

Income/Franchise:

Texas Appellate Court Says Only Net Proceeds from Hedging Transactions Includable in Sales Factor

Case No. 03-21-00011-CV, Tex. Ct. App. (10/14/21). A Texas Court of Appeals (Court) affirmed a previously issued Texas District Court ruling that only the net proceeds, rather than gross proceeds, from a company's sales of commodity futures were includable in the company's apportionment factor denominator for Texas franchise tax purposes, and thus the taxpayer was *not* entitled to a refund of taxes paid. During the report years at issue, the company filed combined Texas franchise tax reports that included a wholly-owned subsidiary that bought and sold commodity futures to manage the risks associated with potential fluctuations in the value of the company's inventory along with the crude oil the company refined to produce inventory ultimately sold to its customers. In its holding, the Court:

URL: <https://search.txcourts.gov/SearchMedia.aspx?MediaVersionID=36216e3f-5f52-4110-8057-6ae353cade0f>

1. Explained the company had conceded its "non-inventory securities" did not constitute "inventory of the seller" for federal income tax purposes; and
2. Rejected the company's claim that the securities fell within the scope of Texas Tax Code section 171.106(f) because it made an election under Internal Revenue Code section 475(e) and section 475(f), which permitted the company to apply mark-to-market accounting to the securities.

See forthcoming Multistate Tax Alert for more details on this recent opinion, including related taxpayer considerations, and please contact us with any questions in the meantime.

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