

Texas Comptroller Revises Policy on Temporary Credit for Business Loss Carryforwards

Overview

On June 30, 2017, the Texas Comptroller of Public Accounts ("Comptroller") released guidance (hereinafter referred to as "Comptroller Letter") indicating that two existing policies related to the temporary credit for business loss carryforwards¹ (hereinafter referred to as "the credit") would be revised.² In this Tax Alert, we summarize the existing regulatory and statutory guidance affecting the credit, the guidance provided in the Comptroller Letter and provide some taxpayer considerations.

Policy Revision 1 – Ability to Utilize Credit on Subsequent Reports

Under Texas Tax Code ("TTC") § 171.111, taxable entities are permitted to utilize the credit by notifying the Comptroller in writing of an intent to take the credit on the first report due. In addition to the statutory requirements for calculating and utilizing the credit, Title 34 of the Texas Administrative Code § 3.594(e) ("Rule 3.594") requires taxable entities to make an annual election on a timely filed report to claim the credit. Under its current language, Rule 3.594 provides that a temporary credit is lost and cannot be carried over to a subsequent year if the report on which the election to utilize the credit is made is not timely filed each year.

However, a recently released Comptroller's Decision found that Rule 3.594(e) adds additional requirements to the clear and unambiguous provisions of TTC § 171.111 and is, therefore, invalid.³ As explained in the Comptroller's Letter, "[b]ecause the statute does not require an annual election, the Comptroller cannot add such a requirement by rule."⁴ In addition, the Comptroller's Decision found no statutory basis for disallowing a credit claimed on a late-filed report.⁵ As such, the filing of a timely return is not a statutory condition for taking the credit.⁶

Under the revised Comptroller policy, once a taxable entity has taken the credit on a timely filed report, the taxable entity may claim the credit on any subsequent report, even if the subsequent report is not timely filed. For report years after the credit is initially taken on a timely filed report, a taxable entity may amend any late-filed reports to take a credit not previously claimed or allowed, if the report is within the statute of limitations for refunds. If the report is beyond the statute of limitations, a taxable entity may carryover the credit not previously claimed or allowed. The Comptroller's Letter indicates that Rule 3.594 and any other affected Comptroller guidance will be amended to reflect this revised policy.⁷

Policy Revision 2 – Ability for Combined Group to Utilize Credit of Departing Group Member

Under TTC § 171.111(d), a taxable entity may not convey, assign, or transfer a credit. In addition, a taxable entity may not claim the credit if it "changes combined groups."⁸ The statute does not specify the reporting period when the entity's credit is lost. However, Rule 3.594 provides that when a member entity leaves a combined group, the group cannot claim any of the entity's credit on the report that is based on the accounting period when the entity leaves the group.

¹ As part of the transition from the old Texas franchise tax to the new margin tax in 2008, taxpayers were permitted to convert existing business loss carryforwards (i.e., apportioned net operating losses) to a temporary credit. Eligible taxpayers are able to utilize the credit over a 20-year period. See Tex. Tax Code § 171.111.

² Texas Comptroller of Public Accounts, Accession No. 201706006L (June 30, 2017), available [here](#) (hereinafter referred to as "Comptroller Letter - Accession No. 201706006L").

³ SOAH Docket No. 304-15-0575.13, CPA Hearing No. 110,191, Accession No. 201506219H (June 24, 2015), available [here](#) (hereinafter referred to as "Recent Comptroller Decision - Accession No. 201506219H").

⁴ Comptroller Letter - Accession No. 201706006L.

⁵ Recent Comptroller Decision - Accession No. 201506219H.

⁶ Comptroller Letter - Accession No. 201706006L.

⁷ *Id.*

⁸ Tex. Tax Code § 171.111(d).

External Multistate Tax Alert

Under the revised Comptroller policy, if a member entity leaves a combined group during the accounting period on which a report is based, the combined group may claim, subject to credit limitations, the entire amount of the departing member's credit that is available for that report year, along with any of that member's available credit carryover for the report year at issue.⁹ For subsequent reports, the departed member's credit is no longer available to the combined group, consistent with the current credit policy.¹⁰ If a credit from a departing member was previously excluded for the accounting period on which the combined group's report was based, a combined group may file an amended franchise tax report to claim the credit of a member entity that left the combined group, within the statute of limitations for refunds. The Comptroller's Letter indicates Rule 3.594 and any other affected Comptroller guidance will be amended to reflect this policy.¹¹

Considerations

Taxpayers that have excluded the credit for previous report years based on the Comptroller's prior policy may wish to consult with a Texas tax specialist in order to determine if an amended return should be filed to properly utilize the credit. Taxable entities considering filing an amended report should keep in mind that the statute of limitations for franchise tax reports filed in 2013 could potentially expire this year.¹²

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⁹ For numerical examples on application of revised policy surrounding the credit, see Comptroller Letter - Accession No. 201706006L.

¹⁰ See Tex. Tax Code § 171.111(d).

¹¹ Comptroller Letter - Accession No. 201706006L.

¹² Generally, a refund claim must be made within the period during which the Comptroller may assess a deficiency for the tax, which is typically four years from the date the tax becomes due and payable, including extensions of time based on the filing of a valid extension. See Tex. Tax Code §§ 111.104, 111.107(a), 111.201. For example, the statute of limitations for filing a refund claim related to a Report Year 2013 filing that was properly extended to and filed on or before November 15, 2013, would potentially close on November 15, 2017.

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