ALABAMA DEPARTMENT OF REVENUE
ADMINISTRATIVE CODE

CHAPTER 810-3-14
GROSS INCOME OF INDIVIDUALS

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810-3-14-.01 Gross Income In General.

(1) The term "gross income" means all wealth flowing to the taxpayer from whatever source derived other than as a return of his capital and other than those items exempted by Section 40-18-14(3), Code of Ala. 1975. Gross income includes income realized in any form, whether in money, property, or services. Income may be realized in the form of services, meals, accommodations, stock, or other property, as well as in cash. Such income is to be reported for the year in which received, or accrued and reported in accordance with accepted accounting procedures applicable to the taxpayer's particular type of business. See Reg. 810-3-13-.03 for discussion of accounting methods.

(2) In the case of a manufacturing, merchandising, or mining business, gross income means the total sales less the cost of goods sold, plus any income from investments and from incidental or outside operations or sources. In determining the gross income

of a business, subtraction should not be made for losses, or for items not ordinarily used in computing the cost of goods sold.

(3) Earnings constitute gross income before deductions for withholding for federal income tax, social security tax, insurance and retirement programs (including those allowable as a deduction under Code of Ala. 1975, Section 40-18-15(11)) or other voluntary or involuntary withholdings.

(4) Income actually received or accrued must be included in gross income, although losses may later incur against this income. An exception to this general rule occurs in situations involving the renegotiation of war contracts under federal statutes. Where repayment is made to the government as a result of renegotiation, the amount of income for the year of original payment is the amount of such payment less the amount refunded to the government, even though the repayment is made to the government in a later year. As long as the matter of renegotiation is open, the extent of the gain or profit of the contractor, if any, for that year of payment remains undetermined.

(5) If services are paid for with something other than money, the fair market value of the property or services taken in payment is the amount to be included as gross income. If living quarters or meals are furnished to employees for the convenience of the employer, the ratable value need not be added to the compensation of the employees, but if a person receives a compensation for service rendered compensation in the form of living quarters or meals, the value to such person of the quarters furnished constitutes income subject to tax. For living quarters furnished to ministers, see Reg. 810-3-14.02(1)(g).

(6)(a) An employee who is given an annuity by his employer must pay income tax on the amount of the premium in the year in which the premium is paid. The annuity is considered as additional compensation for services rendered and not as a gratuity. The payments that qualify as a deduction under Code of Ala. 1975, §40-18-15(11) shall be included in gross income.

(b) An employee who is the insured or owner of a group life insurance policy with a face value in excess of $50,000, and the premiums on such policy are paid by the employer, must include in gross income the value of such premiums for coverage in excess of $50,000.

(7) For procedure in reporting the income of minors, see §40-18-27 and regulations thereunder.

(8) The Federal Internal Revenue Code contains provisions similar to those of §40-18-14(1). Decisions and interpretations of the federal courts and agencies will be given due weight in interpreting this section.

(9) Gross income includes recovery of items deducted in previous years. See Reg. 810-3-14-.04.

(10) For tax years beginning after December 31, 1981, gross income includes alimony and separate maintenance according to I.R.C. §71 in effect January 1, 1982. For tax years beginning after December 31, 1984, gross income includes alimony and separate maintenance payments as defined in I.R.C. §71, as in effect on January 1, 1985. For tax years beginning after December 31, 1989, gross income includes alimony and separate maintenance payments as defined in I.R.C. §71, as in effect from time to time. Decisions and interpretations of the federal courts and agencies interpreting I.R.C. §71 will be given due weight in interpreting Code of Ala. 1975, Section 40-18-14(1) and this regulation as it relates to alimony and separate maintenance payments. Regulations pertaining to I.R.C. §71 are hereby made a part of this regulation.

(a) Alimony or separate maintenance payments received under a divorce or separation instrument executed after March 1, 1954, but prior to January 1, 1985, will be included in gross income as follows:

1.(i) Periodic payments, (for definition of periodic payments see section 2. below) whether or not received at regular intervals, received after January 1, 1982 are includible in gross income if -

(I) Payments received are in discharge of (or attributable to property transferred, in trust or otherwise, in discharge of) a legal obligation, and

(II) the obligation is imposed on or incurred because of a marital or family relationship, and

(III) the legal obligation is under the decree, or written agreement incident to divorce or separation, and

(IV) the payment received does not represent payment in support of minor children, and

(V) the payment received does not represent a settlement of property rights.

(ii) The source of the payments is immaterial. The payments may be from property held in trust, life insurance, endowment or annuity contract, any other interest in property or from income or capital of the payor whether paid directly or indirectly by him.

(iii) If the decree or written agreement specifies an amount to be paid in support of minor children, the payment received goes first to satisfy this obligation. If the payment is less than the amount specified as support of minor children, then the payment received shall be considered a payment of support of minor children.

(I) If the decree or written agreement specifies one amount as payment of both alimony or separate maintenance and child support, the entire amount will be considered as alimony or separate maintenance and will be included in gross income of the recipient.

2. In general, periodic payment means "payable over a period of indefinite duration". Payments made for an unspecified principal amount are considered periodic payments even if, by provision of the decree or written agreement or local law, payments will be terminated by death of either spouse, remarriage, or change in economic status of either spouse.

3. Payment of a specified amount, in terms of money or property, under the decree or written agreement to be made over a period of 10 years or less from the date of the decree or agreement will be considered periodic payments if -

(i) payments are subject to one or more of the contingencies of death, remarriage, or change in the economic status of either spouse, and

(ii) payments are in the nature of alimony or an allowance for support.

4. If payment of a specified amount, in terms of money or property, under the decree or written agreement, is to be made over a period of more than 10 years from the date of the decree or agreement, payments will be considered periodic payments but only to the extent that the installment payment, or sum of the installment payment, received during the recipient's taxable year does not exceed 10 percent of the principal sum. This 10 percent limitation applies to installment payments made in advance, but does not apply to delinquent installment payments for a prior taxable year of the recipient made during the current taxable year.

5. A transfer of property in settlement of marital rights may result in a recognizable gain or loss. The gain or loss is the difference between the adjusted basis of the

property and its fair market value at the time of the transfer.

(i) If the property has appreciated, there may be a taxable gain on the transfer. Property has appreciated if its fair market value is more than its adjusted basis. The difference is a gain.

(ii) If the fair market value is less than the adjusted basis, a loss is realized. Such a loss is deductible if it is on business or investment property, but is not deductible if it is on property held for personal use.

(iii) An equal division of property that is co-owned by husband and wife does not result in a gain or loss.

(iv) If husband and wife each keep their separately owned property in a divorce settlement, there is no taxable gain or loss.

(v) If one spouse transfers separately owned property to the other spouse, the spouse transferring the property realizes a gain or loss. The spouse receiving the property has no gain or loss on the transaction. The basis of the property to the receiving spouse is its fair market value on the date of the transfer.

(vi) Taxpayers report the gain or loss in a property settlement the same as any sale or exchange of an asset.

(b) Alimony or separate maintenance payments received from divorce or separation instruments executed after December 31, 1984, (and to divorce or separation agreements executed prior to January 1, 1985, if modified to expressly provide for the application of this subparagraph) is includible in gross income as follows:

1. the term "alimony or separate maintenance payment" means any payment in cash, if -

(i) such payment is received by (or on behalf of) a spouse under divorce or separation instrument, and

(ii) the divorce or separation instrument does not designate such payment as a payment which is not includible in gross income under §40-18-14 and not allowable as a deduction under §40-18-15, and

(iii) in the case of an individual legally separated from his spouse under a separate maintenance instrument or decree of divorce, the payee and payors are not members of the same household at time such payment is made and do not file a joint income tax return, and

(iv) there is no liability to make any such payment for any period after the death of the payee spouse and there is no liability to make any payment (in cash or other property) as a substitute for such payments after the death of the payee spouse.

2. The term "divorce or separation instrument" means:

(i) a decree of divorce or separate maintenance or a written instrument incident to such a divorce, or

(ii) a written separation agreement, or

(iii) a decree (not described in subsection (I) above) requiring a spouse to make payments for the support of the other spouse, such as temporary alimony.

3. The term "alimony or separate maintenance" shall not apply to that part of any payment which the terms of the divorce or separation instrument designates (in terms of an amount of money or a part of a payment) as a sum which is payable for the support of children of the payor. If any amount specified in the instrument will be reduced -

(i)(I) on the happening of a contingency specified in the instrument relating to a child (such as attaining a specified age, marrying, dying, leaving school, or a similar contingency), or

(II) At a time which can be clearly associated with a contingency of a kind specified in (I); an amount equal to the amount of such reduction will be treated as an amount designated or fixed as payable for the support of children of the payor.

(ii)(I) If any payment is less than the amount specified in the instrument as support of the children of the payor, then so much as such payment as does not exceed the sum payable for support shall be considered a payment for such support.

(II) If the instrument specifies a single amount in payment of both alimony or separate maintenance and child support with no more contingency of the type provided in sections

3. (I)(I) or (II) above, or no support of money or part of the payment specifically designated as child support, the entire payment will be considered as alimony or separate maintenance and will be included in gross income of the recipient.

4. Alimony or separate maintenance payments in excess of $10,000 during any calendar year paid to a single payee will not be treated as alimony or separate maintenance unless such payments are to be made by the payor to the payee in each of the six (6) post-separation years (not taking into account any termination contingent on the death of or remarriage of either spouse).

5. If there is an excess amount determined under section 6. below for any computation year - (i) the payor spouse shall include such excess in gross income for the taxable year beginning in the computation year, and (ii) the payee spouse shall be allowed a deduction in computing adjusted gross income for such excess amount for the taxable year which ends on or after the taxable year of the payor spouse beginning in the computation year.

6.(i) The excess amount determined under this section for any computation year is the sum of -

(I) the excess (if any) of - I. the amount of alimony or separate maintenance payments paid by the payor spouse during the immediately preceding post-separation year, over II. the amount of alimony or separate maintenance payments paid by the payor spouse during the computation year increased by $10,000, plus

(II) a like excess for each of the other post-separation years.

(ii) In determining the amount of alimony or separate maintenance payments made by the payor spouse during any preceding post-separation year, the amount paid during such year shall be reduced by any excess previously determined in respect of such year under this section 6.

(I) EXAMPLE: H makes alimony payments to W of $25,000 in 1985 and $12,000 in 1986. The excess amount with respect to 1985 that is recaptured in 1986 is $3,000 ($25,000 - ($12,000 + $10,000)). For purposes of subsequent computation years, the amount deemed paid in 1985 is $22,000. If H makes alimony payments to W of $1,000 in 1987, the excess amount that is recaptured in 1987 will be $12,000. This is the sum of an $11,000 excess

amount for 1985 ($22,000 - $1,000 + $10,000)) and a $1,000 excess amount with respect to 1986 ($12,000 - ($1,000 + $10,000)). If, prior to the end of 1990 (the end of the six year post-separation period), payments decline further, additional recapture will occur.

7. For purposes of this subparagraph, the term "post-separation year" means any calendar year in the six (6) calendar year period beginning with the first calendar year in which the payor spouse paid alimony or separate maintenance payments to the recipient spouse, and the term "computation year" means the post-separation year for which the excess under section 6. above is being determined.

8. The recapture rule provided in section 5. above shall not apply to any post-separation year (and subsequent post-separation years).

(i) either spouse dies or the payee spouse before the close of such post-separation year, and

(ii) the alimony or separation maintenance payments cease by reason of such death or remarriage, or

(iii) the payments are received under a decree described in section 2. (iii) above, or (iv) the payment is made pursuant to a continuing liability (over a period not less than six years) to pay a fixed portion of the income from a business or property or from compensation or employment or self-employment.

9. To qualify for the deduction provided in §40-18-15, alimony or separate maintenance payments may not be made in any form other than cash. Transfers of services or property (including a debt instrument of a third party or any annuity contract), executing of a debt instrument by the payor, or the use of property of the payor, do not qualify as alimony or separate maintenance payment. See §§40-18-8(m) and 40-18-6(a)(13) for treatment of gain or loss on transfers of property incident to a divorce.

(c) Alimony or separate maintenance payments received from divorce or separation instruments executed after December 31, 1989 (and to divorce or separation agreements executed prior to January 1, 1990, if modified to expressly provide for the application of this subparagraph (is includible in gross income in the same manner as provided in subparagraph (b) of this regulation with the following exceptions;

1. the payments must be cash payments received by (or on behalf of) a spouse or former spouse:

2. the payments must be under a divorce or separation instrument;

3. the payments must not extend after the death of a payee-spouse (need not be expressly stated in the instrument);

4. the spouses (or former spouses) must not be members of the same household and must not file joint returns;

5. the divorce or separation instrument can designate such payment which is not includible in gross income under I.R.C. §71 and not allowable as a deduction under I.R.C. §215 (if so designated, the payments are not considered as alimony):

6. the payment must not be for child support; and

7. the payments need not be made in discharge of marital obligations imposed by state law, nor need the payments be "periodic."

(11) Except for plans specifically exempt by law from tax, payments received from pension, profit-sharing, stock bonus, retirement, annuity, or bond purchase plans, in excess of the taxpayer's investment in such plans, shall be included in gross income.

(a) This includes all payments received, not just those received upon completion of the plan.

(b) The taxpayer's investment in the above plans is the taxpayer's contributions to such plans, excluding those allowable as a deduction under §§40-18-15(a)(11) and 40-18-15(a)(12) and/or those allowable as an exclusion from gross income under §40-18-14(1)(I). See also Reg. 810-3-14-.10.

(c) Those employer contributions previously included in gross income of the taxpayer but not allowable as a deduction by the taxpayer are included in the taxpayer's investment.

(12)(a) For tax years beginning after December 31, 1981, but before January 1, 1990, in accordance with §40-18-14(2)e (I.R.C. §105 as in effect January 1, 1982), any amount an employee receives for disability through an accident and health insurance plan that is attributable to his employer's contributions is included in gross income except:

1. Payments for permanent loss of, or loss of use of a member or function of the body, or for permanent disfigurement,

2. Payments under a plan as reimbursement for expenses incurred by the employee for medical care for himself, spouse or dependents, or

3. Payments, within limits that are in lieu of wages for a period during which an employee is absent from work on account of permanent and total disability if the employee has not attained age 65 before the close of the taxable year and has retired on disability.

(i) The disability income exclusion of this paragraph (c) is limited to $100 per week, and

(ii) The disability exclusion to which the taxpayer would be entitled shall be reduced by the amount that adjusted gross income, including disability income, exceeds $15,000.00.

(iii) EXAMPLE: A disabled taxpayer under age 65 received $6,000.00 in disability retirement income in lieu of wages. He also had $10,000.00 of other income which, together with the $6,000.00 of disability payments in lieu of wages, gave him an adjusted gross income of $16,000.00. Assume that before reduction the taxpayer is entitled to an exclusion of $5,200.00 for the year. Since the taxpayer's adjusted gross income exceeds $15,000.00, his exclusion is reduced by the $1,000.00 excess. Consequently, his maximum exclusion is $4,200.00 ($5,200.00 minus $1,000.00).

(b) The exclusion provision of paragraph (a) above does not apply to disability income received after December 31, 1989.

(13) Gross income includes the fair market value of the personal use (including commuting) of an employer (including a governmental employer) owned automobile, together with the fair market value of any fuel furnished by the employer. The rates and methods for determining the values for this paragraph will be as provided in I.R.C. §61(a)(1) (and I.R.C. Reg. 1-61-2T) as in effect January 1, 1985.

(14)(a) For taxpayers who are shareholders of an Alabama S corporation with a tax year which began before January 1, 1990 -

1. Gross income includes the deemed distributive share of separately stated and nonseparately stated income (or loss) for shareholders of an electing Alabama S corporation.

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

2.(i) Gross income does not include actual distributions from electing Alabama S corporations which have been previously included in gross income under subparagraph (a)1. above.

(ii) For resident shareholders, all other actual distributions from a S corporation, including distributions representing income taxable in other states, is included in gross income.

3. Gross income does include actual distributions from S corporations which have not elected to be Alabama S corporations, but does not include deemed distributive shares of income (or losses) of such corporations.

4. See §§40-18-160, et seq., and regulations thereunder, relating to Alabama S corporations.

(b) For taxpayers who are shareholders of an Alabama S corporation with a tax year which began after December 31, 1989 and before January 1, 1997 -

1. Gross income includes the deemed distributive share of separately stated and nonseparately stated income (or loss) of the Alabama S corporation.

2. Gross income does not include actual distributions from an Alabama S corporation which have been previously included in gross income under subparagraph (a)1. above.

(c) For taxpayers who are shareholders of an Alabama S corporation with a tax year which began after December 31, 1996 and before January 1, 2011:

1. Gross income includes the shareholder's pro rata share of separately stated and nonseparately stated items of income, loss, deduction, or credit attributed to Alabama by the Alabama S corporation for the corporation's taxable year which ends with or during the individual's tax year.

2. Gross income does not include actual distributions from an Alabama S corporation which have been previously included in gross income under subparagraph (a)1. above.

3. Gross income does not include actual distributions from an Alabama S corporation which are determined to be

nontaxable under the provisions of §40-18-165 and the regulations thereunder.

(d) For taxpayers who are shareholders of an Alabama S corporation with a tax year which began after December 31, 2010 gross income is determined in accordance with Code of Ala. 1975, §§40-18-162 and 40-18-14 and without regard to (c)above.

(15)(a) For taxpayers providing foster care services who are not engaged in the trade or business of providing such services, gross income includes payments received in excess of expenses incurred in providing such services but does not include expenses in excess of receipts.

(b) For taxpayers engaged in the trade or business of providing foster care services, gross income includes all payments received for such services, less expenses incurred in the performance of such services. A taxpayer will be presumed to be engaged in the trade or business of providing foster care services when such services are provided for more than ten (10) minors or more than five (5) adults.

(c) The provisions of this paragraph are substantially similar to the provisions of I.R.C. §131, and regulations and decisions regarding the interpretation and implementation of I.R.C. §131 will be given due consideration in the administration of this paragraph.

(16)(a) For tax years beginning after December 31, 1996 and before January 1, 2011, gross income for a resident partner or member of a subchapter K entity includes the following:

1. For a multi-state subchapter K entity doing business within and without the State of Alabama, only that income which is required to be allocated and apportioned to Alabama under the rules of Section 40-18-22. (If the multi-state subchapter K entity is not doing business in Alabama, no income is reportable to Alabama from that subchapter K entity.)

2. For a subchapter K entity doing business in only one state, whether the State of Alabama or another state, the distributive share of the entire income from that subchapter K entity.

(b) For tax years beginning after December 31, 2010, the amount of income, deduction, gain, loss or credit includable or deductible by an owner of an interest in a subchapter K entity shall be determined in accordance with subchapter K of the Internal Revenue Code, 26 U.S.C. §§701-761, Code of Ala. 1975, §§40-18-24 and 40-18-14 and without regard to (a) above.

(17) Property transferred in connection with performance of service-Tax years beginning after December 31, 9891.

(a) Inclusion in gross income.

1. If stock or other property is transferred to any person other than the person for whom the services are performed, the excess of -

(i) the fair market value of such property (determined without restrictions other than restrictions that will never lapse) at the first time the rights of the person having beneficial interest in such property are transferable or are not subject to substantial risk of forfeiture, whichever occurs first, over

(ii) the amount actually paid for such property, shall be included in the gross income of the transferee who performed the service in the first tax year during which a fair market value under provisions of (a)(I) above can be determined.

2. Paragraph (a)1 shall not apply if the transferee sells or otherwise disposes of such property in an arms length transaction before his rights in such property become transferable or not subject to substantial risk of forfeiture.

(b) Election to include in gross income in the year of transfer.

1. The transferee may elect to have paragraph (a) above apply in the year of transfer.

2. The election must be made in the same manner and within the same time frame as required by regulations pertaining to 26 U.S.C. §83.

3. The statement of election required by regulations pertaining to 26 U.S.C. §83 shall be made a part of the Alabama income tax return for the year of transfer.

(c) Special rules - For the purpose of this regulation -

1. Substantial risk of forfeiture. - The rights of a person in property are subject to a substantial risk of forfeiture if such person's rights to full enjoyment of such property are conditioned upon the future performance of substantial services by the individual.

2. Transferability of property - The rights of a person in property are transferable only if the rights in such

property of the transferee are not subject to substantial risk of forfeiture.

3. Sales which give rise to suit under section 16(b) of the Securities Exchange Act of 1983. - So long as the sale of property at a profit could subject a person to suit under section 16(b) of the Securities Exchange Act of 1934, such person's rights in such property are -

(i) subject to substantial risk of forfeiture, and

(ii) not transferable.

(d) Restrictions which will never lapse.

1. Valuation - Property subject to restrictions which by its terms will never lapse, and which allows the transferee to see such property for a price determined under some formula, the formula price shall be determined to be the fair market value of the property.

2. Cancellation - If, property subject to a restriction which by its terms will never lapse has the restriction canceled, then unless the transferee establishes -

(i) that such cancellation was not compensatory, and

(ii) that the taxpayer, if any, who would be allowed a deduction for compensation, will treat the transaction as non-compensation:

(I) the excess of the fair market value of the property (computed without regard to the restrictions) at the time of the cancellation over the fair market value of the property (computed by taking the restriction into account) immediately before the cancellation plus the amount paid for the cancellation, shall be treated as compensation for the tax year in which the cancellation occurs.

(e) Applicability, - This regulation shall not apply to -

1. a stock option to which 26 U.S.C. §421 applies.

2. a transfer to or from a trust described in 26 U.S.C. §401(a) or a transfer under an annuity plan which meets the requirements of 26 U.S.C. §404(a)(2).

3. the transfer of an option without a readily ascertainable fair market value.

4. the transfer of property upon the exercise of an option with a readily ascertainable market value at the date of the grant, or

5. group term life insurance to which 26 U.S.C. §79 applies.

(f) Code of Ala. 1975, §40-18-14(1) stipulates that 26 U.S.C. §83 will be the guiding document for determining amount and time that income under this regulation is to be included in gross income; therefore, regulations pertaining to 26 U.S.C. §83 are hereby made a part of this regulation. Judicial and administrative decision of Federal agencies will govern in administering this regulation.

(18) With the exception noted below, the amendments to this regulation which were filed with the Legislative Reference Service on March 21, 2011 are effective for tax years beginning after December 31, 2010. The Department of Revenue will not enforce these regulatory changes for tax periods ending prior to January 1, 2011, or for gains associated with the taxable disposition of all or any portion of a taxpayer's assets or Subchapter K interests where the parties to the transaction can document that negotiations began prior to January 1, 2011 and continued with regularity until the transaction was completed in 2011. These amendments are consistent with the Administrative Law Division's Ruling, McNees v. Department of Revenue, DOCKET NO. 06-523, entered December 12, 2006.

(19) The Department will not rely on the amendments to this regulation which were filed with the Legislative Reference Service on March 21, 2011 for tax periods beginning after December 31, 2011. For tax periods beginning after December 31, 2011, the Department will issue new regulatory language addressing the issues to which these amendments pertain.

Author: Ann Winborne, CPA, Individual and Corporate Tax Division, Joe Garrett, Tax Policy Administrator

Statutory Authority: Code of Ala. 1975, §§40-2A-7(a)(5), 40-18-1.1(c), 40-18-14.

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810-3-14-.02 Exclusions From Gross Income.

(1) Items which are excluded from gross income are listed in §40-18-14(3), Code of Ala. 1975, as follows:

(a) Amounts received under life insurance policies and contracts paid by reason of the death of the insured, in accordance with 26 U.S.C. §101.

(b) Amounts received, other than amounts paid by reason of the death of the insured, under life insurance, endowment or annuity contracts determined in accordance with 26 U.S.C. §72.

(c) The value of property acquired by gift, bequest, devise, or descent, in accordance with 26 U.S.C. §102 - the income from such property shall be included in gross income.

1. Gross income does not include a fellowship or grant that is an outright gift with no obligation on the part of the recipient. Payments to an individual as a scholarship at an educational institution or as a fellowship grant are excluded from the gross income of the student to the extent that services are not required of the student in order to receive the payments. The value of contributed services and accommodations are also excluded from gross income. If there is a condition that a person must teach or enter into employment, payments are not gifts.

2. Payments for teaching, research, or other services in the nature of part-time employment required as a condition to receiving the scholarship or fellowship grant are not exempt and should be included in gross income.

3. Prizes, awards, and scholarships are not specifically addressed by Alabama income tax law. The Department will look to 26 U.S.C. §74, Prizes and Awards, and 26 U.S.C. §117, Qualified Scholarships, as guidance to determine whether specific prizes, awards, and scholarships are excluded from gross income.

(d) Interest upon obligations of the United States or its possessions; or securities issued under provisions of the Federal Farm Loan Act of July 18, 1916. Examples of exempt obligations include U.S. Savings Bonds, U.S. Treasury Notes or Bills, obligations of the Bank for Cooperatives, Federal Land Banks, Federal Intermediate Credit Banks, Federal Home Loan Banks, Productions Credit Associations, Federal Financing Bank, and the Tennessee Valley Authority. Interest received from the United States government earned on other than investment obligations, such as interest on tax refunds, is subject to Alabama income tax and should be included in gross income.

(e) Amounts received which are excludable from gross income under 26 U.S.C. §104, relating to compensation for injuries or sickness.

(f) Amounts received which are excludable from gross income under 26 U.S.C. §105, relating to amounts received from accident or health plans.

(g) Interest on obligations of the State of Alabama and any county, municipality, or other political subdivision thereof. It should be noted that interest on obligations of other states and political subdivisions thereof is taxable.

(h) The rental value of a parsonage provided to a minister of the gospel, to the extent excludable under 26 U.S.C. §107.

(i) Income from discharge of indebtedness to the extent allowed by 26 U.S.C. §108, with the exception that the reductions in tax attributes required by 26 U.S.C. §108 shall be applied only to the net operating losses determined under Alabama income tax law and to the basis of depreciable property. The basis reductions of depreciable property shall not exceed the basis reductions for federal income tax purposes. All other tax attribute reductions required by 26 U.S.C. §108 shall not be recognized.

(j) Gain from the sale of a personal residence to the extent excludable for federal income tax purposes under 26 U.S.C. §121.

(k) Contributions made by an employer on behalf of an employee to a trust which is a part of a qualified cash or deferred arrangement, as defined in 26 U.S.C. §401(k)(2) or 5 U.S.C. §8437, subject to the limitations of 26 U.S.C. §402(g).

(l) Contributions, made by an employer for an employee for an annuity contract, which would be excludable from the gross income of the employee, in accordance with 26 U.S.C. §403(b), subject to the limitations of 26 U.S.C. §402(g).

(m) Amounts excludable in accordance with 26 U.S.C. §125, relating to cafeteria plans.

(n) Amounts excludable in accordance with 26 U.S.C. §132, relating to certain fringe benefits.

(o) Amounts excludable in accordance with 26 U.S.C. §129, relating to dependent care expenses.

(2) In addition, items of income which federal law prohibits the states from taxing, or which are otherwise exempt from taxation by the Code of Ala. 1975, are excluded from gross income. For example, the daily subsistence allowance paid to state law enforcement officers pursuant to §36-21-2, Code of Ala. 1975, is excluded from gross income. Also, federal law exempts from taxation allowances for quarters, subsistence, uniforms and travel furnished military personnel by the United States Government.

(3) Other items of income are exempt:

(a) Income of foreign missionaries - see §40-18-2.1, Code of Ala. 1975.

(b) Certain retirement allowances, net income realized from a financial business, personal exemptions and dependent exemptions - see §40-18-19.

(c) Certain severance payments - see §40-18-19.1.

(d) Military retirement benefits - see §40-18-20.

(4) For interpretation of federal statutes adopted by the Alabama legislature, see Rule 810-3-1.1-.01, Operating Rules.

(5) The provisions of the federal "Taxpayer Relief Act of 1997" which were adopted by Alabama Act 98-502 have the same effective date for Alabama income tax purposes as they do for federal income tax purposes.

Author: Ann F. Winborne, CPA, Ed Cutter, CPA, John Danziger, and Rebecca S. Whisenant

Statutory Authority: Code of Ala. 1975, §§40-2A-7(a)(5), 40-18-14.

History: **Amended:** June 17, 1988; February 8, 1989; filed March 20, 1989. **Amended:** Filed July 27, 1988; May 15, 1992. **Repealed and New Rule:** Filed May 3, 2000; effective June 7, 2000.

810-3-14-.03 Gross Income Of Farmers.

(1) A taxpayer is engaged in the business of farming if he cultivates, operates, or manages a farm for gain or profit, either as owner or tenant. A taxpayer who receives a rental (either in cash or in kind) which is based upon farm production is engaged in the business of farming. However, a taxpayer who receives a fixed rental (without reference to production) is engaged in the business of farming only if he participates to a material extent in the operation or management of the farm. A taxpayer engaged in forestry or the growing of timber is not thereby engaged in the business of farming. A person cultivating or operating a farm for recreation or pleasure rather than a profit is not engaged in the business of farming. For the purpose of this rule, the term "farm" is used in its ordinary, accepted sense and includes stock, dairy, poultry, fish, fruit, and truck farms, and also plantations, ranches, ranges, and orchards.

(2) A farmer shall make a return using the same taxable year and in accordance with the same method of accounting that the farmer uses for federal income tax purposes, as provided for under §40-18-13, Code of Ala. 1975.

(3) Crop shares shall be included in gross income as of the year in which the crop shares are reduced to money or the equivalent of money.

(4) If farm produce is exchanged for merchandise, groceries, or the like, the market value of the articles received in exchange is to be included in gross income.

(5) Proceeds of insurance, such as hail and fire insurance on growing crops, should be included in gross income, whether received in cash or its equivalent for the crop injured or destroyed.

(6) Inventory shall be taken by a farmer in accordance with the methods and procedures prescribed under §40-18-11.
Author: Ann F. Winborne, CPA, John Danziger, Rebecca Whisenant
Statutory Authority: Code of Ala. 1975, §§40-2A-7(a)(5), 40-18-14.
History: **Amended:** June 17, 1988; filed July 27, 1988. **Amended:** Filed September 18, 1996; effective October 23, 1996. **Amended:** Filed May 3, 2000; effective June 7, 2000.

810-3-14-.04 Collections Of Items Previously Deducted.

(1) If an amount which was properly allowed as a deduction in a prior year is subsequently recovered or refunded, the amount recovered or refunded must be included in income for the year of recovery to the extent that a tax benefit resulted from the deduction.

(2) A tax benefit includes a net operating loss available for carryback or carryforward.

(3) The phrase "recovery of an amount properly allowed as a deduction" does not include the "recovery" of depreciation on the sale or other disposition of an asset for more than its depreciated basis. Such "recovery" is included in the amount of gain to be recognized pursuant to §40-18-8, Code of Ala. 1975, and regulations thereunder.
Author: Ann F. Winborne, CPA, John Danziger, Rebecca S. Whisenant
Statutory Authority: Code of Ala. 1975, §§40-2A-7-(a)(5), 40-18-14.
History: **Amended:** September 7, 1988; filed October 26, 1988. **Amended:** Filed September 18, 1996; effective October 23, 1996. **Amended:** Filed July 26, 1999; effective August 30, 1999.

810-3-14-.05 Gross Income Of Nonresidents.

(1)(a) The gross income of a nonresident includes compensation for personal services only to the extent that the services were rendered in this State.

(b) Compensation for personal services rendered by a nonresident outside this State and not connected with the management or conduct of a business in this State is excluded from gross income even if payment is made from a point within this State or the employer is a resident individual, partnership or corporation.

1. Compensation for personal services rendered by a nonresident within this State is to be included in gross income although payment is received at a point outside this State or from a nonresident individual, partnership or corporation.

2. Where compensation is received for personal services rendered partly within and partly without this State, that part of the income attributable to this State is included in gross income. In such cases the test of physical presence is used to determine the situs of the rendition of the services, except where the peculiar nature of such services causes the objective of the employment to be accomplished or to take effect within this State, as, for example, where a nonresident acts as a fiduciary of an Alabama estate or trust. The gross income from commissions earned by a nonresident traveling salesman, agent, or other employee for services performed or sales made, whose compensation is in the form of a specified commission on each sale made, or service rendered, includes the specific commissions earned on sales made, or services rendered, in this State; and allowable deductions must be computed on the same basis. The gross income of all other nonresident employees, including corporate officers, includes that portion of the total compensation for services which the total number of working days employed within this State bears to the total number of working days employed both within and without this State during the taxable period. In the case of corporate officers and executives who spend only a portion of their time within this State, but whose compensation paid by a corporation operating in Alabama is exclusively for managerial services rendered by such officers and executives while within this State, the entire amount of compensation so earned is taxable without apportionment.

(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 status 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 (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 Ala. 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.
Author: Rebecca Whisenant, John H. Burgess, Amanda G. Scott, CPA
Statutory Authority: Code of Ala. 1975, §40-18-14.
History: Amended: June 17, 1988; filed July 27, 1988. **Amended:** Filed September 18, 1996; effective October 23, 1996.

810-3-14-.06 Payments By Employers For Past Services To Those No Longer In Their Employment; Payments To Widows Of Deceased Employees.

(1) Bonus or other post-employment payments made by an employer to his employee in the military service are considered to be compensation for services and includable in gross income, where the plan and agreement are that the employee is to return to his position when discharged from military service. If the payments are made as a gift, then the payments are not includable in gross income of the recipient. The deduction by the payer of the payments as a business expense is prima facie evidence that the payments are not gifts.

(2) Payments made by an employer to the widow of a deceased officer or employee as additional compensation, in recognition of and in consideration of services of said deceased officer or employee, are includable in the gross income of the widow.

(3)(a) Payments received by the widow of a deceased partner from a partnership are includable in gross income to the extent the payments represent a distribution of profits.

(b) If the payments represent a purchase or cancellation of the deceased partner's interest in the partnership, gain or loss will be recognized as provided in §40-18-8, Code of Ala. 1975.

(c) Any payments which constitute a gift from the partnership to the widow are not includable in gross income.

Author: Ann F. Winborne, CPA, John Danziger, Rebecca S. Whisenant
Statutory Authority: Code of Ala. 1975, §§40-2A-7(a)(5), 40-18-14.
History: **Amended:** June 17, 1988; filed July 27, 1988. **Amended:** Filed September 18, 1996; effective October 23, 1996. **Amended:** Filed May 3, 2000; effective June 7, 2000.

810-3-14-.07 Nonrecognition Of Gain On Sale Of Personal Residence (Repealed 11/16/01).

(Repealed)
Author: Royce Lader, Ann F. Winborne
Statutory Authority: Code of Ala. 1975, §40-18-14.
History: **Amended:** June 17, 1988; filed July 27, 1988. Filed May 15, 1992. **Repealed:** Filed October 12, 2001; effective November 16, 2001.

810-3-14-.08 Sale Of Principal Residence By Taxpayer Who Has Attained Age 55 (Repealed 11/16/01).

(Repealed)
Author: Royce Lader, Ann F. Winborne
Statutory Authority: Act 90-583.
History: **Amended:** June 17, 1988; filed July 27, 1988. Filed July 22, 1992; October 30, 1992. **Amended:** Filed September 18, 1996; effective October 23, 1996. **Repealed:** Filed October 12, 2001; effective November 16, 2001.

810-3-14-.09 Rental Value Of Home Or Rental Allowance Furnished A Minister Of The Gospel (Repealed 6/7/00).

(Repealed)
Author: Rebecca S. Whisenant, Amanda G. Scott, CPA
Statutory Authority: Code of Ala. 1975, §40-18-14.
History: **Amended:** June 17, 1988; filed July 27, 1988. **Amended:** Filed September 18, 1996; effective October 23, 1996. **Repealed:** Filed May 3, 2000; effective June 7, 2000.

810-3-14-.10 Estate And Trust Beneficiary Taxable Income (Repealed 6/7/00).

(Repealed)

Author: Roy Wiggins, Amanda G. Scott, CPA, Ann F. Winborne, CPA
Statutory Authority: Code of Ala. 1975, §§40-2A-7(a)(5), 40-18-14.
History: **Amended:** June 17, 1988; filed July 27, 1988. **Amended:** Filed September 18, 1996; effective October 23, 1996. **Repealed:** Filed May 3, 2000; effective June 7, 2000.

810-3-14-.11 Severance Pay Exemption (Repealed 3/12/09) .

(Repealed)
Author: Edward F. Cutter, CPA; Richard H. Henninger, Jr.; Judy A. Robbins, Ann F. Winborne, CPA
Statutory Authority: Code of Ala. 1975, §§40-2A-7(a)(5), 40-18-19.1.
History: **New Rule:** Filed February 20, 1998; Effective March 27, 1998. **Amended:** Filed May 3, 2000; effective June 7, 2000.
Repealed: Filed February 5, 2009; effective March 12, 2009.