

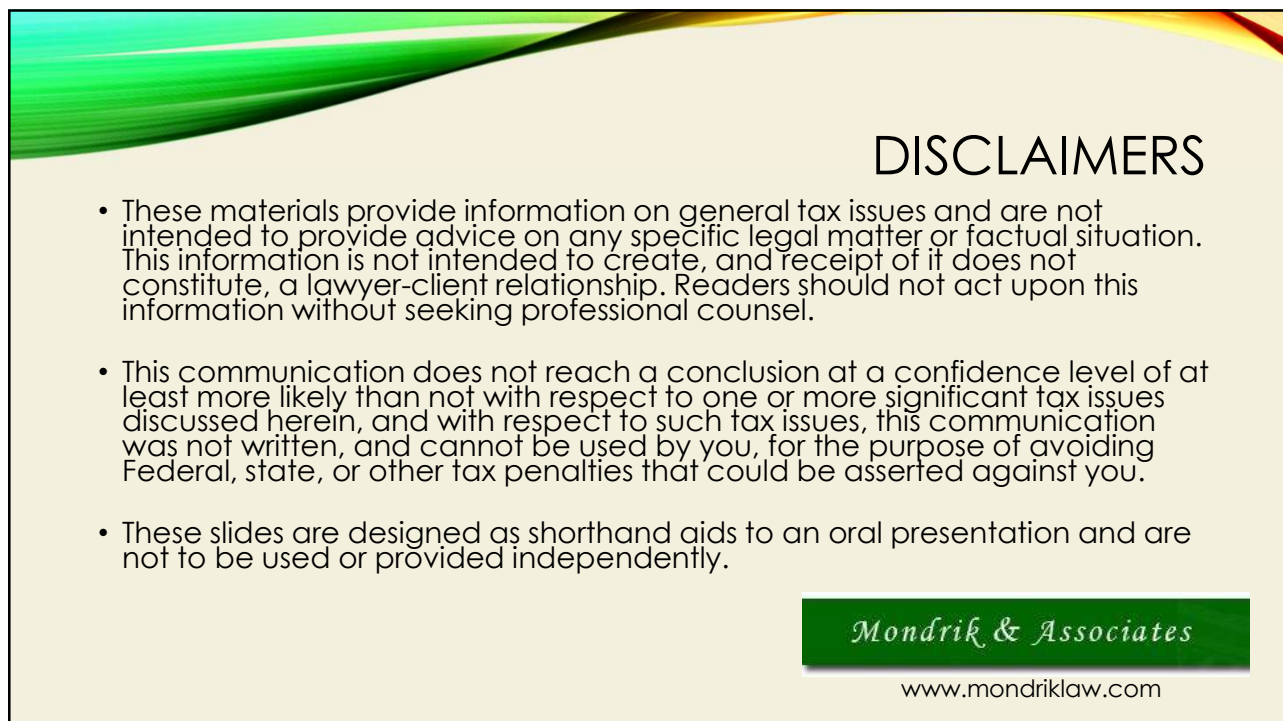
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SALT UPDATES:

What CPAs Need to Know About State and Local Tax

Christi Mondrik, CPA, Esq. TBLS Board Certified – Tax Law
TXCPA Austin Annual Tax Conference ~ November 12, 2025

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DISCLAIMERS

- These materials provide information on general tax issues and are not intended to provide advice on any specific legal matter or factual situation. This information is not intended to create, and receipt of it does not constitute, a lawyer-client relationship. Readers should not act upon this information without seeking professional counsel.
- This communication does not reach a conclusion at a confidence level of at least more likely than not with respect to one or more significant tax issues discussed herein, and with respect to such tax issues, this communication was not written, and cannot be used by you, for the purpose of avoiding Federal, state, or other tax penalties that could be asserted against you.
- These slides are designed as shorthand aids to an oral presentation and are not to be used or provided independently.

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AGENDA

- Texas Legislative and Case Law Updates
- Franchise Tax R&D Credit
- Manufacturing Exemption
- Data Processing Rule
- Administrative Updates
- Texas SALT Litigation Options

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TEXAS LEGISLATIVE UPDATE

- 89th Legislative session <https://capitol.texas.gov/> (Texas Legislature Online)
- Constitutional prohibition of "death taxes" → referendum passed on ballot (HJR 2)
- Evidentiary requirements Texas Tax Code § § 111.041(c), 112.052(d), 112.202 (SB 266)
 - Contemporaneous evidence → Sufficient evidence
- Penalties
 - Additional 10% penalty waived if timely lawsuit filed
- State tax lien alternatives
 - Posting a bond or cash deposit

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FRANCHISE TAX R&D

- New legislation effective January 1, 2026 (SB 2206)
- Franchise tax research and development credit – no more sales tax exemption
- Credit ranges from 4.361% to 10.903%
- Varies based on prior expenses and collaborations
- Refundable option for entities owing no tax

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FRANCHISE TAX R&D

- Qualified Research Expense: References the portion of Form 6765, line 48 attributable to research conducted in Texas
- Amount of Credit: 8.722% of the difference between:
 - Qualified Research Expenses incurred during report period and
 - 50% of average Qualified research expenses during prior three years
- Public or private higher education institution partnership: 10.903% of the difference between:
 - Qualified Research Expenses incurred during report period and
 - 50% of average Qualified research expenses during prior three years
- If no prior three years use 4.361%

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FRANCHISE TAX R&D

- Credit for Certain Taxable Entities that Owe No Tax
 - Apply the same calculation to compute expenses
 - Refundable credit
- Combined Reporting – Must be claimed on combined group report
- Tiered Reporting – Upper tier may claim credit for qualified research expenses incurred by lower tier entity to the extent of upper tier entity's ownership

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FRANCHISE TAX R&D

- Limitation: Credit may not exceed 50% of amount of tax due for the report before other applicable credits
- Carryforward: Unused credit may carry forward for up to 20 consecutive reports
- Ordering of R&D credits:
 - Subchapter O credits (repealed 1/1/2008)
 - Subchapter M credits (repealed 1/1/2026)
 - Credit carryforward under new subchapter (effective 1/1/2026)
 - Current year credit
- Assignment of credits is prohibited

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FRANCHISE TAX R&D

- Memo 202503003M (3/24/2025): IRC Sec. 41(b)(2)(C) excludes depreciable property. Even if an expense is deductible under IRC Sec. 174 depreciable property does not qualify as a "supply" for Franchise Tax R&D Credit
- Memo 202503004M (3/24/2025): Federal intra-group transaction rules do not apply when determining the Texas R&D Credit (or exemption). Qualified research , under existing law, references IRC in effect on December 31, 2011.
 - Federal law – Because all members of a group under common control are treated as a single taxpayer for purposes of determining the research credit, transfers between members of the group are generally disregarded
 - Franchise tax – Members of a combined group shall be treated as a single taxpayer.
 - Sales tax – Each person (entity) is a single taxpayer.

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FRANCHISE TAX LEGISLATION

- New Franchise tax Strong Families Credit (SB 2018)
 - Designated contributions to eligible organizations for comprehensive case management for at-risk families and services assisting fathers in learning and improving parenting skills
- COGS for television or radio broadcasters (SB 263)
- Revenue exclusions for registered securities market operators (SB 1058)
- Reduced franchise tax rate for industrial linens, garments, uniforms (SB 2774)
- Broadband grant recipients (SB 1405)

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FRANCHISE TAX POLICY

- Sales of bitcoin (Comptroller Letter No. 202506007L PLR)
 - Bitcoin determined to be an intangible for franchise tax purposes
 - No COGS
 - Apportionment: Sourced by location of payor rule

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NUSTAR ENERGY, LP v. HEGAR

- Appealed to Texas Supreme Court
- Oral argument September 10, 2025
- Issue: Gross receipts apportionment
- Place of transfer v. purchaser's location
- Texas Tax Code § 171.1055: "delivered or shipped to a buyer in this state"
- Rule: 3.591
- Taxpayer's argument is that "in this state" refers to "buyer"
- Fuel delivered in Texas waters and used elsewhere

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TEXAS LEGISLATIVE UPDATE

- Internet access services removed from taxable service list (SB 1405)
 - Texas Tax Code Sec. 151.0101
 - Internet Tax Freedom Act grandfathered states already charging tax on internet access fees through June 30, 2000.
- Sales and use tax agricultural exemption for exotic and game animals (HB 135)

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EXEMPT GOVERNMENT

- Texas Supreme Court: *GEO Group v. Hegar*, 709 S.W.3d 585 (Tex. 2025)
- Burden of proof: preponderance of the evidence
 - Contrast with “clear and convincing” at administrative level
- Government contractor was not an “unincorporated instrumentality of the government” under Rule 3.322(c)
 - For-profit entity
 - Arm of the government v. vendor
- Sales tax exemption did not apply

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SALES AND USE TAX MANUFACTURING EXEMPTION

- *Sabine Mining Co., v. Combs*
 - Draglines not exempt
 - No direct physical or chemical change to coal
 - Draglines removed overburden and exposed coal to elements
- *Hegar v. Texas Westmoreland Coal Co.*
 - Excavators dug coal from hillside and dropped into trucks
 - Direct chemical or physical change to product being manufactured for sale
 - Manufacturing exemption applies to sales of tangible personal property
 - Raw materials need not start as tangible personal property

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SALES AND USE TAX MANUFACTURING EXEMPTION

- Comptroller Letter No. 202506001M (June 13, 2025):
 - Excavators, stone-cutting tools, and explosive qualify for tax exemption if they cause a chemical or physical change in severing materials from the earth.
 - Transportation equipment is still taxable.
 - Prior policy: Unprocessed materials (e.g., sand and gravel) were not subject to sales and use tax; Processed materials (altered by crushing, cutting or mixing) were taxable.
 - New policy effective 10/1/2025: previously nontaxable materials may be treated as taxable because they were extracted from the earth and/or wash, dried, or separated in a manner that caused a chemical or physical change.
 - Credits for tax paid in error.
 - Divergent use of manufacturing equipment.
 - Many prior letters and hearings superseded.
- Oct. 2025 Tax Policy News – implementation indefinitely delayed

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AMENDED RULE 3.330 DATA PROCESSING

- Revised April 2, 2025, with certain parts enforceable October 1, 2025
- Ancillary services v. "essence of the transaction"
- Sourcing of transactions and burden of proof
- Professional services exclusions
- Effective 10/1/2025 marketplace provider services may be included in taxable data processing
- Excluded: Internet, streaming video, video games, etc.

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TEXAS SALES AND USE TAX

- Fuel Discount App (Comptroller Letter No. 202508025L PLR)
 - Charges for app providing fuel discounts to truck drivers involved data compilation, data manipulation, and information storage
 - Fuel stops paid a percentage-based fee of fuel sold
 - Ruled taxable data processing (20% exemption)
- Merchant Credit and Debit Card Processing
 - 2021 legislative session
 - Fees for settling electronic payment transaction
 - Payment Card Industry Security Standards Council
 - Settling of electronic payment transactions
- Credit Rating Services deemed taxable
 - Comptroller Policy Memo No. 202302004L
 - Effective August 1, 2024

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TEXAS SALES AND USE TAX

- Sales Price and Credit Card Processing Fees (Memo 202406004M June 27, 2024)
 - Separately-stated credit card processing fees are part of the retailers' sales price
- Residual fees from credit card processors nontaxable (PLR 20210226061035)
 - Fees paid for referrals
- Pre-authorization services nontaxable (PLR 20230615102809)
 - Using proprietary software to process pre-authorization requests submitted by medical providers for insurance provider's healthcare plans

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TEXAS SALES AND USE TAX

- Staffing Services to Hotels (Comptroller Letter No. 202506015L PLR)
 - Temporary help services (SB 745, eff. 9/1/2017) exclusion → exemption
- Factors:
 - Services client normally performs
 - Client provides supplies
 - Client supervises work
 - Seasonal or temporary
- Comptroller denied exemption
 - Agreements did not specify end dates
 - Client did not maintain adequate workforce
 - Services fit category of taxable services

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TEXAS SALES AND USE TAX

- Service v. Rental of Equipment (Comptroller Letter No. 202506016L PLR)
 - Charge for equipment used to triage wireless phones and devices
 - Equipment supplier set up equipment for client at client's location
 - Supplier provided on-site technicians to activate and deactivate equipment
 - Beginning and end of each shift
 - Client used devices to test wireless devices (new, damaged beyond repair, defective, or eligible for recycling)
 - Ruling: Operational control transferred to customer
 - Taxable rental, rather than nontaxable service

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ADMINISTRATIVE DEVELOPMENTS

- Kelly Hancock appointed Acting Texas Comptroller of Public Accounts
 - Effective July 1, 2025
- Next election will determine Texas Comptroller of Public Accounts
- October 2025 Tax Policy News: Items being removed from STAR:
 - Tax Policy News (published elsewhere, but removing >4 years old)
 - Superseded administrative rules

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ADMINISTRATIVE DEVELOPMENTS

- Buying Existing Business Publication Revised
- Joint Certificate of No Tax Due
- Franchise tax COGS for logging and timber operator

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JOINT REQUEST FOR CERTIFICATE OF NO TAX DUE

High Risk Name of Purchaser: _____ High Risk Name of Seller: _____

Address: _____ Date: _____ ZIP code: _____

Phone number (Area code and number): _____ (Alt number (Area code and number): _____) Email address: _____

High Risk Name of Seller: _____ High Risk Name of Purchaser: _____

Address: _____ Date: _____ ZIP code: _____

Phone number (Area code and number): _____ (Alt number (Area code and number): _____) Email address: _____

High Risk Name of Seller: _____ High Risk Name of Seller: _____

Address: _____ Date: _____ ZIP code: _____

Phone number (Area code and number): _____ (Alt number (Area code and number): _____) Email address: _____

Purchaser and Seller are actively engaged in negotiations for the purchase/sale of the business or the stock of goods of the business of Seller to Purchaser. Purchaser and Seller request that the comptroller issue a certificate stating that no tax is currently due to the Seller or issue a statement of the amount required to be paid before such a certificate may be issued pursuant to Texas Tax Code section 111.020(c). Purchaser and Seller further request that a copy of such certificate or statement be provided to the County Agent identified below.

For the Purchaser: _____

For the Seller: _____

Each Certificate of No Tax Due is tax specific. All state taxes for which the business is permitted or otherwise determined to be liable will be reviewed and subject to audit. Each tax for which the business is permitted or otherwise determined to be liable will be addressed separately, but only one request is required.

Only the Purchaser identified above may rely upon the certificate or statement issued in response to this request. Such reliance may not be transferred or assigned. Each prospective purchaser must submit a separate request.

Submit the completed form to the comptroller by emailing it to entdg@cpa.texas.gov or faxing it to 512-475-0349

This form complies with Chapters 202 and 203, Government Code, to require, request and correct information we have on file about you. Contact us at 800.544.7914 or Texas Comptroller of Public Accounts, P.O. Box 13088, Austin, TX 78713-0808.

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ADMINISTRATIVE OPTIONS

- Texas Notification of Audit Results
- Redetermination
- Oral Hearing / Written Submissions
- Refund Claims

CONTESTING DISAGREED AUDITS, EXAMINATIONS AND REFUND DENIALS

At the Comptroller's office, we want to be fair and give taxpayers full consideration in every case. This publication explains how to exercise your rights as a taxpayer if you disagree with the Comptroller's position in your audit, examination or refund verification.

YOUR OPTIONS BEFORE RECEIVING A TEXAS NOTIFICATION OF AUDIT OR EXAM RESULTS

We encourage you to provide all records and information requested by the auditor, and to work with the auditor to resolve disagreements as they arise. You can speak with the auditor's supervisor or manager at any time during the process. If you cannot resolve your disagreements in this manner, you have the following options:

RECONCILIATION CONFERENCE

You can ask for a reconciliation conference with the audit supervisor or manager to discuss and attempt to resolve disagreements. This informal conference can be held at either your location or the audit office.

REQUESTING TAXABILITY GUIDANCE

During the course of the audit, examination or refund verification, you and the auditor can ask the Tax Policy Division for taxability guidance on an agreed set of facts.

To request taxability guidance from Tax Policy, work with the auditor to prepare a document that outlines the taxability issue and requests guidance. Tax Policy can only provide assistance when you and the auditor agree on the underlying facts. The auditor will submit that document through Audit Headquarters to Tax Policy. Tax Policy will respond to the auditor, who will share the findings with you.



If Tax Policy issues a written taxability determination, you cannot have an Independent Audit Review Conference (IARC) on the same subject.

INDEPENDENT AUDIT REVIEW CONFERENCE

If disagreed issues remain after the reconciliation conference, you can request an IARC.

The IARC allows you to meet with a person who has not been involved in the audit, examination or refund verification process to attempt to resolve disagreed issues. The IARC is an informal meeting between you, the auditor, and an Independent Audit Reviewer (IAR). The IAR will conduct the meeting by asking questions of both you and the auditor to gather information. Matters that can be

MARCH 2025



Glenn Hegar
Texas Comptroller of
Public Accounts

At the Comptroller's office, we want to be fair and give taxpayers full consideration in every case. This publication explains how to exercise your rights as a taxpayer if you disagree with the results of your audit.

FOR MORE INFORMATION,
VISIT OUR WEBSITE AT
Comptroller.Texas.gov

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TEXAS SALT LITIGATION OPTIONS

- Protest Lawsuits
 - Pay tax, penalty, and interest under protest
 - Protest letter and protest lawsuit
- Lawsuits after redetermination
 - Taxpayer must go through redetermination process first
 - Decision identifies contested / uncontested portion
 - Uncontested portion must be paid to prevent collection

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TEXAS SALT LITIGATION OPTIONS

- Refund Claim Administrative Bypass
 - New form issued when refund claim is denied (60-day deadline)
 - Request administrative hearing on refund claim by filing a Statement of Grounds
 - File Notice of Intent to Bypass the Hearing (may require conference)
- Both options must assert
 - The material facts
 - Each specific legal basis on which the refund is claimed
 - The dollar amount of the claim

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TEXAS SALT LITIGATION OPTIONS

- New bypass procedures for managed audits
- Request managed audit within 60 days of audit notification
- Qualifications
- Signed agreement
- Penalty and interest waiver
- Samples, scheduling, and timelines apply

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