

## Income/Franchise:

### Texas Letter Ruling Concludes Certain Subcontractor Payments are Excludable from Franchise Tax Base

*Letter No. 202407025L*, Tex. Comptroller of Public Accounts (7/24/24). The Tax Policy Division of the Texas Comptroller of Public Accounts issued a letter ruling holding that a taxpayer may exclude from its Texas franchise tax base subcontracting payments related to consulting and supervision services for completions and workovers of oil and gas drilling and workover rigs as the services were made in connection with the construction, remodeling, remediation, or repair of improvements on real property. However, the ruling explains that any subcontractor activities related to production are not considered to “improve real property,” and must be included in total revenue. The ruling cites Texas caselaw involving the exclusion of certain subcontractor payments under Texas Tax Code § 171.1011(g)(3) – explaining that a payment to a third-party generally qualifies for an exclusion from revenue where:

**URL:** <https://star.comptroller.texas.gov/view/202407025L?q1=202407025L>

- The payment is a subcontracting payment, meaning the payments the taxpayer makes to another entity to do work or provide materials that the taxpayer is obligated to provide to its customer and for which that customer compensates the taxpayer;
- The payment is a flow-through fund, meaning the taxpayer’s customer compensates the taxpayer for the subcontractor’s work;
- The payment is mandated by contract or subcontract, meaning the taxpayer has a contractual obligation to pay its subcontractor; and
- The payment is in connection with the actual or proposed design, construction, remodeling, remediation, or repair of improvements to real property, which requires more than a tangential or incidental relationship between the subcontracting activities and the services, labor, or materials for which the subcontractors receive payment.

Consistent with prior guidance, the ruling also acknowledges that drilling an oil or gas well is considered an improvement to real property. Please contact us with any questions.

— Robert Topp (Houston)  
Managing Director  
Deloitte Tax LLP  
rtopp@deloitte.com

Grace Taylor (Houston)  
Senior Manager  
Deloitte Tax LLP  
grtaylor@deloitte.com

This communication contains general information only, and none of Deloitte Touche Tohmatsu Limited (“DTTL”), its global network of member firms or their related entities (collectively, the “Deloitte organization”) is, by means of this communication, rendering professional advice or services. Before making any decision or taking any action that may affect your finances or your business, you should consult a qualified professional adviser.

No representations, warranties or undertakings (express or implied) are given as to the accuracy or completeness of the information in this communication, and none of DTTL, its member firms, related entities, employees or agents shall be liable or responsible for any loss or damage whatsoever arising directly or indirectly in connection with any person relying on this communication. DTTL and each of its member firms, and their related entities, are legally separate and independent entities.

#### **About Deloitte**

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited (“DTTL”), its global network of member firms, and their related entities (collectively, the “Deloitte organization”). DTTL (also referred to as “Deloitte Global”) and each of its member firms and related entities are legally separate and independent entities, which cannot obligate or bind each other in respect of third parties. DTTL and each DTTL member firm and related entity is liable only for its own acts and omissions, and not those of each other. DTTL does not provide services to clients. Please see [www.deloitte.com/about](http://www.deloitte.com/about) to learn more.

Deloitte provides industry-leading audit and assurance, tax and legal, consulting, financial advisory, and risk advisory services to nearly 90% of the Fortune Global 500® and thousands of private companies. Our professionals deliver measurable and lasting results that help reinforce public trust in capital markets, enable clients to transform and thrive, and lead the way toward a stronger economy, a more equitable society and a sustainable world. Building on its 175-plus year history, Deloitte spans more than 150 countries and territories. Learn how Deloitte’s approximately 415,000 people worldwide make an impact that matters at [www.deloitte.com](http://www.deloitte.com).