****

**The Alabama Economic Freedom Act
Plain English Summary**

The Act is called the “Alabama Economic Freedom Act (AEFA).” As of Dec. 31, 2017, it repeals all income (including capital gains and corporate), estate and gift taxes and the existing state sales tax and replaces them with this bill.

Effective January 1, 2018 it replaces the above taxes with a state consumption tax on all goods and services sold at retail. The tax rate is set to be revenue neutral at the level necessary to replace the revenues generated by the repealed taxes.

A 6.0-percent (of the tax-inclusive sales price) consumption tax is imposed on all retail sales for personal consumption of new goods and services. Exports and the purchase of inputs by businesses (i.e., intermediate sales) are not taxed, nor are used goods or any savings, investment, or education tuition expenses. The consumption tax must be separately stated and charged on the sales receipt. This makes it clear to the consumer exactly how much they are paying in state taxes. Local sales taxes and real property taxes are not currently covered by this bill.

There are no exemptions under the Alabama Economic Freedom Act, meaning that no lobbyist, corporation, or individual can obtain tax advantages that are not available to the general public. Also, everyone pays the same rate, but those who spend more pay more total taxes than those who spend less.

The Alabama Economic Freedom Act provides every Alabama family with a rebate of the consumption tax on spending up to the federal poverty level (plus an extra amount to prevent any marriage penalty). The rebate is paid monthly in advance. It allows a family of four, for instance, to spend $32,480 tax free each year. The rebate for a married couple with two children is $162.40 per month ($1,948.80 annually). Therefore, no family pays state consumption tax on essential goods and services and middle-class families are effectively exempted on a large part of their annual spending. Retail businesses receive an administrative fee for collecting and remitting the tax.

Strong taxpayer rights provisions are incorporated into the Act. The burden of persuasion in disputes is on the government. The taxpayer is considered innocent until proven guilty. Taxpayers are entitled to professional fees in disputes unless the government establishes that its position was substantially justified.

**SECTION 1 --- TABLE OF CONTENTS**

**SECTION 2 --- FINDINGS OF THE ALABAMA LEGISLATURE**

Sec. a. Findings Relating to Alabama Income Tax.

Sec. b. Findings Relating to Existing Sales and Use Tax.

Sec. c. Findings Relating to the Estate and Inheritance Tax.

Sec. d. Findings Relating to the consumption tax.

**SECTION 3 --- TAXES REPEALED**

Sec. a. Effective Date.

Sec. b. Title 40 chapters repealed.

**SECTION 4 --- CONSUMPTION TAX ENACTED**

Sec. a. Effective Date.

Sec. b. Chapter 23 of Title 40 repealed and replaced with new Chapter 23

**Chapter 23. Consumption and Use Tax**

**§40-23-1. Table of Contents**

**Article 1. Interpretation; Definitions; Imposition of Tax; Etc.**

§40-23-11. Principles of interpretation

§40-23-12. Definitions

§40-23-13. Imposition of consumption tax

§40-23-14. Intermediate and out-of-state sales

§40-23-15. Rules relating to collection and remittance of tax

**Article 2. Credits; Refunds**

§40-23-21. Credits and refunds

§40-23-22. Business use conversion credit

§40-23-23. Intermediate and out-of-state sales credit

§40-23-24. Administration credit

§40-23-25. Bad debt credit

§40-23-26. Insurance proceeds credit

§40-23-27. Refunds

**Article 3. Family Consumption Allowance**

§40-23-31. Family consumption allowance

§40-23-32. Qualified family

§40-23-33. Monthly poverty level

§40-23-34. Rebate mechanism

§40-23-35. Change in family circumstances

**Article 4. Other Administrative Provisions**

§40-23-41. Destination determination

§40-23-42. Monthly reports and payments

§40-23-43. Registration

§40-23-44. Accounting

§40-23-45. Penalties

§40-23-46. Burden of persuasion and burden of production

§40-23-47. Summons, examinations, audits, etc.

§40-23-48. Records

§40-23-49. Tax to be separately stated and charged

§40-23-50. Applicable interest rate

**Article 5. Collections; Appeals; Taxpayer rights**

§40-23-51. Collections

§40-23-52. Power to levy, etc.

§40-23-53. Taxpayer Advocate

§40-23-54. Appeals

§40-23-55. Attorneys’ and accountancy fees

§40-23-56. Taxpayer rights

§40-23-57. Installment agreements; compromises

§40-23-58. Bankruptcy

**Article 6. Special Rules**

§40-23-61. Hobby activities

§40-23-62. Gaming activities

§40-23-63. Government purchases

§40-23-64. Government enterprises

§40-23-65. Mixed use property

§40-23-66. Not-for-Profit organizations

**Article 7. Financial Intermediation Services**

§40-23-71. Determination of financial intermediation services amount

§40-23-72. Bad debts

§40-23-73. Timing of tax on financial intermediation services

§40-23-74. Financing leases

§40-23-75. Basic interest rate

§40-23-76. Out-of-state financial intermediation services

**Article 8. Additional Matters**

§40-23-81. Additional matters

§40-23-82. Transition matters

§40-23-83. Phase-out of administration of repealed taxes.

**SECTION 5 --- CONFORMING AMENDMENTS**

Sec. a. Section 40-2-25 repealed.

Sec. b. Section 40-2A-4(b)(1)(a) amended.

Sec. c. Section 40-2A-4 amended.

Sec. d. Section 40-2A-17 repealed.

Sec. e. Section 40-2A-18 amended.

Sec. f. New section 40-5-48 enacted.

Sec. g. New section 40-29-122 enacted.

SECTION BY SECTION SUMMARY

SEC. 1. SHORT TITLE; TABLE OF CONTENTS

The Act is named the “Alabama Economic Freedom Act.” This section also contains an overview Table of Contents.

SEC. 2. LEGISLATIVE FINDINGS

This section sets forth substantive reasons why the Alabama Legislature finds that a state consumptions tax should replace the present tax system.

SEC. 3. TAXES REPEALED

Effective January 1, 2018, this section repeals the following chapters of Title 40:

(a) Chapter 9F (relating to tax credits for rehabilitation of historic structures);

(b) Chapter 14 (relating to the taxation of corporations);

(c) Chapter 14A (relating to the business privilege and corporation shares tax);

(d) Chapter 14B (relating to certified capital company and the premium tax credit);

(e) Chapter 15A (relating to the generation-skipping transfer tax);

(f) Chapter 16 (relating to financial institution excise tax)

(g) Chapter 18 (relating to income taxes); and

(h) Chapter 31 (relating to the facilitating business rapid response to declared disasters act)

SEC. 4. CONSUMPTION TAX ENACTED

Effective January 1, 2018, this section enacts new “Chapter 23. Consumption and Use Tax”, consisting of 8 Articles.

**ARTICLE 1—INTERPRETATION; DEFINITIONS; IMPOSITION OF TAX; ETC.**

This article contains the provisions that impose the state consumption tax on the use or consumption of taxable goods and services in the State of Alabama. It defines the tax rate, provides for the coordination of the tax with import duties, and defines the liability for the tax.

**§40-23-11. Principles of interpretation**

This section provides guidance that any court, the Commissioner of Revenue and his delegates, and any other authority shall consider the purposes of this chapter as the primary aid in statutory construction. The purposes are to raise revenue needed by the State of Alabama in a manner consistent with the other purposes of this chapter, to tax all consumption of goods and services in Alabama once, without exception, but only once, to prevent double, multiple, or cascading taxation; to simplify the tax law and reduce the administration costs of, and the costs of compliance with, the tax law; to provide for the administration of the tax law in a manner that respects privacy, due process, individual rights when interacting with the government, the presumption of innocence in criminal proceedings, and the presumption of lawful behavior in civil proceedings. As a secondary aid in statutory construction, any court, the commissioner and his delegates, and any other authority shall consider the common law canons of statutory construction; the meaning and construction of concepts and terms used in Title 40 as in effect before the effective date of this Act; and construe any ambiguities in this Act in favor of reserving powers to the people. Whenever chapter 23 is inconsistent with any other chapter of this title, chapter 23 shall govern with respect to the administration and collection of the taxes imposed by chapter 23.

**§40-23-12. Definitions**

These definitions are key to understanding which transactions are taxable and which are not. The key definitions are listed below:

AFFILIATED FIRMS – A firm is affiliated with another if one firm owns 50 percent or more of the voting shares in a corporation or 50 percent or more of the capital interests of a business firm that is not a corporation.

COMMISSIONER.—The term ‘commissioner’ means the individual appointed by the Governor as state Commissioner of Revenue pursuant to section §40-2-40 and his or her delegates.

DESIGNATED COMMERCIAL PRIVATE COURIER SERVICE.—A designated courier service must be used to submit a revised Prebate registration and remit weekly tax collections by the larger retailers. The term ‘designated commercial private courier service’ means a firm designated as such by the commissioner. To gain this designation, the firm’s application must show that it provides its services to the general public, electronically records the date an item was given to such firm for delivery to its data base kept in the regular course of its business and has been operating for at least 1 year.

EDUCATION AND TRAINING.— Tuition for primary, secondary, postsecondary education, and job-related training courses is not taxable. It is treated the same as services used to “produce, provide, render, or sell taxable property or services” which are also not taxable. This applies to both public schools and private schools. Generally, public schools at the primary and secondary level don’t charge tuition; however, the tuition charged by public postsecondary education institutions, such as state universities and community colleges, is exempt.

Tuition does not include charges for room and board, sports activities, recreational activities, hobbies, games, arts or crafts or cultural activities.

GROSS PAYMENTS – equals payments for the taxable good or service plus the consumption tax. A retail business computes its state tax liability by multiplying the rate of 6.0 percent times the monthly gross payments received.

INTANGIBLE PROPERTY/ CERTAIN TYPES OF PROPERTY.— In general, the term ‘intangible property’ includes copyrights, trademarks, patents, goodwill, financial instruments, securities, commercial paper, debts, notes and bonds, and other property deemed intangible at common law. The term ‘certain types of property’ does not include tangible personal property (or rents or leaseholds of any term thereon), real property (or rents or leaseholds of any term thereon) and computer software.

PERSON.—The term ‘person’ is defined in §40-1-1(8).

PRODUCE, PROVIDE, RENDER, OR SELL TAXABLE PROPERTY OR SERVICES.— If a person or business buys taxable property or services for the purpose of using such property or service in the production, provision, rendering, or sale of other taxable property or services in the ordinary course of that business, then that purchase is not subject to the consumption tax. This exempts intermediate sales to businesses and prevents the consumption tax from cascading and being hidden in the retail price of the final consumption good or service produced by that person or business. Example: If a business were to pay sales tax on the purchase of “inputs,” then, in order to recover its costs, it would have to build the taxes paid on inputs into the retail price of what it sells. This would result in taxing a tax.

The purchases of property or services used for research, experimentation, testing, and development are included as non-taxable business purchases.

Taxable property or services purchased on behalf of an insured person (policyholder) are treated as purchases for business purposes and are not taxed if sales tax was paid on the premium for the insurance contract under which the claim was paid. If the premium for the insurance policy is taxed, it would be double taxation to also charge tax on the benefits paid for by the insurance policy.

Tuition for education and training is treated as a service used to produce, provide, render, or sell taxable property or services.

REGISTERED SELLER.—The term ‘registered seller’ means a person registered pursuant to §40-23-43.

RESPONSIBLE OFFICERS AND PARTNERS.— For purposes of §40-23-45(m), the term ‘responsible officers and partners” means in the case of a corporation, any officer who is the President, the Chief Executive Officer, a Vice-President, the Secretary, the Treasurer, the Chief Financial Officer or serves a similar function for the corporation; in the case of a partnership, any partner other than limited partners; in the case of a limited liability company, any officer serving the function of a corporate President or Chief Executive Officer, Treasurer or Chief Financial Officer or Secretary and any member actively engaged in the management of the company.

TAXABLE EMPLOYER.— Generally, the term taxable employer includes (1) any household employing domestic services (nannies, housekeepers, gardeners, etc.), and (2) any government except for government enterprises (as defined in §40-23-64). Excluded from the definition of taxable employers are: (1) any employer engaged in a trade or business, (2) an employer who is a not-for-profit organization (as defined in §40-23-66), or (3) a government enterprise (as defined in §40-23-64) - (quasi business entity that charges a fee for their services, such as the U.S. Post Office and Amtrak).

For cross reference regarding rules relating to collection and remittance of tax on wages by taxable employers, see §40-23-15(b)(2).

TAX INCLUSIVE FAIR MARKET VALUE.—The term ‘tax inclusive fair market value’ means the fair market value of taxable property or services plus the tax imposed by this chapter.

TAXABLE PROPERTY OR SERVICE.— In general. the term ‘taxable property or service’ means any property (including leaseholds of any term or rents with respect to such property) but excluding intangible property, used property, and any service (including any financial intermediation services as determined by §40-23-71).

The term ‘service’ includes any service performed by an employee for which the employee is paid wages or a salary by a taxable employer, and shall not include any service performed by an employee for which the employee is paid wages or a salary by an employer in the regular course of the employer’s trade or business, by an employer who is a not-for-profit organization (as defined in §40-23-66), by an employer who is a government enterprise (as defined in §40-23-64), and by taxable employers to employees directly providing education and training.

USED PROPERTY.—The term ‘used property’ means property on which the tax imposed by this chapter has been collected and for which no credit has been allowed under §§40-23-22, 40-23-23, or 40-23-26, or property that was held other than for a business purpose (as defined in §40-23-14) on December 31, 2017.

WAGES AND SALARY.—The terms ‘wages’ and ‘salary’ mean all compensation paid for employment service including cash compensation, employee benefits, disability insurance, or wage replacement insurance payments, unemployment compensation insurance, workers’ compensation insurance, and the fair market value of any other consideration paid by an employer to an employee in consideration for employment services rendered.

The definitions of taxable employer and taxable service operate together to require that wages paid by a government agency (as a taxable employer) are taxable and the tax must be remitted by the government agency to the state consumption tax division. They also require households that employ domestic servants to remit the tax on the price paid for the domestic employee’s services. The household is both the consumer of the services and the person liable for collecting and remitting the consumption tax on those services. If the household purchases domestic services from a registered seller (e.g., “Nannies Are Us”), then the registered seller is responsible for collecting the consumption tax on the sale of the nanny services to the household and remitting the tax.

Services performed by an employee who is employed by (1) an employer in the regular course of the employer’s trade or business, (2) a not-for-profit organization, (3) an employer who is a government enterprise, and (4) taxable employers (i.e., government school districts and universities) directly providing education and training are not taxable. In other words, wages paid to employees by businesses, not-for-profit organizations, and government enterprises are not subject to the consumption tax. These entities collect the consumption tax on the sale of taxable goods or services to the consumer.

The above definitions of “taxable employer” and “taxable service” have the effect of taxing government consumption. Since governments generally provide services free to the public, the value of the consumption is the value of the services used to provide services to the public, i.e., the services of labor or compensation paid.

Cross References.—

1. For the definition of business purposes, see §40-23-14.

2. For the definition of insurance contract, see §40-23 -26(e).

3. For the definition of qualified family, see §40-23-32.

4. For the definition of monthly poverty level, see §40-23-33.

5. For the definition of large seller, see §40-23-42(e)(3).

6. For the definition of hobby activities, see §40-23-61.

7. For the definition of gaming sponsor, see §40-23-62(a).

8. For the definition of a chance, see §40-23-62 (b).

9. For the definition of government enterprise, see §40-23-64(b).

10. For the definition of mixed use property, see §40-23-65.

11. For the definition of qualified not-for-profit organization, see §40-23-66.

12. For the definition of financial intermediation services, see §40-23-71.

**§40-23-13. Imposition of consumption tax**

This section imposes a tax on the use or consumption in the State of Alabama of taxable property or services. The tax rate is 6.0 percent of the gross payments for the taxable property or service. The purchaser of the property or service is liable to the State for the tax, except where the purchaser pays the tax to the seller and receives a receipt therefore (see Section §40-23-49).

**§40-23-14. Intermediate and out-of-state sales**

For purposes of this chapter, no tax is imposed under §40-23-13 on any taxable property or service purchased for a business purpose in a trade or business. No tax is imposed under §40-23-13 on any taxable property or service purchased for an investment purpose and held exclusively for an investment purpose.

The term ‘purchased for a business purpose in a trade or business’ means purchased by a person engaged in a trade or business and used in that trade or business for resale, to produce, provide, render, or sell taxable property or services, or in furtherance of other bona fide business purposes.

The term ‘purchased for an investment purpose’ means property purchased exclusively for purposes of appreciation or the production of income but not entailing more than minor personal efforts.

**§40-23-15. Rules relating to collection and remittance of tax**

Generally, the sales tax must be collected and remitted by the seller of taxable property or services. In the case of an exempt purchase, the seller is relieved of liability for the tax if the seller retains on file a copy of the registration certificate from the purchaser. The copies of the registration certificates provide proof, when the seller is audited by the state consumption tax division, that the sale should be tax exempt. (This certificate could be either a business’s registered seller certificate showing that the purchase is being made by a business registered with the state sales taxing authority, or a qualification certificate for a religious or charitable nonprofit agency.)

A consumer who directly brings taxable property into Alabama is required to pay the tax, since the seller is outside of the state.

In the case of wages paid by a taxable employer that are taxable services, the employer must pay the tax imposed by Section §40-23-13. Taxable employers include households that employ maids, nannies or gardeners, etc. as employees (rather than acquiring services from a business that collects and remits the sales tax) and government (except government enterprises).

Government enterprises are governmental entities that receive payments from private persons for goods and services. They must maintain books of accounts separate from the non-enterprise governmental accounts. For example, the expenses and receipts of a county landfill enterprise must be kept separate from the expenses and receipts of the general county government. Examples are the U.S. Post Office, Amtrak, local government waste management operations, etc. These enterprises, at all levels of government, are treated the same as private businesses with respect to their purchases and sales to consumers. This means that any intermediate purchases by government enterprises are not taxed; only the final sale of goods or services to the consumer is taxed.

Property or services originally purchased for a business purpose or for sale outside the state that are subsequently converted to personal use are subject to the sales tax at the fair market value on the date of the conversion. The person using or consuming the property is liable for the tax and has the responsibility to remit the tax to the state sales taxing authority. Example: If a business owner purchased a $20,000 car for business purposes and two years later decided to give the car to his or her teenager, then they would have to pay the sales tax on the value of the car at the time, say $15,000.

Barter transactions are taxed at the fair market value of the goods or services bartered. Example: A plumber fixes a toilet in a farmer’s residence, and the farmer offers to pay him with produce from the farm. As the seller of the service, the plumber is responsible for remitting the tax based on his normal charge for fixing a toilet. If he normally charges $100, then he owes tax on that amount.

**ARTICLE 2—CREDITS; REFUNDS**

This article sets forth the various credits that registered sellers can claim against their consumption tax liability on their monthly consumption tax return.

**§40-23-21. Credits and refunds**

With respect to Section §40-23-13, this section lists certain allowable credits to retailers for business use conversion credit pursuant to §40-23-22, intermediate and out-of-state sales credit pursuant to §40-23-23, the administration credit pursuant to §40-23-24, the bad debt credit pursuant to §40-23-25, the insurance proceeds credit pursuant to §40-23-26 for such month, the transitional inventory credit pursuant to §40-23-82, and any amount paid in excess of the amount due. However, only one credit allowed by Article 2 may be taken with respect to any particular gross payment.

**§40-23-22. Business use conversion credit**

This section explains the calculation of the tax credit available when one converts property to a business use. If a person paid the consumption tax on the purchase of an item for personal consumption, then later began to use that item at least 95 percent for business purposes, he/she can get back a portion of the sales tax paid. The credit amount is the lesser of (a) the consumption tax paid or (b) the consumption tax that would have to be paid to purchase the item at fair market value at the time when it was converted from personal use to business use. Example: Using a home computer as equipment in a new business. If the price of the computer were $2000 in 2017 when it was purchased for personal use, and then it was converted to business use in 2018, the business person could apply for a credit based on the amount of tax that would be due on a two-year-old computer valued at $1000.

**§40-23-23. Intermediate and out-of-state sales credit**

This section provides a credit for any taxes paid on the purchase of any taxable property or service purchased for a business purpose or for use or consumption outside the State of Alabama.

**§40-23-24. Administration credit**

This section basically provides imbursement to every person filing timely monthly reports and remittances. Every registered seller filing a timely monthly consumption tax report is entitled to a taxpayer administrative credit for collecting the tax on behalf of the State of Alabama. To qualify for the credit, the consumption tax report must be filed in a timely manner. Rather than sending the retailer a check, the retailer is allowed to claim an administrative credit against the amount of tax due on its monthly sales tax return, provided that the return is filed timely.

The monthly credit is equal to the *greater* of these two amounts: (1) $200 or (2) one-quarter of one percent of the tax paid, but the credit cannot exceed 20 percent of the tax paid.

Figure 1 shows how to calculate the administrative credit based on various monthly sales amounts. Column (3) shows how much the credit is, based on one-quarter of one percent of sales. Column (5) shows the maximum credit allowable.

The cap affects registered sellers with monthly retail sales of less than $16,000. For example, a retailer with only $500 in monthly sales can claim a credit of $6.40. They will not receive the $200 per month minimum, but will get the amount in the maximum column. Those with monthly sales between $16,000 and approximately $1,400,000 per month will get the minimum credit of $200 per month. Those with monthly sales higher than $1,400,000 per month will receive the one-quarter of one percent of taxes collected amount in column (3). The minimum payment of $200 and the cap of 20 percent are no longer a factor for sales at this level or higher.

The administrative credit is designed to compensate retailers for their costs associated with collecting the consumption tax and remitting it to the state. The AEFA consumption tax is much simpler than the income tax, and businesses already file monthly state sales tax returns. The retailer won’t have to deal with income tax withholding for their employees and never has to file income tax returns again.

**Figure 1: How to calculate the administrative credit**

****

**§40-23-25. Bad debt credit**

This section provides a credit for taxes on Financial Intermediation Services, Unpaid Invoices, Subsequent Payment and Partial Payments, actually remitted to the State of Alabama, but not actually collected by the remitter due to failure of the purchaser to remit payment. The credit provided by this section shall not be available with respect to sales made to related parties. For purposes of this section, related party means affiliated firms (as defined in §40-23-12(a)(1)) and family members.

Any person who has experienced a bad debt (this does not include unpaid invoices) is entitled to a credit which is equal to the tax rate times [the amount of the bad debt divided by (1 minus the tax rate)]. A bad debt of $1000 would qualify for a credit equal to 0.06 times [$1000/0.94] or 0.06 times $1,064 = $64. This would apply to financial institutions.

The credit also applies to persons electing the accrual method of reporting who have remitted tax on unpaid invoices. To qualify for the credit for unpaid invoices, the person must have charged the tax on the invoice, remitted the invoiced tax, delivered the taxable property or performed the taxable service invoiced, and not been paid six months after the invoice was due to be paid. Example: An accountant bills a client on a quarterly basis, and because he uses the accrual method, he pays the consumption tax during the month he invoices. Six months later, his client has not paid the invoice. The accountant is able to get a credit of the taxes he remitted when he issued the invoice, since the invoice has not been paid.

The bad debt credit also prevents the taxation of the risk premium portion of the interest rate. This credit is equal to the sales tax rate times the bad debt amount. Subsequent debt payments are taxable. This credit is also provided to accrual method taxpayers who have remitted sales tax on sales for which they have not yet been paid.

This credit is not available to sales made between related parties, i.e., affiliated firms and/or family members.

**§40-23-26. Insurance proceeds credit**

This chapter provides a tax credit for insurance proceeds and explains the method for calculating that credit. This amount may be paid by the insurer to the insured in which case the insured would be entitled to claim the credit, or the insurer may opt not to remit this sum to the insured, in which case the insured must apply for the credit.

For consumption tax purposes, insurance premiums have two components: (1) dollars paid back as claims, and (2) dollars kept. The dollars kept are what is paid for the service of insuring the policyholder. The consumption tax is paid on the purchase of this service, but not on the dollars paid back as claims. This applies to all types of insurance: Life, health, property and casualty, liability, marine, fire, accident, disability, and long-term care.

To ease administration, the policyholder pays the consumption tax on the entire premium and receives a credit for taxes paid on claims received. Example: Annual Premium = $1000. The policyholder pays $1,000 + $6 consumption tax. If the policyholder were to receive a claim payment of $400, he/she would be entitled to a refund of taxes paid (6.0% of $400 = $24).

When the insurer makes a claim payment to a provider of goods or services to a policyholder (examples: Payment to a doctor for an exam, payment to a hospital for room and meals, payment to an automobile body shop for repairs covered by car insurance) instead of to the policyholder directly, the insurance company does not pay consumption tax on that payment. This is because the policyholder (i.e., consumer) effectively pre-paid the consumption tax when he or she purchased the insurance policy. The purchase of goods or services by the insurer on behalf of the insured are considered purchases for business purposes and are not taxable. Conversely, the consumer’s direct purchase of goods and services from a provider are taxable. Example: Insurance co-payments and services not covered by insurance.

The purchase of insurance by a business for its employees is taxable. The business owes the tax. (See §40-23-81 ADDITIONAL MATTERS.)

**§40-23-27. Refunds**

This section provides for refunds in the cases of overpayment of taxes.

Registered sellers and other persons are entitled to the refund of any overpayment of tax. They can claim a credit on their monthly sales tax report or they can apply to the state consumption tax division for a refund. The overpaid tax must be refunded to the registered seller within 60 days of receipt of the application. If not, the government is required to pay interest on the refund amount from the date the refund application was received, at the federal short-term interest rate. This serves as an incentive for the government to pay refunds on a timely basis.

**ARTICLE 3—FAMILY CONSUMPTION ALLOWANCE**

This article provides for the family consumption allowance or monthly prebate of consumption taxes paid to qualified households.

**§40-23-31. Family consumption allowance [AEFA Prebate]**

This section provides for a rebate (actually a prebate) of all taxes up to the poverty level to each qualified family, as defined in the next section.

Each qualified family is entitled to a monthly rebate of the consumption tax paid on poverty level spending. Poverty level spending is calculated annually by the Department of Health and Human Services to represent what it costs families of varying household size and composition to buy their necessities. The monthly sales tax rebate is equal to the consumption tax rate (6.0 percent) times the monthly poverty level (see §40-23-33).

**§40-23-32. Qualified family**

The term “qualified family” means one or more family members sharing a common residence. A qualified family consists of all family members sharing the common residence. Family members include an individual and his or her spouse, children and grandchildren, parents and grandparents. Children/students living away from home are considered family members if they are registered as a student for at least five months out of the year and receive at least 50 percent of their support from the family unit. Children of divorced parents are considered to be family members of the custodial parent. Incarcerated individuals are not eligible to be a member of a qualified family.

In order for a person to be counted as a member of the family for purposes of determining the size of the qualified family, a person must have a valid Social Security number and be a lawful resident of both the United States and the State of Alabama.

Families who choose to receive the rebate must register annually with the state. Those choosing not to register will not receive a rebate. The registration form requires the following information:

1. The name of each family member who shares the residence
2. The Social Security number of each family member
3. The family member to whom the rebate should be paid
4. A sworn statement that all listed family members are lawful residents of both the United States and the State of Alabama, that all family members sharing the common residence are listed, and that no family members are incarcerated
5. The address of the shared residence

All family members 21 years of age and older must sign the registration form.

After the initial registration, any qualified family that fails to renew its registration each year, within 30 days of the family determination date, will cease receiving the rebate 90 days following the failure to register. However, the family can file to get up to six months of missed rebates later (with no interest on missed payments). A possible method of assigning registration renewal dates would be on the birth date of the person filing the application. 30 or more days before the annual registration date, the consumption tax division is required to mail a proposed registration form to each qualified family that simply needs to be signed and mailed back in if the family’s circumstances have not changed.

Penalties for filing a false rebate claim are addressed in §40-23-45(i).

**§40-23-33. Monthly poverty level**

This section describes how the monthly poverty level is calculated.

The monthly poverty level is 1/12th of the annual poverty level (as determined by the Department of Health and Human Services – DHHS), plus an additional amount to eliminate what would otherwise be a penalty for being married, multiplied by the consumption tax rate. This amount is adjusted each year as DHHS recalculates poverty level spending. See Figure 2a.

**Figure 2a. Rebate Schedule for Single and Two Adult Heads of Household**

****

The annual consumption allowance is the amount of tax-free spending under the consumption tax. For families/households with more than 8 persons, add $4,160 to the annual consumption allowance for each additional person. The annual consumption allowance is based on the DHHS 2017 HHS Poverty Guidelines as published in the Federal Register, January 25, 2016. The annual prebate equals 6.0% of the annual consumption allowance.

 As illustrated in Figure 2b, the prebate makes the consumption tax a progressive system in a positive way for the consumer. Only spending above the poverty level is taxed, which results in the effective rate being lower than 6.0% across the spectrum. To illustrate, the effective tax vs. spending is shown for a family of four. The prebate covers the tax up to $32,480, after which the consumer becomes a discretionary spender. At 1.5 times the poverty level, the effective rate is 2%, at 2 times the poverty level, the effective rate is 3% and so forth across the increasing spending levels. A graph for the effective rate for each poverty level would not approach the full 6.0% consumption tax until spending 16 times each level as illustrated by Figure 2b. Also, notice that under the AEFA, consumers must spend approximately 6-times their allowable poverty level before reaching the current 4.0% sales tax along with no income tax being taken from their salaries.

**Figure 2b. Effective Consumption Tax Rate**



**§40-23-34. Rebate mechanism**

The state consumption tax division sends out the monthly rebates on or before the first day of every month. Rebate payments can only be made to persons 18 years or older. If a family wishes to designate more than one person to receive the rebate, then the rebate payment is divided evenly among those persons designated. Example: Two single people sharing the same residence are able to each get a rebate check. In accordance with instructions from each qualified family, the state consumption tax division provides the rebate in the form of a paper check via U.S. Mail, an electronic funds transfer to a bank account, or a “smart card” that can be used much like a bank debit card.

**§40-23-35. Change in family circumstances**

A qualified family may file a revised registration to report changes in family circumstances. A revised registration must be signed by all members of the qualified family who are 21 years of age or older. Address changes may be filed with the state consumption tax division at any time and do not require the signature of all family members. It is unlawful to willingly and knowingly file a false claim for a family consumption allowance rebate. (See §40-23-45(i) for an explanation of penalties.)

In no event shall a person be considered part of more than one family. Example: The rebate payment process should involve a search for the same Social Security number being listed in more than one family. These rebate checks are not mailed until it is resolved which family that person (and Social Security number) is a member of.

**ARTICLE 4—OTHER ADMINISTRATIVE PROVISIONS**

This article sets forth the general administration of the consumption tax: Seller registration and certificates, the filing of monthly tax reports and payments, and penalties for noncompliance. It also specifies the burden of persuasion and production in disputes regarding tax liability and tax payments.

**§40-23-41. Destination determination**

Generally, the tax imposed by this chapter is a destination principle tax. This section governs for purposes of determining whether the destination of taxable property and services is within or without of the State if Alabama. The following list specifies the destination of the sale for different types of goods or services:

• Tangible personal property (goods) – where the property was first delivered to the purchaser

• Real property – where the property is located

• Other property – the location of the residence of the purchaser

• Services – where the use or consumption of the services takes place

• Telecommunications services – the location of the residence of the purchaser

• Domestic transportation services – the destination of the trip

• Electrical service – the location of the residence of the purchaser

• Financial intermediation services – the residence of the purchaser

• Rents paid for the lease of property – where the property is located while in use

• Rental of vehicles less than one month – where the vehicle was originally delivered to the renter or lessee

• Rental of vehicles greater than one month – the location of the residence of the renter or lessee

**§40-23-42. Monthly reports and payments**

Retailers must regularly report gross sales and the consumption tax collected on those sales and any consumption tax credits the government owes them to their state consumption tax division. They must remit the consumption tax collected (minus any credits owed to them) along with the report. Upon request, a filing date extension of 30 days will be automatically granted. On application, extensions of 30 to 60 days may be granted for reasonable cause. Extensions greater than 60 days may be granted to avoid hardship. Although extensions for the late filing of sales tax reports may be granted, the taxes due must be remitted timely, generally by the 15th of the following month. Example: The consumption tax collected on sales in January must be remitted to the state sales tax authority by February 15th.

The sales tax report requires the following information:

1. The gross payments
2. The tax collected
3. The amount and type of any credit claimed
4. Other information reasonably required for the administration, collection, and remittance of the tax (example: Business name, address, type of business, registered seller number).

Small sellers are persons who have collected less than $5,000 of consumption tax in any of the previous 12 months. They are required to remit the consumption tax on or before the 15th day of the following month. Example: Taxes collected on sales during the month of January must be sent to the state consumption tax division on or before February 15th.

Medium-sized retailers who collect more than $5,000, but less than $50,000, of consumption tax per month must deposit the taxes they collect in a separate bank account each week within three business days of the end of the week. They must report and remit taxes on a monthly basis.

Large sellers are sellers who have collected $50,000 or more of consumption tax in any of the previous 12 months. They must deposit all taxes collected in a separate bank account and remit the taxes to the state consumption tax division on a weekly basis. Example: Last week’s taxes must be remitted on the following Monday.

The Commissioner may adopt a regulation that requires large sellers to remit collected taxes by electronic funds transfer. (Most large sellers are already set up to do this since most states already require large sellers to remit taxes by electronic funds transfer.)

Large sellers must also post a bond in an amount equal to the greater of $100,000 or 1.5 times their average monthly tax liability during the previous six calendar months. If the seller fails to remit taxes due then the bond or part of the bond may be forfeited to pay overdue taxes plus interest (if any).

**§40-23-43. Registration**

Each person liable to collect the consumption tax (pursuant to §40-23-15(a) and including corporations and sole proprietors) who is engaged in a trade or business shall register as a “seller” with the commissioner. This includes retailers, wholesalers selling to businesses tax exempt, exporters, service providers, mortgage brokers, real estate brokers, insurance agencies, etc. They are required to designate a contact person for tax matters, and are required to notify the sales tax authority of a change in the identity of the tax matters person within 30 days of said change. Any person who is required to register, and fails to do so, may be prohibited from selling taxable property or services by a temporary restraining order or injunction, as appropriate.

Affiliated firms are treated as one person and require only one registration.

**§40-23-44. Accounting**

Registered sellers and other persons shall report transactions using the cash method of accounting unless an election to use the accrual method of accounting is made.

Most businesses will probably prefer the cash method since it means that they do not need to pay tax on a transaction until they have been paid. If someone pays only part of a bill, then the tax is remitted for only the portion that has been paid. Example: A lawyer bills a client $500. Taxes due on this sale are $32 for a total of $532. If his/her client only pays $282, then the lawyer would only remit 6.0 percent of the gross payment as tax ($17) with the monthly sales tax report. The next month, his client pays the balance of $250. The lawyer would remit 0.06 times $250 or $15 on that month’s sales tax report. The total tax remitted is the same. Those who use the accrual method of accounting internally may find it easier to pay taxes using the accrual method. There is a bad debt credit for registered sellers using the accrual method whereby they can get a refund of taxes paid on gross payments that were not received (i.e., paid for with a check with insufficient funds). See §40-23-22, Business Use Conversion Credit.

Businesses collecting the consumption tax may report and remit the consumption tax in the month in which they actually collect the tax or they may elect to report and remit the tax in the month in which they invoice and accrue the sale. (Accrual accounting is a method of accounting that recognizes economic events regardless of when cash transactions happen. It is the opposite of cash accounting, which recognizes transactions only when there is an exchange of cash.) Example: Under accrual accounting, if a business sells a stereo on credit, the business would still recognize the event as a completed transaction in that month and remit the tax, even though full payment had not yet been received. See Section 40-23-25 for rules relating to bad debts for sellers electing the accrual method.

**§40-23-45. Penalties**

Civil penalties for noncompliance are graduated so that more severe violations are punished more severely and generally escalate over time (subject to caps) so that there is a continuing incentive to comply. There are also criminal fines and imprisonment for noncompliance. The fact that a civil penalty has been imposed shall not prevent the imposition of a criminal penalty, and vice versa.

The tax matters person (designated by the business) and responsible officers or partners of a firm shall be jointly and severally liable for the tax and penalties. The concept of “joint and several liability” provides that both the tax matters person and the responsible officers or partners are each responsible for the entire amount of taxes and penalties, regardless of their relative degree of responsibility for the nonpayment of taxes. However, each person who paid such tax or penalty is entitled to recover from the other persons who are liable an amount equal to the excess of the amount he paid over his proportionate share of the tax or penalty.

* Failure to register – penalty of $500
* Reckless or willful failure to collect tax, reckless or willful failure to pay tax, and willful assertion of invalid exemption – civil penalty, the greater of $500 or 20 percent of tax not collected; criminal penalty, imprisonment for up to one year
* Reckless or willful assertion of an invalid intermediate or out-of-state sales exemption: civil penalty; fraud, liable for a penalty equal to the greater of $500 or 20 percent of the tax not collected or remitted; criminal penalty, possibly may be fined up to the amount determined in civil penalty or imprisoned for a period of not more than 1 year or both.
* Reckless or willful failure to remit tax collected: civil penalty; fraud, liable for a penalty equal to the greater of $1,000 or 50 percent of the tax not remitted; criminal penalty, may be fined an amount up to the amount determined in civil penalty or imprisoned for a period of not more than 2 years or both.
* Reckless or willful failure to pay tax: liable for a penalty equal to the greater of $500 or 20 percent of the tax not paid.
* Late filing – the greater of $50 for each month the report is late, or 0.5 percent of gross payments required to be shown on reports. Caps this penalty to 12 percent.
* Accepting false intermediate or export sales certificate – fined 20 percent of the tax not collected
* Late payment interest – Interest penalty shall be charged on late tax payments equal to 1.0 percent per month from the due date. Caps this penalty to 24 percent.
* False rebate claim – civil penalty, the greater of $500 or 50 percent of the claimed annual rebate amount not actually due, must repay any falsely due rebates; criminal penalty, imprisonment for up to one year
* Bad checks – the greater of $25 per check or 2 percent of check amount
* Failure to maintain a segregated account – $500 penalty
* Penalty for Failure To Deposit Collected Taxes in a Separate Segregated Account.— failure to timely deposit taxes into the separate segregated account - pay a penalty equal to 1 percent of the amount required to be deposited. The penalty is tripled unless the taxes have been deposited in the separate segregated account or remitted to the commissioner within 16 days of the deposit due date.
* Joint and Several Liability for Tax Matters Person and Responsible Officers or Partners.—The tax matters person and responsible officers or partners of a firm shall be jointly and severally liable for tax and penalties imposed.
* Right of Contribution.— If the liability for any tax or penalty can be spread over several persons, each person who paid the tax or penalty is entitled to recover from the others any excess s/he may have paid. Controlling regulations from the commissioner may take culpability into account when allocating liability for tax or penalty among responsible officers or partners.
* Civil Penalties and Criminal Fines Not Exclusive.—The fact that a civil penalty has been imposed does not prevent the imposition of a criminal fine. Conversely, the fact that a criminal fine has been imposed shall not prevent the imposition of a civil penalty.
* Violation of confidentiality of tax information – fined up to $10,000 or imprisoned for up to one year, or both

This is much simpler that the current income tax system which has approximately many more different penalties.

**§40-23-46. Burden of persuasion and burden of production**

In all disputes concerning taxes imposed by this chapter, the person engaged in a dispute with the commissioner shall have the burden of production of documents, but the commissioner shall have the burden of persuasion.

**§40-23-47. Summons, examinations, audits, etc.**

The commissioner may issue summons for documents and testimony to accurately determine liability for tax and may conduct at a reasonable time and place examinations and audits, except where the person is under investigation by the Attorney General’s Office.

The commissioner may conduct reasonable audits and examine the books, papers, records, or other relevant data to ensure that the consumption tax is administered properly. Persons are subject to administrative summons by the commissioner for records, documents, and testimony required by the commissioner to accurately determine liability for tax. The summons must describe with certainty what information is being sought and must be served by an attested copy delivered in hand to the person to whom it is directed or left at his/her last known address.

**§40-23-48. Records**

Businesses collecting the consumption tax are required to keep records. These records include:

1. A record of all consumption tax receipts provided to customers
2. Complete records of intermediate and export sales
3. Purchaser’s intermediate and export sales certificates and tax numbers
4. The net of tax amount of purchase

These records must be sufficient to determine the amounts reported, collected, and remitted for a period of six years after the report was filed.

Purchasers (any business including not-for-profit organizations and government enterprises) that purchased taxable property or services but did not pay tax because they asserted an intermediate or export sales exemption are required to keep records sufficient to determine whether said exemption was valid for a period of seven years after the purchase of the taxable property or service.

The purpose of such record retention is to allow an auditor to review reported taxable and exempt sales after the fact. It enables the auditor to determine if sales were properly tax exempt or if the consumption tax should have been collected on the sale.

**§40-23-49. Tax to be separately stated and charged**

A business collecting the consumption tax must provide to the purchaser a receipt for each transaction that sets forth at least the following information:

1. The property or services price exclusive of tax
2. The amount of tax paid
3. The property or service price inclusive of tax
4. The tax rate (the amount of tax paid divided by the price inclusive of tax)
5. The date that the good or service was sold
6. The name of the vendor
7. The vendor registration number

There are two exceptions: (1) the above does not apply to sales by certain vending machines, and (2) receipts with respect to financial intermediation services. These receipts are issued when the consumption tax is imposed, which is generally when monthly or quarterly financial statements are rendered (see §40-23-73).

**§40-23-50. Applicable interest rate**

In the case of a debt instrument, investment, financing lease, or account with a term of not over 3 years, over 3 years but not over 9 years, and over 9 years, the applicable interest rate is the Federal short-term, mid-term, and long-term, respectively, as determined by the United States Secretary of the Treasury, or by the commissioner in the absence of Treasury determination. The amount of interest due to be paid by the taxpayer with respect to past due taxes imposed by this chapter shall be determined by the rate determined in accordance with §40-23-40.

**ARTICLE 5—COLLECTIONS; APPEALS; TAXPAYER RIGHTS**

This article provides for the general collection and enforcement of the consumption tax, including an appeals process and a specification of taxpayer rights.

**§40-23-51. Collections**

The commissioner is responsible for collecting the taxes imposed by this chapter.

**§40-23-52. Power to levy, etc.**

The commissioner may levy and seize property, garnish wages or salary and file liens to collect amounts due under this chapter only if a judgment has been rendered by a court of law, the taxpayer has failed to appeal an assessment of an amount due, or the taxpayer has failed to timely petition a court for relief after decision in the appeals process. Exempted from this process are wearing apparel, school books, fuel, provisions, furniture, personal effects tools of a trade or profession, livestock in a household up to an aggregate value of $15,000 and monthly money income equal to 150% of the monthly poverty level. Any such lien will be released within 30 days after the liability is satisfied, becomes unenforceable, or a bond has been accepted as security.

**§40-23-53. Taxpayer Advocate**

This section cross-references §40-2A-4.

**§40-23-54. Appeals**

This section cross-references §40-2B-2.

**§40-23-55. Attorneys’ and accountancy fees**

In all disputes concerning taxes imposed by this chapter, the person engaged in a dispute with the commissioner shall be entitled to reasonable attorneys’ fees, accountancy fees, and other reasonable professional fees incurred in direct relation to the dispute unless the commissioner establishes that its position was substantially justified.

**§40-23-56. Taxpayer rights**

This section cross-references §40-2A-4.

**§40-23-57. Installment agreements; compromises**

This section cross-references §40-2A-4.

**§40-23-58. Bankruptcy**

Two specific cases are provided to protect the taxpayer from the penalties of Section 40-23-45 by providing that under certain circumstances and with respect to a period during which a case is pending under Title 11, United States Code, no addition to the tax shall be made.

**ARTICLE 6—SPECIAL RULES**

The article provides special rules for certain activities: Hobbies, the taxation of gaming services, the taxation of government purchases and of sales by government enterprises, the taxation of mixed use property, and the provisions governing the tax exempt status of nonprofit organizations.

**§40-23-61. Hobby activities**

This section prevents people from using a hobby as if it were a business to take unfair and unintended advantage of the exemption for intermediate sales. The intermediate sales exemption (§40-23-14) and the credits (§40-23-22 or §40-23-23) do not apply to activities not engaged in for profit. An activity is deemed to be “for profit” if it meets the following criteria: The activity has received gross payments for the sale of property/services that are greater than the combined total of taxable goods and services purchased for use in that activity plus wages paid to persons engaging in that activity plus taxes paid (any type of taxes) in at least two of the most recent three years.

Example: If a person spent $5000 on collecting antiques, paid themselves a salary of $10,000 and paid property taxes and consumption taxes of $2000, then, in order for the “collecting antiques” activity to be considered for profit and eligible to purchase goods/services tax free, the “collecting antiques” activity must have received gross payments for the sale of goods/services greater than $17,000. If the collecting antiques activity received payments for sales less than $17,000, it would be considered an activity that is not engaged in for profit. In this case, the person engaged in this activity would not be eligible to purchase goods and services for use in this activity tax free.

**§40-23-62. Gaming activities**

This provision requires those in the gaming business to register. Sales tax is not collected on the purchase of lottery tickets, casino chips, and the like. Instead, a tax is imposed on gaming services at the business level. The tax is paid by the gaming sponsor and must be remitted by the 15th day of each month for the gaming services sold during the prior month. The tax is computed by multiplying 6.0 percent times the gross receipts for gaming services received by the gaming business minus the total gaming payoffs to chance purchasers and minus any other gaming taxes. Example: Off-track betting is a gaming activity. The off-track betting business pays taxes equal to 6.0 percent of its gross receipts for gaming activities minus the prize money paid to winners plus any Federal, State or local gaming taxes.

**§40-23-63. Government purchases**

Purchases by the federal government, state government, and local governments of taxable property and services are subject to the consumption tax. Example: Supplies, furniture, services purchased from independent contractors such as janitorial services and maintenance services, food, uniforms, etc. Government is not charged taxes on the payment of tuition for its employees to attend job related training courses, as all education and training are exempt. For purchases by government enterprises see §40-23-64.

**§40-23-64. Government enterprises**

Government enterprises are governmental entities that receive gross payments from private persons for services. Example: U.S. Post Office, Amtrak, local government garbage collection fees, etc. For a unit of government to be considered a government enterprise, it must maintain books of account separate from the non-enterprise governmental accounts, in accordance with generally accepted accounting principles. All government enterprises whose receipts for services exceed $2,500 per quarter are required to collect the consumption tax on the fees charged for such services.

Government enterprises at the federal, state, and local level are treated the same as private businesses with respect to their purchases and sales to consumers. Their intermediate purchases are not taxed and the sale of goods/services to the consumer is taxed.

The purchase and subsequent transfer of taxable property or services from a government enterprise to other governmental units are taxable. This prevents units of general government from buying property and services through government enterprises to avoid paying the consumption tax on general government purchases.

**§40-23-65. Mixed use property**

Mixed use property or services are taxable property or services purchased both for taxable use or consumption and for a business purpose. An example would include a home office or a car used for both business and personal purposes. Mixed use property or services are subject to the consumption tax unless the property or service is used more than 95 percent for business purposes. For property/services that are used less than 95 percent for business purposes, the property/service is taxed at the time of purchase but a registered person is entitled to a “business use conversion credit.” This credit is equal to the mixed use property amount times the business use ratio times the consumption tax rate. Example: A sole proprietor spends $20,000 for an automobile that he or she uses 80 percent for business purposes and 20 percent for personal purposes. This person is entitled to a business use conversion credit of $20,000 times 80 percent times 6.0 percent ($20,000 x 0.8 x 0.06) or $960.

There are detailed and, unavoidably, somewhat complex rules for calculating the business use portion of mixed use property. For example, the business use ratio is calculated differently for vehicles, real property, and tangible personal property:

1. Vehicles – ratio of business purpose miles to total miles in a particular month
2. Real property – ratio of floor space used primarily for business purposes to total floor space in a particular month
3. Tangible personal property – ratio of the total time used for business purposes to total time used in a particular calendar year
4. Other property or services – the ratio shall be calculated using a reasonable method appropriate to the property or service

Reasonable records must be maintained to support a person’s use of the mixed use property or service. Example: A mileage log documenting business use of a vehicle, the purchase price, and date of purchase. These rules are, however, simpler than the current income tax rules governing the same problem. Those who wish to avoid the application of these rules need to avoid using property for both business and nonbusiness purposes.

Timing of Business Use Conversion Credit Arising Out of Ownership of Mixed Use Property.—A person entitled to a mixed use property or services arising out of the ownership of mixed use property must account for the mixed use on a calendar year basis, and may file for the credit with respect to mixed use property in any month following the calendar year giving rise to the credit. For business use conversion credit, see §40-23-22.

**§40-23-66. Not-for-Profit organizations**

“Qualified not-for-profit organizations” receive favorable tax treatment under the consumption tax. These are organizations that are organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes; as a civic league or social welfare organization; as a labor, agricultural or horticultural organization; as a chamber of commerce, business league, or trade association; or as a fraternal beneficiary society, order, or association. No part of the net earnings of not-for-profit organizations can serve to the benefit of any private shareholder or individual.

Organizations that meet the above criteria are issued a “qualification certificate” upon application to the state consumption tax division (on a form prescribed by the commissioner).

Tithes, dues, contributions, and similar payments to qualified not-for-profit organizations are not considered payments for taxable property or services subject to tax. Individuals make such payments or contributions to qualified not-for-profit organizations tax free.

If churches or not-for-profit organizations provide taxable services at no charge (running a soup kitchen for the poor, for example) these services are not subject to tax. If they provide taxable property or services in connection with contributions, dues or other payments to the organization, then the provision of the taxable property or service is treated as a taxable purchase at the fair market value of the taxable property or services. Example: An organization sells tickets to a dinner to raise funds for the group and charges $100 per ticket which includes a $25 dinner and a $75 donation. The organization has to collect tax on the $25 dinner portion of the ticket. Also, the sale of Bibles by a church is taxable.

The not-for-profit organization is responsible for collecting the tax and filing tax reports to the state consumption tax division. Taxable property and services purchased by a qualified not-for-profit organization “for business purposes” are not taxable. So, in other words, purchases for business purposes are not taxable and sales to consumers are taxable. However, the organization must present its qualification certificate to the seller when making a purchase in order for the sale to be tax exempt.

This is a narrower definition of not-for-profit organization than under current law. For example, the National Football League is not viewed as not-for-profit under the sales tax but is under the income tax.

**ARTICLE 7—FINANCIAL INTERMEDIATION SERVICES**

This article sets forth the provisions for taxing the services of financial institutions, brokers, and so on. In general, the fees charged for their services are taxable. These services have special characteristics which require special provisions to define what is taxable and how the tax is collected.

**§40-23-71. Determination of financial intermediation services amount**

Interest rates may be viewed as having five components: (1) the normal (risk-free) return on capital, (2) the compensation to the lender for the expected loss in purchasing power (inflation) caused by excess money and credit creation, (3) the premium paid for the risk that the capital will not be repaid, (4) the compensation to the lender for taxes due on the interest, and (5) the payment for financial intermediation services – the servicing of the loan or deposit. Item (4) is no longer relevant since income taxes are repealed and the consumption tax does not tax interest. The consumption tax does tax the last component (5) of interest which is the implicit payment for financial intermediation services. This is not simple. Although some financial intermediation services are explicitly charged, in practice they may be incorporated into the interest paid. Similarly, insurance premiums have a financial intermediation services component. Under the consumption tax, financial intermediation services purchased by consumers are taxable services, while financial intermediation services purchased by businesses are exempt as business inputs.

The term “financial intermediation services” means the sum of explicitly charged fees for financial intermediation services and implicitly charged fees for financial intermediation services.

“Explicit” means fully revealed, leaving no question as to meaning or intent. Explicitly charged fees for financial intermediation services include brokerage fees; explicitly stated banking, loan origination, processing, documentation, credit check fees or other similar fees; safe-deposit box fees; insurance premiums, to the extent such premiums are not allocable to the investment account of the underlying insurance policy; trustees' fees; and other financial services fees (including, but not limited to, mutual fund management, sales, and exit fees). All explicitly charged fees for financial intermediation services are taxable to the consumer and are not taxable when they are for business purposes.

“Implicit” means involved in the nature or essence of something though not revealed. Implicitly charged fees for financial intermediation services include any service charges or fees, the cost of which is rolled into the interest rate rather than stated separately. The most common and obvious example is a “free” checking account that pays little or no interest on balances held in the account.

The consumption tax calculates the amount of financial intermediation services by determining the gross imputed amount in relation to any underlying interest-bearing investment, account or debt. The term “gross imputed amount” equals the excess (if any) of the basic interest rate over the rate paid on such investment multiplied by the account balance; and with respect to any underlying interest-bearing debt, the excess (if any) of the rate paid on such debt over the basic interest rate multiplied by the debt balance. The basic interest rate is the applicable interest rate (i.e., the federal borrowing rate for like-term instruments).

The consumption tax is not imposed on the risk premium (item (3) above) because lenders get a credit equal to the consumption tax rate times their bad debts.

Example: For a 30-year fixed rate home mortgage, the measure of the taxable financial intermediation services is the mortgage interest rate minus the interest rate for a 30-year Treasury obligation (which represents the price of items (1) and (2) above) times the mortgage balance. Example: For a checking account that pays no interest, the measure of taxable financial intermediation services is the interest rate on short-term Treasury obligations times the average daily deposit during the month.

**§40-23-72. Bad debts**

This section provides the definition of bad debts for which a credit can be taken under §40-23-25 BAD DEBT CREDIT. A bad debt is a business loan or debt that becomes wholly or partially worthless. A business loan or debt is a bona fide loan or debt made for a business purpose that both parties intended be repaid. No loan or debt shall be considered wholly or partially worthless unless it has been in arrears for 180 days or more unless a debt is discharged wholly or partially in bankruptcy before 180 days has elapsed. A loan or debt that has been in arrears for 180 days or more may be deemed wholly or partially worthless by the holder unless a payment schedule has been entered into between the debtor and the lender.

**§40-23-73. Timing of tax on financial intermediation services**

To simplify compliance, the consumption tax on financial intermediation services provided in connection to an underlying investment account or debt is calculated and collected with the same frequency that statements are rendered by the financial institution in connection with the investment account or debt but not less frequently than quarterly. Example: The sales tax on a monthly checking account fee is charged on each monthly statement.

**§40-23-74. Financing leases**

This section defines financing lease as any lease under which the lessee has the right to acquire the property for 50 percent or less of its fair market value at the end of the lease term. Except where previously taxed, this section sets out the rules for disaggregating the principal and interest components of the lease, with the principal component subject to tax as if a purchase in the amount of the principal component had been made on the day on which said lease was executed and the interest component taxed pursuant to the financial intermediation services tax under this chapter.

**§40-23-75. Basic interest rate**

The basic interest rate with respect to a debt instrument, investment, financing lease, or account shall be the applicable interest rate as determined in §40-23-50. For contractually fixed interest, the applicable interest rate of the month of issuance shall apply. For variable interest rates and which have no reference interest rate, the applicable interest shall be the Federal short-term interest rate for each month. For variable interest rates and which have a reference interest rate, the applicable interest shall be the applicable interest rate for the reference interest rate for each month.

**§40-23-76. Out-of-state financial intermediation services**

Any out-of-state person who provides financial intermediation services to Alabama residents must, as a condition of lawfully providing such services, designate, in a form prescribed by the commissioner, a tax representative for purposes of this chapter. The tax representative shall be responsible for ensuring that the taxes imposed by this chapter are collected and remitted and shall be jointly and severally liable for collecting and remitting these taxes.

**ARTICLE 8—Additional Matters**

Various anti-avoidance rules, de minimis payments exceptions, employee discounts, timeliness of reports and other actions, transition matters and phase-out of administration of repealed taxes are provided in this article.

**§40-23-81. Additional matters**

The sale of a copyright or trademark is treated as the sale of taxable services and subject to taxation if the substance of the sales of copyright or trademark constituted the sale of the services that produced the copyrighted material or the trademark.

**De minimis payments.** Up to $1,000 of gross payments per calendar year shall be exempt from the tax imposed by this chapter if made by a person not in connection with a trade or business at any time during such calendar year prior to making said gross payments and made to purchase any taxable property or service which is brought into Alabama by such person for use or consumption by such person in Alabama.

Up to $5,000 per calendar year of gross payments shall be exempt from the tax imposed by this chapter if received by a person not in connection with a trade or business during such calendar year prior to the receipt of said gross payments and in connection with a casual or isolated sale.

Up to $10,000 per calendar year of gross payments received by a person from the sale of financial intermediation services shall be exempt from the tax imposed by this chapter.

If a registered person provides taxable property or services to a person either as a gift, prize, reward, or as remuneration for employment, and such taxable property or services were not previously subject to tax, then the provision of such taxable property or services by the registered person shall be deemed the conversion of such taxable property or services to personal use subject to tax at the tax inclusive fair market value of such taxable property or services. Example: A business person gives his/her employees a Christmas present. If he/she purchased those gifts as business expenses and did not pay the consumption tax, then giving the presents to his/her employees is converting the presents to personal use. The business owes the tax on the gifts. The business is required to remit the tax.

The substance of a transaction will prevail over its form if the transaction has no bona fide economic purpose and is designed to evade tax imposed by this chapter.

**Employee discounts.** In addition, employer-provided employee discounts over 20 percent are taxable. The term “employee discount” means an employer’s offer of taxable property or services for sale to its employees or their families for less than the offer of such taxable property or services to the general public. If the employee discount amount exceeds 20 percent of the price that the taxable property or services would have been sold to the general public, then the sale of such taxable property or services by the employer shall be deemed the conversion of such taxable property or services to personal use and tax shall be imposed on the taxable employee discount amount. The taxable employee discount amount shall be the employee discount amount, minus 20 percent of the amount for which said taxable property or services would have been sold to the general public.

**Timeliness of reports or other required actions.** If a report or other action is due on a Saturday, Sunday or legal holiday, the report or action is considered timely if it is performed on the next day which is not a Saturday, Sunday, or legal holiday (in the jurisdiction where the return is to be filed).

**§40-23-82. Transition matters**

This section covers the handling of inventory and work-in-progress as of close of business on December 31, 2017. In general, such inventory qualifies for a “transitional inventory credit” if sold before December 31, 2019. The credit will be the tax rate times the cost of the inventory as of close of business on December 31, 2017.

Businesses that have inventory on the close of business December 31, 2017qualify for a transitional consumption tax credit if the inventory is sold subject to the consumption tax and prior to December 31, 2017.

Qualified inventory shall have the cost that it had for Federal income tax purposes for the trade or business as of December 31, 2017 (including any amounts capitalized by reason of section 263A of the Internal Revenue Code of 1986 as in effect on December 31, 2017). The transitional inventory credit belongs to the trade or business which held the qualified inventory on the close of business on December 31, 2017, and is entitled to a transitional inventory credit equal to the cost of the qualified inventory (as determined immediately above) times the rate of tax imposed by Section 40-23-13.

Businesses may sell the right to receive the credit, so the credit can follow qualified inventory through the supply chain. Qualified inventory includes work in process.

A business entitled to the transitional inventory credit may sell the right to receive the credit to the purchaser of the qualified inventory. Example: A wholesaler who purchased inventory before the consumption tax went into effect can sell the right to receive the credit to the retailer who buys that inventory. The retailer can then claim the credit as he sells that inventory to consumers (as described above).

Lastly, there may have arisen a question about the tax implementation based on the "transitional inventory credit" which applies to all "qualified inventory," including "work in progress," that existed on the date preceding the effective date of the sales tax. Such inventory may be sold throughout the year following the effective date and a credit may be taken by the retailer for the sale until the product is exhausted or the year has lapsed. For example, let's say on 31 December a specific widget is sold by retailer "B" for $1 and the next day, 1 Jan, the sales tax becomes effective. Assuming no other economic impact occurs to cause a price increase in the widgets, the store can continue to sell the widget for $1. This now becomes the "gross payment" for the widget which is inclusive of the product price and the 6.0% consumption tax. The retailer will then submit his monthly sales tax report to the state administering authority which will include the 6.0% tax due on the sale of the widgets followed by a credit of 6.0 %, thus no taxes due on the widget sales and the retailer keeps his $1 for each of the widgets he sold. Another example. If manufacturing company "A" had a widget being manufactured on the assembly line before the effective date which was then sold to retailer "B" after the effective date, the same rule applies. Retailer "B" purchases the widget from the manufacturer as an "intermediate sale" (business-to-business), thus no taxes due, and then retailer "B" sales it to the final consumer for the same price as before, $1. This assumes the manufacturer sells it wholesale to the retailer at the same price as before the effective date. Once the in-work inventory and retailer's inventory is exhausted, or the second year has lapsed, whichever comes first, then the tax is applied to the sales price as set by both manufacturer and retailer. The transitional inventory credit expires at the end of the first year the sales tax is in effect.

The transition credit supports the assertion that products produced and sold under the current tax code are loaded with embedded state taxes that have been cascaded through the production and final sale process, thus they should not be taxed again. Lastly, though not potentially all the reasons, the credit indirectly allows for a transitional period for production and retail to adjust to pricing without the inclusion of income taxes, corporate taxes, and compliance costs that before the consumption tax was a large percentage of the cost passed along to the consumer. This means being able to keep some prices the same immediately after the effective date and then change prices over time consistent with new-found production and retail savings as tax burdens are lifted.

**§40-23-83. Phase-out of administration of repealed taxes**

This section ends appropriations for any Department of Revenue expenses related to taxes repealed by this act on September 30, 2020 and all records related to administration of taxes repealed by this act shall be destroyed by September 30, 2020, except those necessary to support ongoing litigation.

SEC. 5. CONFORMING AMENDMENTS

Sec. a. Alabama Code Title 40, Revenue and Taxation , Department of Revenue §40-2-25 is repealed. Removes income tax audits and examinations.

Sec. b. Alabama Code Title 40, Revenue and Taxation , Rights of the Tax Payer §40-2A-4(b)(1)(a) is amended and concerns the Taxpayer Advocate’s authority and review of Taxpayer Advocate’s issue of taxpayer assistance orders.

Sec. c. Alabama Code Title 40, Revenue and Taxation, Rights of the Tax Payer §40-2A-4 is amended by adding a new subsection (e) and which provides for confidentiality of all reports and report information provided to the commissioner pursuant to this Title. This section also outlines to whom such information may be provided. These confidentiality rights may be waived.

Sec. d. Alabama Code Title 40, Revenue and Taxation, Department of Revenue §40-2A-17 is repealed. Removes income tax evasion statute that is no longer required.

Sec. e. Alabama Code Title 40, Revenue and Taxation, Department of Revenue §40-2A-18 is amended by adding the following sentence at the end thereof:

 “Interest on amounts due to, or owed by, the Commissioner pursuant to chapter 23 shall be governed by chapter 23.”

Sec. f. A new §40-5-48 is enacted as follows:

Section 40-5-48, Resolution of Conflicts.

Whenever chapter 23 is inconsistent with this chapter, chapter 23 shall govern with respect to the administration and collection of the taxes imposed by chapter 23.

Sec. g. A new §40-29-122 is enacted as follows:

Section 40-29-122, Resolution of Conflicts.

Whenever chapter 23 is inconsistent with this chapter, chapter 23 shall govern with respect to the administration and collection of the taxes imposed by chapter 23.