

Texas – Reimbursed costs not included in total revenue

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In brief

A taxpayer was not required to include fuel surcharge reimbursements in its Texas franchise tax calculation of total revenue. The Comptroller determined that the taxpayer properly excluded such reimbursements from its *federal* gross receipts because they: (1) constituted ordinary and necessary business expenses under I.R.C. § 162 and (2) were reasonably expected to be repaid by customers at the time the expenses were incurred. Because the fuel surcharge reimbursements were properly excluded from federal gross receipts, they were not included in the taxpayer's computation of total revenue for Texas franchise tax purposes. [Texas Comptroller Ruling [201404021H](#) (12/4/14, released February 2015)]

In detail

During the period at issue, Taxpayer was a transportation company that transported freight on a contract basis. Taxpayer charged and collected from its customers a reimbursement of fuel costs (the 'fuel surcharge') that exceeded a 'floor' level of fuel costs. Such amounts were separately stated on invoices to customers.

For Texas franchise tax purposes, 'total revenue' includes amounts reported on Form 1120, line 1c. Texas Tax Code § 171.1011(c). Taxpayer included fuel surcharge reimbursements in its 2008 federal corporate tax return (Form 1120, line 1c and in deductible expenses) and in its 2009 Texas franchise tax 'total revenue' calculation.

Following the filing of its amended 2008 federal corporate tax return that removed the fuel surcharge reimbursement from line 1c, Taxpayer filed an amended 2009 Texas franchise tax return that removed the fuel surcharge reimbursement from its 'total revenue' calculation and requested a refund.

The Tax Division denied the refund claim and Taxpayer appealed to the State Office of Administrative Hearings where an administrative law judge (ALJ) ruled in favor of Taxpayer. The Texas Comptroller reviewed the ALJ's decision and ruled as follows.

The fuel surcharge

The Comptroller acknowledged that a fuel surcharge allows

carriers to recover excess fuel costs on a dollar-by-dollar basis during periods of high fluctuation in fuel prices. The surcharge is within the transportation industry's normal practice. There is no markup in the calculation of Taxpayer's fuel surcharge.

Other reimbursed costs

Taxpayer pays certain 'accessorial fees' upfront and then invoices its customers for reimbursement. Such charges include lumper fees, stop-off fees, escort fees, and shuttle fees. Taxpayer did not include such charges within its Texas 'total revenue' computation. The Tax Division did not contest Taxpayer's treatment.

Amounts excluded from federal revenue are excluded from Texas total revenue

The Comptroller recognized that Texas franchise tax 'total revenue' is computed using amounts reported as income on federal Form 1120, line 1c, "to the extent the amount entered complies with federal income tax law." Accordingly, the dispute in this case turned on whether the fuel surcharge reimbursements excluded from line 1c of Taxpayer's amended 2008 federal income tax return complied with federal income tax law.

Federal reimbursement theory

The Comptroller reviewed federal guidance stating that taxpayers are not allowed a federal income tax deduction for expenses made with a right or expectation of reimbursement since they are in the nature of loans or advancements (the 'reimbursement theory'). If such deductions are disallowed, then such reimbursement amounts are not included in gross income.

The reimbursement theory requires that (1) the expenditure in question would otherwise constitute an I.R.C. § 162 business expense and (2) a right or expectation of reimbursement exists at the time the expenditure occurs (an unconditional right or expectation is not required).

In this case, the Comptroller acknowledged there was no dispute that Taxpayer's fuel costs constituted ordinary business expenses otherwise deductible under I.R.C. § 162. The Comptroller determined that the charges were made with a right or expectation of reimbursement for reasons including:

- customers were routinely invoiced fuel surcharges by Taxpayer and they were required to make payment within fifteen days
- less than one percent of the fuel surcharges billed to customers was ultimately written off as bad debt.

The Comptroller determined that the amounts Taxpayer reported on its amended Form 1120, line 1c, that

excluded fuel surcharge reimbursements were correct. Accordingly, the excluded fuel surcharge reimbursements were not required to be included in Taxpayer's computation of Texas 'total revenue.' Moreover, the Comptroller could not identify a reasonable basis for treating the fuel surcharge reimbursements differently from the uncontested exclusion of reimbursed accessorial charges.

The takeaway

Refund claims may be available for taxpayers that are including cost reimbursements in federal gross income that (1) constitute ordinary and necessary business expenses under I.R.C. § 162 and (2) are reasonably expected to be repaid at the time the expenses are incurred. In order to have these reimbursements properly excluded from Texas 'total revenue' a taxpayer would have to amend its corresponding federal return to remove such reimbursements from federal gross income.

Let's talk

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