975, §40-2A-5(a).

TO:

SUBJECT: Income tax treatment and fling requirements applicable to revocable and irrevocable Trust established by nonresident grantors and testamentary trusts established through the probate of wills of nonresident decedents.

DATE: July 11, 1997

FACTS

Florida Bank will merge with and into Alabama Bank. Both Florida Bank and Alabama Bank are wholly owned subsidiaries of Holding Company, a regulated bank holding company. The merger will be effective under the Riegle-Neal Interstate Banking and Branching Efficiency Act and the enabling and legislature enacted by Florida and Alabama. Both Alabama Bank and Florida Bank have trust powers.

Florida Bank currently serves as trustee for a number of inter vivos revocable trusts, irrevocable trusts, and testamentary trusts (collectively the "Florida Trusts"). Alabama Bank will be the surviving entity from the merger and have its principal office in City, Alabama. As a result of the merger, Alabama Bank will become the legal entity serving as trustee with respect to the Florida Trusts.

Following the merger, Alabama Bank will continue to maintain trust offices and trust officers in Florida for the conduct of a trust business and its Florida based trust officers will continue to administer the Florida Trusts which will be assumed by operation of law from Florida Bank. While Alabama Bank will

continue to provide at its headquarters in Birmingham, Alabama, centralized data processing for all of its trust accounts, the books and records, including the trust agreements and related documents pertaining to the Florida Trusts, will continue to be

maintained in Florida trust offices. Florida base trust officers will be responsible for the administration of the Florida Trust.

For purposes of this ruling, we were informed by the requestor and we have assumed:

1. the Florida Trusts do not hold assets consisting of either Alabama real estate or Alabama business interests;

2. the Florida Trusts will not have revenues from property owned or business transacted in Alabama;

3. the Florida Trusts have not reported any Alabama source income and have never filed state of Alabama income tax returns;

4. the Florida Trusts have no Alabama beneficiaries as such term is defined in Code of Alabama 1975, §19-3-320(2);

5. all assets of the Florida Trusts to be managed and administered by Alabama Bank after the merger will be physically held and maintained outside of the state of Alabama;

6. the administration of the Florida Trusts will be accomplished through trust offices and trust officers in the state of Florida, with only ministerial functions performed by Alabama Bank from its offices located in Alabama;

7. none of the Florida Trusts are being administered pursuant to or under any Alabama court;

8. all trust investment decisions and discretionary functions of the Alabama Bank under the Florida Trusts will be made by trust officers in the state of Florida;

9. there is no Alabama receipt of income produced without the state of Alabama;

10. there is no Alabama source income to the Florida Trusts; and

11. the Florida Trusts were established by either grantors who were not residents of Alabama or through the probate of wills of decedents who were not residents of Alabama and administered pursuant to a court without the state of Alabama.

ISSUES

1. Whether the Florida Trusts are liable for state of Alabama income taxes following the merger.

2. Whether Alabama Bank, as trustee of the Florida Trusts, is required to file a state of Alabama fiduciary tax return on behalf of the Florida Trusts following the merger.

3. Whether any trust for which Alabama Bank is appointed trustee in the future and for which all of the assumptions stated above with respect to Florida Trusts are applicable, will be liable for state of Alabama income taxes and whether the trustee will be required to file a state of Alabama fiduciary return for these trusts.

4. Whether any trust for which Alabama Bank is appointed trustee in the future where all of the assumptions stated above with respect to Florida Trust are applicable, except that administration of the trust will take place in a state other than Florida and Alabama, will be liable for state of Alabama income taxes and whether the trustee will be required to file a state of Alabama fiduciary return for these trusts.

LAW AND ANALYSIS

Code of Alabama 1975, §40-18-25 provides that the Alabama income tax applies to the income of any kind of property held in trust, including the following types of income:

1. Income received by the estate of a deceased person during the period of administration or settlement or settlements of the estate;

2. Income accumulated in trust for the benefit of unborn or unascertained persons with contingent interests;

3. Income held for future distribution under the terms of a will or trust; and

4. Income which is to be distributed to the beneficiaries periodically, whether or not at regular intervals, and the income collected by a guardian of an infant to be held or distributed as the court may direct.

In the first three subparts of the statute above, the taxes are imposed on the trust and paid by the fiduciary. In the fourth subpart of the statute, the gross income is included by the fiduciary on the fiduciary return but the trust is allowed a

deduction from income upon which tax is to be paid by the fiduciary. As to such income, the tax is not paid by the fiduciary, but is paid by the beneficiaries on their individual returns.

There are three situations when a trust is subject to Alabama income taxation that are addressed in this ruling. The first of these is where the trust is a resident trust. The second is where the trust is a nonresident but liable for taxes on income earned in Alabama. The third is where the trust has one or more Alabama resident beneficiaries.

A trust may be subject to Alabama income tax as either a resident or nonresident taxpayer. A "resident trust" is generally considered to be a trust either created by an Alabama resident or the estate of an Alabama resident. If the trust is a resident trust of the State of Alabama, all revenues, receipts and income of the trust is taxed to the trust by the state of Alabama with certain deductions and credits as allowed by law. Based on the assumptions above, the Florida Trusts are not resident trusts or resident estates.

A trust may also be subject to Alabama income tax if it is a nonresident. A trust is generally considered to be a "nonresident trust" or estate if it was created by a nonresident or is the estate of a nonresident. Based on the information and assumptions provided, the Florida Trusts are nonresidents. Alabama Department of Revenue Regulation 810-3-25-2(b) (explaining Code of Alabama 1975, §40-18-25(c) or (d)) provides as follows:

"In the case of a trust created by a nonresident or the estate of a nonresident, gross income of such trust or estate includes only amounts which would be included in the gross income of a nonresident individual as provided in Section 40-18-14(3)."

The effect of the above regulation is that a trust created by a nonresident is taxed in the same manner as a nonresident individual, regardless of the domicile of the trustee or the beneficiaries. The taxation of nonresidents is governed by Code of Alabama 1975, §40-18-2(6), which levies a tax on "[e]very nonresident individual receiving taxable income from property owned or business transacted in Alabama". Alabama Department of Revenue Regulation 810-3-14-.05 relates to the gross income of nonresidents and provides as follows:

"810-3-14-.05. Gross Income of Nonresidents.

. . . .
(2) (a) Gross income of a nonresident includes income from real and/or tangible personal property located within Alabama, or intangible personal property with a business situs in Alabama.

(b) The income from property may be derived from the operation of the property, from rents or royalties for its use, or from the sale, exchange or other disposition of the property.

1. For real property located within Alabama, gross income includes gains or losses from the sale, exchange or disposition of such property. See Chapters 6 and 8 of these regulations for computation of gains and losses to be recognized.

2. For tangible personal property located within Alabama, gross income includes gains from the sale, exchange or disposition of such property. Losses are included in gross income from the sale, exchange or disposition of such property only if such property was "business income" producing property (as defined in Reg. 810-3-31-.02).

3. For intangible personal property which has a business situs in Alabama, gross income includes gains from the sale, exchange or disposition of such property. Losses are included in gross income from the sale, exchange or disposition of such property only if such property was "business income" producing property (as defined in Reg. 810-3-31-.02).

4. As a general rule, for the purpose of determining the source of income attributable to the sale of personal property, a sale is consummated at the place where the seller surrenders all his right, title, and interest to the buyer. Where bare legal title is retained by the seller, the sale will be deemed to have occurred at the time and place of passage to the buyer of beneficial ownership and risk of loss.

(3) (a) Gross income includes the deemed distributive share of separately stated and nonseparately stated income (or loss not to exceed basis) for shareholders of an electing Alabama S corporation.

1. For electing Alabama S corporations with income from more than one state, gross income includes only the deemed distributive share attributable to Alabama.

(b) Gross income does not include actual distributions from electing Alabama S corporations which have been previously included in gross income under subparagraph (3)(a) above.

(c) Gross income of a nonresident does not include actual distributions from S corporations which have not elected to be Alabama S corporations, nor does it include deemed distributive shares of income (or losses) of such corporations.

(d) See §§40-18-160, et seq., Code of Alabama 1975, and regulations thereunder, relating to Alabama S corporations.

(4) Gross income of a nonresident partner of a partnership includes the distributive share of the partnership income (or loss not to exceed basis), plus any "Guaranteed Payments to Partner". See Regs. 810-3-24-.01(3) and 810-3-24-.03. If the partnership has income from Alabama and any other state, Alabama gross income includes only the amount attributed to Alabama as provided in Reg. 810-3-24-.02(2).

(5) Gross income of a nonresident beneficiary of an estate or trust includes income from such estate or trust attributable to Alabama. See Reg. 810-3-25-.05.

Because all trust income, functions, decisions and operations of the Florida Trusts are unconnected with Alabama, the Florida Trusts are not subject to income taxation by Alabama as a nonresident under the regulation set forth above.

The third possibility for the Florida Trusts to be subject to taxation in Alabama would be met if one or more of the beneficiaries are residents of Alabama. In such a case, the Florida Trusts would not primarily be liable for the taxes, but would be required to file the fiduciary return for the trust in Alabama to report the liability of the Alabama resident beneficiary. We have assumed there are no Alabama beneficiaries.

Alabama law imposes filing requirements independent of tax liability. Code of Alabama 1975, §40-18-29 provides as follows:

"(a) Every fiduciary, ..., shall make a return for the taxpayer for whom he acts, ...which return shall state specifically the items to the gross income and the deductions, exemptions and credits allowed by this chapter ..."

Taken literally, this would impose a filing requirement on every fiduciary in the world, even those having absolutely no contacts with Alabama. Obviously, such an interpretation would be overbroad. Instead, the Department may require the filing of a fiduciary return if either the trust or the beneficiary is "subject to" the Alabama income tax even where there is no ultimate liability to the filing entity. Alabama Department of

Revenue Regulation 810-3-2-.03 addresses estates, trusts and fiduciaries subject to income taxation as follows:

"810-3-2-.03. Estates, Trusts and Fiduciaries Subject to Alabama Income Tax.

(1) Every individual or corporation acting in a fiduciary capacity, receiving income from sources within the State of Alabama, is subject to the Alabama income tax with respect to such income. For definitions of resident individuals and resident corporations, see Regs. 810-3-2-.01 and 810-3-2-.02.

(2) An estate or trust resident in the State of Alabama, or having a resident fiduciary, is subject to the Alabama income tax. An estate or trust having income from sources within the State is subject to tax on such income. For a discussion of the situs of income, see Reg. 810-3-14-.05(2). For specific rules with respect to estates, trusts and fiduciaries, see §§40-18-25 and 40-18-29, Code of Alabama 1975.

Part (1) of this regulation requires all resident fiduciaries to file an income tax return for the fiduciaries' corporate or individual income. Part (2) of the regulation applies to the filing of fiduciary income tax returns for the trust or estate. Part (2) would appear to require the filing of a fiduciary return whenever the fiduciary is a resident of Alabama, even when neither the trust or the beneficiaries are subject to Alabama income tax. Clearly this is outside the taxing jurisdiction of Alabama. Instead the "resident fiduciary" language should be interpreted to require the filing of the fiduciary return by all fiduciaries whenever there is a "resident beneficiary".

Because Alabama is without jurisdiction to require the filing of a fiduciary return when the trust (i)is not a resident in the state of Alabama; (ii)has no business situs or income from sources within the state; and (iii) has no resident beneficiaries, the trustee of the Florida Trusts will not have to file fiduciary returns for those trusts and estates in Alabama. However, should some of the assumptions stated above change as to any particular Florida Trust, the trustee may be required to file an Alabama fiduciary return.

RULINGS

1. Based on the assumptions stated above, the Florida Trusts are not resident trusts or estates of Alabama, have no Alabama business situs or income from sources within the state, and have no Alabama beneficiaries. Therefore, the Florida Trusts will not

be liable for state of Alabama income taxes following the merger.

2. Based on the assumptions stated above, the Florida Trusts are not resident trusts or estates of Alabama, have no Alabama business situs or income from sources within the state and have no Alabama beneficiaries. Therefore, Alabama Bank, as trustee of the Florida Trusts, is not required to file state of Alabama fiduciary tax returns on behalf of the Florida Trusts following the merger.

3. Unless the Department of Revenue changes its interpretation of the law or regulations and so long as the assumptions stated above with respect to Florida Trusts remain applicable to future trusts and estates naming Alabama Bank as trustee, Alabama Bank will not be liable for state of Alabama income taxes on the trusts and estates and the trustee will not be required to file a state of Alabama fiduciary return for these trusts.

4. Unless the Department of Revenue changes its interpretation of the law or regulations and so long as the assumptions stated above with respect to Florida Trusts remain applicable to any trust for which Alabama Bank is appointed trustee in the future, except that administration of the trust will take place in a state other than Florida and Alabama, Alabama Bank will not be liable for state of Alabama income taxes and Alabama Bank will not be required to file a state of Alabama fiduciary return for these trusts or estates.

The Commissioner of Revenue has recused himself from issuing this revenue ruling. In accordance with Code of Alabama 1975, §40-2-44, the Commissioner has assigned the Assistant Commissioner of Revenue the duty of issuing this ruling.

ALABAMA DEPARTMENT OF REVENUE

By: _____
GEORGE E. MINGLEDORFF, III
Assistant Commissioner of Revenue

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