Amend **CSHB 3** by striking ARTICLE 2 (house committee report, page 16, line 16, through page 29, line 9) and substituting a new ARTICLE 2 to read as follows:

ARTICLE 2. REFORMED FRANCHISE TAX

SECTION 2.01. Subchapter A, Chapter 171, Tax Code, is amended to read as follows:

SUBCHAPTER A. TAX IMPOSED

Sec. 171.001. TAX IMPOSED. (a) A franchise tax is imposed on[~~:~~

[~~(1)~~] each taxable entity [~~corporation~~] that does business in this state or that is chartered or organized in this state[~~; and~~

[~~(2) each limited liability company that does business in this state or that is organized under the laws of this state~~].

(b) In this chapter:

(1) "Banking corporation" means each state, national, domestic, or foreign bank, whether organized under the laws of this state, another state, or another country, or under federal law, including a limited banking association organized under Subtitle A, Title 3, Finance Code, and each bank organized under Section 25(a), Federal Reserve Act (12 U.S.C. Secs. 611-631) (edge corporations), but does not include a bank holding company as that term is defined by Section 2, Bank Holding Company Act of 1956 (12 U.S.C. Sec. 1841).

(2) "Beginning date" means:

(A) for a taxable entity [~~corporation~~] chartered or organized in this state, the date on which the taxable entity's [~~corporation's~~] charter or organization takes effect; and

(B) for any other taxable entity [~~a foreign corporation~~], the date on which the taxable entity [~~corporation~~] begins doing business in this state.

(3) "Corporation" includes:

(A) a limited liability company, as defined under the Texas Limited Liability Company Act;

(B) a savings and loan association; and

(C) a banking corporation.

(4) "Charter" includes a limited liability company's certificate of organization, a limited partnership's certificate of limited partnership, and the registration of a limited liability partnership.

(5) "Internal Revenue Code" means the Internal Revenue Code of 1986 in effect [~~for the federal tax year beginning~~] on [~~or after~~] January 1, 2005, not including any changes made by federal law after that date [~~1996, and before January 1, 1997~~], and any regulations adopted under that code [~~applicable to that period~~].

(6) "Officer" and "director" include a limited liability company's directors and managers and a limited banking association's directors and managers and participants if there are no directors or managers.

(7) "Savings and loan association" means a savings and loan association or savings bank, whether organized under the laws of this state, another state, or another country, or under federal law.

(8) "Shareholder" includes a limited liability company's member and a limited banking association's participant.

(9-a) "Taxable entity" includes, except as provided by Subdivision (9-b):

(A) a corporation;

(B) a partnership; and

(C) any entity that does business in this state or that is chartered or organized in this state, including an entity described by Subdivision (9-c).

(9-b) "Taxable entity" does not include, except as provided by Subdivision (9-c):

(A) an entity that is:

(i) a grantor trust as defined by Sections 671 and 7701(a)(30)(E), Internal Revenue Code, all of the grantors and beneficiaries of which are natural persons or charitable entities as described in Section 501(c)(3), Internal Revenue Code, excluding a trust taxable as a business entity pursuant to Treasury Regulation Section 301.7701-4(b);

(ii) an estate of a natural person as

defined by Section 7701(a)(30)(D), Internal Revenue Code, excluding an estate taxable as a business entity pursuant to Treasury Regulation Section 301.7701-4(b); or

(iii) an escrow;

(B) a real estate investment trust as defined by Section 856, Internal Revenue Code, and its "qualified REIT subsidiary" entities as defined by Section 856(i)(2), Internal Revenue Code;

(C) an entity other than a corporation or a limited liability company that is:

(i) a publicly traded partnership, as defined by Section 7704(b)(1), Internal Revenue Code, interests in which are listed and traded in an established national securities market and that is treated as a partnership for federal income tax purposes; and

(ii) a limited partnership at least 90 percent of whose interests are owned directly or indirectly by an entity described in Subparagraph (i) and at least 90 percent of whose income constitutes qualifying income as defined by Section 7704(d), Internal Revenue Code;

(D) a family limited partnership in which at least 80 percent of the interests are held, directly or indirectly, by members of the same family, including an individual's ancestors, lineal descendants, spouse, brothers and sisters by the whole or half blood, and the estate of any of these persons, and that is a limited partnership:

(i) formed pursuant to the Texas Revised Limited Partnership Act (Article 6132a-1, Vernon's Texas Civil Statutes);

(ii) formed pursuant to the limited partnership law of any other state; or

(iii) treated as a partnership for federal income tax purposes;

(E) a regulated investment company as defined by Section 851, Internal Revenue Code;

(F) a real estate mortgage investment conduit as defined by Section 860D, Internal Revenue Code;

(G) a passive investment partnership as described by Subparagraph (i) or (ii), at least 90 percent of whose federal gross income is composed of passive investment income, including dividends, interest, capital gains, foreign currency exchange gain, periodic and nonperiodic payments with respect to notional principal contracts, option premiums, cash settlement or termination payments with respect to a financial instrument, royalties from the license of intangible property and nonoperating mineral interests, rents from the lease of real property provided that the lessor does not furnish the lessee with any services or utilities other than customary cleaning and security services, and distributive shares of limited partnership income and income from a limited liability company, and the partnership is:

(i) formed pursuant to the Texas Revised Limited Partnership Act (Article 6132a-1, Vernon's Texas Civil Statutes); or

(ii) formed pursuant to the limited partnership law of any other state or a foreign country;

(H) a sole proprietorship;

(I) a general partnership;

(J) an entity, arrangement, or investment vehicle without any employees that is used solely for a finance, securitization, or monetization purpose; or

(K) a trust:

(i) that is taxable as a trust under Section 641, Internal Revenue Code;

(ii) all of the beneficiaries of which are natural persons or charitable entities as defined in Section 501(c)(3), Internal Revenue Code;

(iii) that is not a trust taxable as a business entity pursuant to Treasury Regulation Section 301.7701-4(b);

(iv) at least 90 percent of whose federal gross income consists of passive investment income as described under Paragraph (G); and

(v) that is organized as a trust and is described in Section 7701(a)(30)(E), Internal Revenue Code.

(9-c)(A) A family limited partnership as described in Subdivision (9-b) is a taxable entity under this chapter if the partnership:

(i) is not a passive investment partnership as defined under Subdivision (9-b)(G); and

(ii) conducts an active trade or business.

(B) An entity conducts an active trade or business if:

(i) the activities being carried on by the entity include one or more active operations that form a part of the process of earning income or profit; and

(ii) the entity performs active management and operational functions.

(C) Activities performed by the entity shall include activities performed by persons outside the entity, including independent contractors, to the extent such persons perform services on behalf of the entity and those services constitute all or part of the entity's trade or business.

(D) An entity conducts an active trade or business if assets held by the entity are used in the active trade or business of one or more related entities.

(E) For purposes of this subdivision, the ownership of a royalty interest or a non-operating working interest in mineral rights shall not constitute conduct of an active trade or business.

(c) The tax imposed under this chapter extends to the limits of the United States Constitution and the federal law adopted under the United States constitution.

(d) For purposes of Subsection (a), a taxable entity does business in this state if the entity is a foreign entity and is:

(1) holding a partnership interest, including an interest as an assignee, as a general partner in a general partnership that is doing business in this state;

(2) holding a partnership interest, including an interest as an assignee, as a general partner in a limited partnership that is doing business in this state; or

(3) holding a partnership interest, including an

interest as an assignee, as a limited partner in a limited partnership that is doing business in this state.

Sec. 171.0011. ELECTION OF RATES. (a) Except as otherwise provided by this section and Section 171.0012, a taxable entity shall elect to pay the tax imposed under this chapter at:

(1) the rate provided by Section 171.002; or

(2) the alternate rate provided by Section 171.003.

(b) The election cannot be changed until after the third anniversary of the date the election is made.

(c) A taxable entity that is in the business of leasing employees:

(1) may not elect to pay the tax imposed under this chapter at the rate provided by Section 171.002 and shall pay the tax imposed under this chapter at the alternate rate provided by Section 171.003; and

(2) for the purposes of this chapter, is considered as having elected to pay the tax imposed under this chapter at the alternate rate provided by Section 171.003.

(d) A taxable entity that is an airline:

(1) may not elect to pay the tax imposed under this chapter at the alternate rate provided by Section 171.003 and shall pay the tax imposed under this chapter at the rate provided by Section 171.002;

(2) for the purposes of this chapter, is considered as having elected to pay the tax imposed under this chapter at the rate provided by Section 171.002; and

(3) is not subject to the minimum tax liability under Section 171.0013.

(e) The comptroller shall promulgate a form for a taxable entity to use to make an election under this section. If the taxable entity is an entity other than a corporation and any interests in the entity are owned by natural persons, the election form must be signed by each of those natural persons and by an authorized officer of the entity. The election form shall provide that the taxable entity and those natural persons agree that the taxable earned surplus of the entity shall be calculated pursuant to this chapter without regard to any exclusion, exemption, or

prohibition in Section 24, Article VIII, Texas Constitution.

Sec. 171.0012. MANDATORY ELECTION FOR ALL MEMBERS OF AFFILIATED GROUP. (a) In this section:

(1) "Affiliated group" means one or more chains of entities connected through ownership with a common parent, but only if the common parent has a controlling interest in at least one of the connected entities and maintains a controlling interest indirectly through the ownership chain in the other connected entities.

(2) "Controlling interest" means:

(A) for a corporation, either 50 percent or more, owned directly or indirectly, of the total combined voting power of all classes of stock of the corporation, or 50 percent or more, owned directly or indirectly, of the beneficial ownership interest in the voting stock of the corporation; and

(B) for a partnership, association, trust, or other entity, 50 percent or more, owned directly or indirectly, of the capital, profits, or beneficial interest in the partnership, association, trust, or other entity.

(b) Notwithstanding any other provision of this chapter, all entities that are part of the same affiliated group must make the same election and must pay the tax imposed under this chapter at the rate provided by either Section 171.002 or the alternate rate provided by Section 171.003.

(c) For the purposes of this chapter, a taxable entity required to elect the same rate as all the other members of its affiliated group under this section is considered as having elected to pay the tax imposed under this chapter at that rate.

Sec. 171.0013. MINIMUM TAX LIABILITY. (a) Except as provided by Section 171.0011(d)(3), the minimum tax liability for a taxable entity that elects to pay the tax under this chapter at the rate provided by Section 171.002 is an amount equal to 50 percent of the amount of tax the taxable entity would be liable for under this chapter if the taxable entity had elected to pay the tax under this chapter at the alternate rate provided by Section 171.003.

(b) The minimum tax liability for a taxable entity that elects to pay the tax under this chapter at the alternate rate

provided by Section 171.003 is an amount equal to 50 percent of the amount of tax the taxable entity would be liable for under this chapter if the taxable entity had elected to pay the tax under this chapter at the rate provided by Section 171.002.

(c) This section does not apply to an entity that is not a taxable entity as defined by Section 171.001(b)(9-b).

Sec. 171.0014. ADDITIONAL TAX. (a) An additional tax is imposed on a taxable entity that has elected to pay the tax imposed by this chapter at the rate provided by Section 171.002 and during the period in which that election is in effect [~~corporation that~~] for any reason becomes no longer subject to the earned surplus component of the tax, without regard to whether the taxable entity [~~corporation~~] remains subject to the taxable capital component of the tax, other than through a valid election to pay the tax imposed under this chapter at the alternate rate provided by Section 171.003. An additional tax is imposed on a taxable entity that has elected to pay the tax imposed by this chapter at the alternate rate provided by Section 171.003 and during the period in which that election is in effect for any reason becomes no longer subject to the tax imposed under this chapter.

(b) The additional tax is equal to 4.5 percent of the taxable entity's [~~corporation's~~] net taxable earned surplus computed on the period beginning on the day after the last day for which the tax imposed on net taxable earned surplus was computed under Section 171.1532 and ending on the date the taxable entity [~~corporation~~] is no longer subject to the earned surplus component of the tax.

(c) The additional tax imposed and any report required by the comptroller are due on the 60th day after the date the taxable entity [~~corporation~~] becomes no longer subject to the earned surplus component of the tax.

(d) Except as otherwise provided by this section, the provisions of this chapter apply to the tax imposed under this section.

Sec. 171.0015. RULES: AVOIDANCE OF DOUBLE TAXATION. (a) Except as provided by Section 171.0012, each entity shall be treated as a separate taxable entity.

(b) Wages, as that term is defined under Subchapter F, Chapter 201, Labor Code, that are paid by one taxable entity may not be included in the tax base of another taxable entity either directly, indirectly, or constructively for purposes of determining taxable wages under Subchapter C-1.

(c) A taxable entity shall be entitled to the dividends received deduction for dividends received in computing its earned surplus. For the purposes of this subsection, "dividends received deduction" means the deduction allowed by Section 243, Internal Revenue Code.

(d) Except as provided by Subsection (e), any taxable entity that is allocated a distributive share of income, gain, or capital from another taxable or exempt entity under federal income tax rules, including an actual distribution of income, gain, or capital, shall be entitled to exclude that amount in computing its earned surplus for purposes of this chapter.

(e) Subsection (d) does not apply to the distributive share of income, gain, or capital from an interest in a publicly traded partnership, as defined by Section 171.001(b)(9-b)(C)(i), that is allocated to a taxable entity that is a direct owner of that interest. If the direct owner of that interest is not a taxable entity, Subsection (d) does not apply to the first upper-tier level of a taxable entity or entities, if any, that are indirect owners of that interest.

Sec. 171.002. RATES; COMPUTATION OF TAX. (a) Subject to the minimum tax liability of the taxable entity under Section 171.0013, the [~~The~~] rates of the franchise tax are for a taxable entity that elects to pay the tax at the rate provided by this section:

(1) 0.25 percent per year of privilege period of net taxable capital; and

(2) 4.5 percent of net taxable earned surplus.

(b) The amount of franchise tax on each taxable entity [~~corporation~~] is computed by adding the following:

(1) the amount calculated by applying the tax rate prescribed by Subsection (a)(1) to the taxable entity's [~~corporation's~~] net taxable capital; and

(2) the difference between:

(A) the amount calculated by applying the tax rate prescribed by Subsection (a)(2) to the taxable entity's [~~corporation's~~] net taxable earned surplus; and

(B) the amount determined under Subdivision (1).

(c) In making a computation under Subsection (b), an amount computed under Subsection (b)(1) or (b)(2) that is zero or less is computed as a zero.

Sec. 171.003. ALTERNATE RATE. Subject to the minimum tax liability of the taxable entity under Section 171.0013, the alternate rate of the franchise tax for a taxable entity that elects to pay the alternate rate is 1.15 percent of taxable wages as determined under Subchapter C-1.

Sec. 171.004. EXEMPTION FOR CERTAIN SMALL BUSINESSES. [~~(d)~~] A taxable entity [~~corporation~~] is not required to pay any tax and is not considered to owe any tax for a period if:

(1) the amount of tax computed for the taxable entity [~~corporation~~] is less than $100; or

(2) the amount of the taxable entity's [~~corporation's~~] gross receipts:

(A) from its entire business under Section 171.105 is less than $150,000; and

(B) from its entire business under Section 171.1051, including the amount excepted under Section 171.1051(a), is less than $150,000.

Sec. 171.005. RATE OF TAX FOR CORPORATION IN PROCESS OF LIQUIDATION. The franchise tax rate on a corporation in the process of liquidation, as defined by Section 171.102 [~~of this code~~], is the rate established by Section 171.002 [~~of this code~~].

SECTION 2.02. Subchapter B, Chapter 171, Tax Code, is amended by adding Section 171.088 to read as follows:

Sec. 171.088. EXEMPTION--NONCORPORATE TAXABLE ENTITY ELIGIBLE FOR CERTAIN EXEMPTIONS. A taxable entity that is not a corporation but that, because of its activities, would qualify for a specific exemption under this subchapter if it were a corporation qualifies for the exemption and is exempt from the tax in the same manner and under the same conditions as a corporation.

SECTION 2.03. Section 171.101, Tax Code, is amended to read as follows:

Sec. 171.101. DETERMINATION OF NET TAXABLE CAPITAL. The [~~(a) Except as provided by Subsections (b) and (c), the~~] net taxable capital of a taxable entity [~~corporation~~] is computed by:

(1) [~~adding the corporation's stated capital, as defined by Article 1.02, Texas Business Corporation Act, and the corporation's surplus, to determine the corporation's taxable capital;~~

[~~(2)~~] apportioning the taxable entity's surplus [~~corporation's taxable capital~~] to this state as provided by Section 171.106(a) or (c), as applicable, to determine the taxable entity's [~~corporation's~~] apportioned taxable capital; and

(2) [~~(3)~~] subtracting from the amount computed under Subdivision (1) [~~(2)~~] any other allowable deductions to determine the taxable entity's [~~corporation's~~] net taxable capital.

[~~(b) The net taxable capital of a limited liability company is computed by:~~

[~~(1) adding the company's members' contributions, as provided for under the Texas Limited Liability Company Act, and surplus to determine the company's taxable capital;~~

[~~(2) apportioning the amount determined under Subdivision (1) to this state in the same manner that the taxable capital of a corporation is apportioned to this state under Section 171.106(a) or (c), as applicable, to determine the company's apportioned taxable capital; and~~

[~~(3) subtracting from the amount computed under Subdivision (2) any other allowable deductions, to determine the company's net taxable capital.~~

[~~(c) The net taxable capital of a savings and loan association is computed by:~~

[~~(1) determining the association's net worth; and~~

[~~(2) apportioning the amount determined under Subdivision (1) to this state in the same manner that the taxable capital of a corporation is apportioned to this state under Section 171.106(a) to determine the association's net taxable capital.~~]

SECTION 2.04. Section 171.103, Tax Code, is amended to read

as follows:

Sec. 171.103. DETERMINATION OF GROSS RECEIPTS FROM BUSINESS DONE IN THIS STATE FOR TAXABLE CAPITAL. In apportioning taxable capital, the gross receipts of a taxable entity [~~corporation~~] from its business done in this state is the sum of the taxable entity's [~~corporation's~~] receipts from:

(1) each sale of tangible personal property if the property is delivered or shipped to a buyer in this state regardless of the FOB point or another condition of the sale, and each sale of tangible personal property shipped from this state to a purchaser in another state in which the seller is not subject to taxation;

(2) each service performed in this state;

(3) each rental of property situated in this state;

(4) the use of a patent, copyright, trademark, franchise, or license in this state;

(5) each sale of real property located in this state, including royalties from oil, gas, or other mineral interests; and

(6) other business done in this state.

SECTION 2.05. Section 171.1032, Tax Code, is amended to read as follows:

Sec. 171.1032. DETERMINATION OF GROSS RECEIPTS FROM BUSINESS DONE IN THIS STATE FOR TAXABLE EARNED SURPLUS. (a) Except for the gross receipts of a taxable entity [~~corporation~~] that are subject to the provisions of Section 171.1061, in apportioning taxable earned surplus, the gross receipts of a taxable entity [~~corporation~~] from its business done in this state is the sum of the taxable entity's [~~corporation's~~] receipts from:

(1) each sale of tangible personal property if the property is delivered or shipped to a buyer in this state regardless of the FOB point or another condition of the sale, and each sale of tangible personal property shipped from this state to a purchaser in another state in which the seller is not subject to any tax on, or measured by, net income, without regard to whether the tax is imposed;

(2) each service performed in this state;

(3) each rental of property situated in this state;

(4) the use of a patent, copyright, trademark,

franchise, or license in this state;

(5) each sale of real property located in this state, including royalties from oil, gas, or other mineral interests;

(6) each partnership or joint venture to the extent provided by Subsection (c); and

(7) other business done in this state.

(b) A taxable entity [~~corporation~~] shall deduct from its gross receipts computed under Subsection (a) any amount to the extent included under Subsection (a) because of the application of Section 78 or Sections 951-964, Internal Revenue Code, any amount excludable under Section 171.110(k), and dividends received from a subsidiary, associate, or affiliated entity [~~corporation~~] that does not transact a substantial portion of its business or regularly maintain a substantial portion of its assets in the United States.

(c) A taxable entity [~~corporation~~] shall include in its gross receipts computed under Subsection (a) the taxable entity's [~~corporation's~~] share of the gross receipts of each partnership, including a general partnership and a publicly traded partnership as defined by Section 171.001(b)(9-b)(C)(i), and joint venture of which the taxable entity [~~corporation~~] is a part apportioned to this state as though the taxable entity [~~corporation~~] directly earned the receipts, including receipts from business done with the taxable entity [~~corporation~~].

SECTION 2.06. Section 171.104, Tax Code, is amended to read as follows:

Sec. 171.104. GROSS RECEIPTS FROM BUSINESS DONE IN TEXAS: DEDUCTION FOR FOOD AND MEDICINE RECEIPTS. A taxable entity [~~corporation~~] may deduct from its receipts includable under Section 171.103(1) [~~of this code~~] the amount of the taxable entity's [~~corporation's~~] receipts from sales of the following items, if the items are shipped from outside this state and the receipts would be includable under Section 171.103(1) [~~of this code~~] in the absence of this section:

(1) food that is exempted from the Limited Sales, Excise, and Use Tax Act by Section 151.314(a) [~~of this code~~]; and

(2) health care supplies that are exempted from the

Limited Sales, Excise, and Use Tax Act by Section 151.313 [~~of this code~~].

SECTION 2.07. Section 171.105, Tax Code, is amended to read as follows:

Sec. 171.105. DETERMINATION OF GROSS RECEIPTS FROM ENTIRE BUSINESS FOR TAXABLE CAPITAL. (a) In apportioning taxable capital, the gross receipts of a taxable entity [~~corporation~~] from its entire business is the sum of the taxable entity's [~~corporation's~~] receipts from:

(1) each sale of the taxable entity's [~~corporation's~~] tangible personal property;

(2) each service, rental, or royalty; and

(3) other business.

(b) If a taxable entity [~~corporation~~] sells an investment or capital asset, the taxable entity's [~~corporation's~~] gross receipts from its entire business for taxable capital include only the net gain from the sale.

SECTION 2.08. Section 171.1051, Tax Code, is amended to read as follows:

Sec. 171.1051. DETERMINATION OF GROSS RECEIPTS FROM ENTIRE BUSINESS FOR TAXABLE EARNED SURPLUS. (a) Except for the gross receipts of a taxable entity [~~corporation~~] that are subject to the provisions of Section 171.1061, in apportioning taxable earned surplus, the gross receipts of a taxable entity [~~corporation~~] from its entire business is the sum of the taxable entity's [~~corporation's~~] receipts from:

(1) each sale of the taxable entity's [~~corporation's~~] tangible personal property;

(2) each service, rental, or royalty;

(3) each partnership and joint venture as provided by Subsection (d); and

(4) other business.

(b) If a taxable entity [~~corporation~~] sells an investment or capital asset, the taxable entity's [~~corporation's~~] gross receipts from its entire business for taxable earned surplus includes only the net gain from the sale.

(c) A taxable entity [~~corporation~~] shall deduct from its

gross receipts computed under Subsection (a) any amount to the extent included in Subsection (a) because of the application of Section 78 or Sections 951-964, Internal Revenue Code, any amount excludable under Section 171.110(k), and dividends received from a subsidiary, associate, or affiliated entity [~~corporation~~] that does not transact a substantial portion of its business or regularly maintain a substantial portion of its assets in the United States.

(d) A taxable entity [~~corporation~~] shall include in its gross receipts computed under Subsection (a) the taxable entity's [~~corporation's~~] share of the gross receipts of each partnership, including a general partnership and a publicly traded partnership as defined by Section 171.001(b)(9-b)(C)(i), and joint venture of which the taxable entity [~~corporation~~] is a part.

SECTION 2.09. Sections 171.106(a)-(d), Tax Code, are amended to read as follows:

(a) Except as provided by Subsections (c) and (d), a taxable entity's [~~corporation's~~] taxable capital is apportioned to this state to determine the amount of the tax imposed under Section 171.002(b)(1) by multiplying the taxable entity's [~~corporation's~~] taxable capital by a fraction, the numerator of which is the taxable entity's [~~corporation's~~] gross receipts from business done in this state, as determined under Section 171.103, and the denominator of which is the taxable entity's [~~corporation's~~] gross receipts from its entire business, as determined under Section 171.105.

(b) Except as provided by Subsections (c) and (d), a taxable entity's [~~corporation's~~] taxable earned surplus is apportioned to this state to determine the amount of tax imposed under Section 171.002(b)(2) by multiplying the taxable earned surplus by a fraction, the numerator of which is the taxable entity's [~~corporation's~~] gross receipts from business done in this state, as determined under Section 171.1032, and the denominator of which is the taxable entity's [~~corporation's~~] gross receipts from its entire business, as determined under Section 171.1051.

(c) A taxable entity's [~~corporation's~~] taxable capital or earned surplus that is derived, directly or indirectly, from the sale of management, distribution, or administration services to or

on behalf of a regulated investment company, including a taxable entity [~~corporation~~] that includes trustees or sponsors of employee benefit plans that have accounts in a regulated investment company, is apportioned to this state to determine the amount of the tax imposed under Section 171.002 by multiplying the taxable entity's [~~corporation's~~] total taxable capital or earned surplus from the sale of services to or on behalf of a regulated investment company by a fraction, the numerator of which is the average of the sum of shares owned at the beginning of the year and the sum of shares owned at the end of the year by the investment company shareholders who are commercially domiciled in this state or, if the shareholders are individuals, are residents of this state, and the denominator of which is the average of the sum of shares owned at the beginning of the year and the sum of shares owned at the end of the year by all investment company shareholders. The taxable entity [~~corporation~~] shall make a separate computation to allocate taxable capital and earned surplus. In this subsection, "regulated investment company" has the meaning assigned by Section 851(a), Internal Revenue Code.

(d) A taxable entity's [~~corporation's~~] taxable capital or taxable earned surplus that is derived, directly or indirectly, from the sale of management, administration, or investment services to an employee retirement plan is apportioned to this state to determine the amount of the tax imposed under Section 171.002 by multiplying the taxable entity's [~~corporation's~~] total taxable capital or earned surplus from the sale of services to an employee retirement plan company by a fraction, the numerator of which is the average of the sum of beneficiaries domiciled in Texas at the beginning of the year and the sum of beneficiaries domiciled in Texas at the end of the year, and the denominator of which is the average of the sum of all beneficiaries at the beginning of the year and the sum of all beneficiaries at the end of the year. The taxable entity [~~corporation~~] shall make a separate computation to apportion taxable capital and earned surplus. In this section, "employee retirement plan" means a plan or other arrangement that is qualified under Section 401(a), Internal Revenue Code, or satisfies the requirements of Section 403, Internal Revenue Code, or a

government plan described in Section 414(d), Internal Revenue Code. The term does not include an individual retirement account or individual retirement annuity within the meaning of Section 408, Internal Revenue Code.

SECTION 2.10. Section 171.1061, Tax Code, is amended to read as follows:

Sec. 171.1061. ALLOCATION OF CERTAIN TAXABLE EARNED SURPLUS TO THIS STATE. An item of income included in a taxable entity's [~~corporation's~~] taxable earned surplus, except that portion derived from dividends and interest, that a state, other than this state, or a country, other than the United States, cannot tax because the activities generating that item of income do not have sufficient unitary connection with the taxable entity's [~~corporation's~~] other activities conducted within that state or country under the United States Constitution, is allocated to this state if the taxable entity's [~~corporation's~~] commercial domicile is in this state. Income that can only be allocated to the state of commercial domicile because the income has insufficient unitary connection with any other state or country shall be allocated to this state or another state or country net of expenses related to that income. A portion of a taxable entity's [~~corporation's~~] taxable earned surplus allocated to this state under this section may not be apportioned under Section 171.110(a-4)(2) [~~171.110(a)(2)~~].

SECTION 2.11. Sections 171.107(b), (d), and (e), Tax Code, are amended to read as follows:

(b) A taxable entity [~~corporation~~] may deduct from its apportioned taxable capital the amortized cost of a solar energy device or from its apportioned taxable earned surplus 10 percent of the amortized cost of a solar energy device if:

(1) the device is acquired by the taxable entity [~~corporation~~] for heating or cooling or for the production of power;

(2) the device is used in this state by the taxable entity [~~corporation~~]; and

(3) the cost of the device is amortized in accordance with Subsection (c) [~~of this section~~].

(d) A taxable entity [~~corporation~~] that makes a deduction under this section shall file with the comptroller an amortization schedule showing the period in which a deduction is to be made. On the request of the comptroller, the taxable entity [~~corporation~~] shall file with the comptroller proof of the cost of the solar energy device or proof of the device's operation in this state.

(e) A taxable entity [~~corporation~~] may elect to make the deduction authorized by this section either from apportioned taxable capital or apportioned taxable earned surplus for each separate regular annual period. An election for an initial period applies to the second tax period and to the first regular annual period.

SECTION 2.12. Sections 171.108(b), (d), and (e), Tax Code, as added by Section 4, **HB 2201**, Acts of the 79th Legislature, Regular Session, 2005, are amended to read as follows:

(b) A taxable entity [~~corporation~~] may deduct from its apportioned taxable capital the amortized cost of equipment or from its apportioned taxable earned surplus 10 percent of the amortized cost of equipment:

(1) that is used in a clean coal project;

(2) that is acquired by the taxable entity [~~corporation~~] for use in generation of electricity, production of process steam, or industrial production;

(3) that the taxable entity [~~corporation~~] uses in this state; and

(4) the cost of which is amortized in accordance with Subsection (c).

(d) A taxable entity [~~corporation~~] that makes a deduction under this section shall file with the comptroller an amortization schedule showing the period for which the deduction is to be made. On the request of the comptroller, the taxable entity [~~corporation~~] shall file with the comptroller proof of the cost of the equipment or proof of the equipment's operation in this state.

(e) A taxable entity [~~corporation~~] may elect to make the deduction authorized by this section from apportioned taxable capital or apportioned taxable earned surplus, but not from both, for each separate regular annual period. An election for an initial

period applies to the second tax period and to the first regular annual period.

SECTION 2.13. Section 171.109, Tax Code, is amended by amending Subsections (a), (b)-(f), (h), (j), (k), (m), and (n), by reenacting and amending Subsection (g), as amended by Chapters 801 and 1198, Acts of the 71st Legislature, Regular Session, 1989, and by adding Subsection (a-2) to read as follows:

(a) In this chapter:

(1) "Surplus" or "taxable capital" means the net assets of a taxable entity [~~corporation minus its stated capital. For a limited liability company, "surplus" means the net assets of the company minus its members' contributions~~]. Surplus includes unrealized, estimated, or contingent losses or obligations or any writedown of assets other than those listed in Subsection (i) [~~of this section~~] net of appropriate income tax provisions. The definition under this subdivision does not apply to earned surplus.

(2) "Net assets" means the total assets of a taxable entity [~~corporation~~] minus its total debts.

(3) "Debt" means any legally enforceable obligation measured in a certain amount of money which must be performed or paid within an ascertainable period of time or on demand.

(a-2) In this section, "distribution" includes a dividend.

(b) Except as otherwise provided in this section, a taxable entity [~~corporation~~] must compute its surplus, assets, and debts according to generally accepted accounting principles. If generally accepted accounting principles are unsettled or do not specify an accounting practice for a particular purpose related to the computation of surplus, assets, or debts, the comptroller by rule may establish rules to specify the applicable accounting practice for that purpose.

(c) A taxable entity [~~corporation~~] whose taxable capital is less than $1 million may report its surplus according to the method used in the taxable entity's [~~corporation's~~] most recent federal income tax return originally due on or before the date on which the taxable entity's [~~corporation's~~] franchise tax report is originally due. In determining if taxable capital is less than $1 million, the taxable entity [~~corporation~~] shall apply the methods the taxable

entity [~~corporation~~] used in computing that federal income tax return unless another method is required under this chapter.

(d) A taxable entity [~~corporation~~] shall report its surplus based solely on its own financial condition. Consolidated reporting of surplus is prohibited.

(e) A taxable entity [~~Unless the provisions of Section 171.111 apply due to an election under that section, a corporation~~] may not change the accounting methods used to compute its surplus more often than once every four years without the written consent of the comptroller. A change in accounting methods is not justified solely because it results in a reduction of tax liability.

(f) A taxable entity making a distribution [~~corporation declaring dividends~~] shall exclude the distribution [~~those dividends~~] from its taxable capital, and a taxable entity [~~corporation~~] receiving a distribution [~~dividends~~] shall include the distribution [~~those dividends~~] in its gross receipts and taxable capital as of the earlier of:

(1) the date the distribution is [~~dividends are~~] declared, if the distribution is [~~dividends are~~] actually paid in cash or property other than a note payable within one year after the declaration date; or

(2) the date the distribution is [~~dividends are~~] actually paid in cash or property other than a note payable.

(g) All oil and gas exploration and production activities conducted by a taxable entity [~~corporation~~] that reports its surplus according to generally accepted accounting principles as required or permitted by this chapter must be reported according to the successful efforts or the full cost method of accounting.

(h) A parent or investor taxable entity [~~corporation~~] must use the cost method of accounting in reporting and calculating the franchise tax on its investments in subsidiary taxable entities [~~corporations~~] or other investees. The retained earnings of a subsidiary taxable entity [~~corporation~~] or other investee before acquisition by the parent or investor taxable entity [~~corporation~~] may not be excluded from the cost of the subsidiary taxable entity [~~corporation~~] or investee to the parent or investor taxable entity [~~corporation~~] and must be included by the parent or investor

taxable entity [~~corporation~~] in calculating its surplus.

(j) A taxable entity [~~corporation~~] may not exclude from surplus:

(1) liabilities for compensation and other benefits provided to employees, other than wages, that are not debt as of the end of the accounting period on which the taxable capital component is based, including retirement, medical, insurance, postretirement, and other similar benefits; and

(2) deferred investment tax credits.

(k) Notwithstanding any other provision in this chapter, a taxable entity [~~corporation~~] subject to the tax imposed by this chapter shall use double entry bookkeeping to account for all transactions that affect the computation of that tax.

(m) A taxable entity [~~corporation~~] may not use the push-down method of accounting in computing or reporting its surplus.

[~~(n) A corporation must use the equity method of accounting when reporting an investment in a partnership or joint venture.~~]

SECTION 2.14. Section 171.110, Tax Code, is amended to read as follows:

Sec. 171.110. DETERMINATION OF NET TAXABLE EARNED SURPLUS. (a) The [~~net~~] taxable earned surplus of a corporation is computed by[~~:~~

[~~(1)~~] determining the corporation's reportable federal taxable income, subtracting from that amount any amount excludable under Subsection (k), any amount included in reportable federal taxable income under Section 78 or Sections 951-964, Internal Revenue Code, and dividends received from a subsidiary, associate, or affiliated corporation that does not transact a substantial portion of its business or regularly maintain a substantial portion of its assets in the United States, and adding to that amount any compensation of officers or directors, or if a bank, any compensation of directors and executive officers, to the extent excluded in determining federal taxable income.

(a-1) The comptroller shall adopt rules to determine the reportable federal taxable income of an entity other than a corporation using principles similar to the standards applied to a corporation and a limited liability company.

(a-2) The taxable earned surplus of a partnership is the greater of:

(1) an amount computed by:

(A) determining the amount of the partnership's ordinary income or loss under applicable provisions of the Internal Revenue Code, and adding guaranteed payments to partners and capital gains that are additional items not already included in ordinary income or loss; and

(B) subtracting:

(i) the amount paid to the partners that is subject to self-employment taxes; and

(ii) the amount paid to a qualified pension plan or benefit plan for the partners; or

(2) 15 percent of the amount determined under Subdivision (1)(A).

(a-3) The taxable earned surplus of an entity other than a corporation or a partnership is the entity's reportable federal taxable income.

(a-4) The net taxable earned surplus of a taxable entity is computed by:

(1) determining the taxable entity's taxable earned surplus as provided by Subsection (a), (a-1), (a-2), or (a-3), as appropriate [~~to determine the corporation's taxable earned surplus~~];

(2) apportioning the taxable entity's [~~corporation's~~] taxable earned surplus to this state as provided by Section 171.106(b) or (c), as applicable, to determine the taxable entity's [~~corporation's~~] apportioned taxable earned surplus;

(3) adding the taxable entity's [~~corporation's~~] taxable earned surplus allocated to this state as provided by Section 171.1061; and

(4) subtracting from that amount any allowable deductions and any business loss that is carried forward to the tax reporting period and deductible under Subsection (e).

[~~(b) Except as provided by Subsection (c), a corporation is not required to add the compensation of officers or directors as required by Subsection (a)(1) if the corporation is:~~

[~~(1) a corporation that has not more than 35 shareholders; or~~

[~~(2) an S corporation, as that term is defined by Section 1361, Internal Revenue Code.~~

[~~(c) A subsidiary corporation may not claim the exclusion under Subsection (b) if it has a parent corporation that does not qualify for the exclusion. For purposes of this subsection, a corporation qualifies as a parent if it ultimately controls the subsidiary, even if the control arises through a series or group of other subsidiaries or entities. Control is presumed if a parent corporation directly or indirectly owns, controls, or holds a majority of the outstanding voting stock of a corporation or ownership interests in another entity.~~]

(d) A corporation's reportable federal taxable income is the corporation's federal taxable income after Schedule C special deductions and before net operating loss deductions as computed under the Internal Revenue Code, except that an S corporation's reportable federal taxable income is the amount of the income reportable to the Internal Revenue Service as taxable to the corporation's shareholders.

(e) For purposes of this section, a business loss is any negative amount after apportionment and allocation. The business loss shall be carried forward to the year succeeding the loss year as a deduction to net taxable earned surplus, then successively to the succeeding four taxable years after the loss year or until the loss is exhausted, whichever occurs first, but for not more than five taxable years after the loss year. Notwithstanding the preceding sentence, a business loss from a tax year that ends before January 1, 1991, may not be used to reduce net taxable earned surplus. A business loss can be carried forward only by the taxable entity [~~corporation~~] that incurred the loss and cannot be transferred to or claimed by any other entity, including the survivor of a merger if the loss was incurred by the taxable entity [~~corporation~~] that did not survive the merger.

(f) A taxable entity [~~corporation~~] may use either the "first in-first out" or "last in-first out" method of accounting to compute its net taxable earned surplus, but only to the extent that

the taxable entity [~~corporation~~] used that method on its most recent federal income tax report originally due on or before the date on which the taxable entity's [~~corporation's~~] franchise tax report is originally due.

[~~(g) For purposes of this section, an approved Employee Stock Ownership Plan controlling a minority interest and voted through a single trustee shall be considered one shareholder.~~]

(h) A taxable entity [~~corporation~~] shall report its net taxable earned surplus based solely on its own financial condition. Consolidated reporting is prohibited.

[~~(i) For purposes of this section, any person designated as an officer is presumed to be an officer if that person:~~

[~~(1) holds an office created by the board of directors or under the corporate charter or bylaws; and~~

[~~(2) has legal authority to bind the corporation with third parties by executing contracts or other legal documents.~~

[~~(j) A corporation may rebut the presumption described in Subsection (i) that a person is an officer if it conclusively shows, through the person's job description or other documentation, that the person does not participate or have authority to participate in significant policy making aspects of the corporate operations.~~]

(k) Dividends and interest received from federal obligations are not included in earned surplus or gross receipts for earned surplus purposes.

(l) In this section:

(1) "Federal obligations" means:

(A) stocks and other direct obligations of, and obligations unconditionally guaranteed by, the United States government and United States government agencies; and

(B) direct obligations of a United States government-sponsored agency.

(2) "Obligation" means any bond, debenture, security, mortgage-backed security, pass-through certificate, or other evidence of indebtedness of the issuing entity. The term does not include a deposit, a repurchase agreement, a loan, a lease, a participation in a loan or pool of loans, a loan collateralized by an obligation of a United States government agency, or a loan

guaranteed by a United States government agency.

(3) "United States government" means any department or ministry of the federal government, including a federal reserve bank. The term does not include a state or local government, a commercial enterprise owned wholly or partly by the United States government, or a local governmental entity or commercial enterprise whose obligations are guaranteed by the United States government.

(4) "United States government agency" means an instrumentality of the United States government whose obligations are fully and explicitly guaranteed as to the timely payment of principal and interest by the full faith and credit of the United States government. The term includes the Government National Mortgage Association, the Department of Veterans Affairs, the Federal Housing Administration, the Farmers Home Administration, the Export-Import Bank, the Overseas Private Investment Corporation, the Commodity Credit Corporation, the Small Business Administration, and any successor agency.

(5) "United States government-sponsored agency" means an agency originally established or chartered by the United States government to serve public purposes specified by the United States Congress but whose obligations are not explicitly guaranteed by the full faith and credit of the United States government. The term includes the Federal Home Loan Mortgage Corporation, the Federal National Mortgage Association, the Farm Credit System, the Federal Home Loan Bank System, the Student Loan Marketing Association, and any successor agency.

(m) Except as provided by Subsection (n), in determining net taxable earned surplus, a taxable entity shall add back to reportable federal taxable income any royalty payment, interest payment, or management fee payment made to a related entity during the period on which earned surplus is based to the extent deducted in computing reportable federal taxable income.

(n)(1) A taxable entity is not required to add back royalty payments made to a related entity if:

(A) the related entity during the period on which earned surplus is based directly or indirectly paid or incurred the amount to a person or entity that is not a related party, the

transaction was done for a valid business purpose, and the payments were made at arm's length; or

(B) the royalty payments are paid or incurred to a related party organized under the laws of a foreign nation, are subject to a comprehensive income tax treaty between the foreign nation and the United States, and are taxed in the foreign nation at a tax rate equal to or greater than 4.5 percent.

(2) A taxable entity is not required to add back interest payments made to a related entity if:

(A) the rate of interest used to calculate interest payments does not exceed the interest rate provided by Section 111.060(b) that was in effect at the time the loan agreement was made; or

(B) the related entity during the period on which earned surplus is based directly or indirectly paid or incurred the amount to a person or entity that is not a related entity, the transaction was done for a valid business purpose, and the payments were made at arm's length.

(3) A taxable entity is not required to add back management fee payments made to a related entity if the taxable entity established by a preponderance of the evidence that the payment between the taxable entity and a related entity had a valid business purpose and the payments were made at arm's length.

(o) For purposes of Subsections (m) and (n), the following terms have the following meanings:

(1) "Arm's length" means the standard of conduct under which unrelated parties having substantially equal bargaining power, each acting in its own interest, would negotiate or carry out a particular transaction.

(2) "Controlling interest" means:

(A) for a corporation, either 50 percent or more, owned directly or indirectly, of the total combined voting power of all classes of stock of the corporation, or 50 percent or more, owned directly or indirectly, of the beneficial ownership interest in the voting stock of the corporation; and

(B) for a partnership, association, trust, or other entity, 50 percent or more, owned directly or indirectly, of

the capital, profits, or beneficial interest in the partnership, association, trust, or other entity.

(3) "Interest payment" means an amount allowable as an interest deduction under Section 163, Internal Revenue Code.

(4) "Management fee" includes expenses and costs paid for services pertaining to accounts receivable and payable, employee benefit plans, insurance, legal, consulting, payroll, data processing, purchasing, tax, financial and securities, accounting, reporting and compliance services, or similar services.

(5) "Related entity" means a person, corporation, or other entity, including an entity that is treated as a pass-through or disregarded entity for purposes of federal taxation, whether the person, corporation, or entity is a taxable entity or not, in which one person, corporation, or entity, or set of related persons, corporations, or entities, directly or indirectly owns or controls a controlling interest in another entity.

(6) "Royalty payment" means a payment related to the acquisition, use, maintenance or management, ownership, sale, exchange, or any other disposition of licenses, trademarks, copyrights, trade names, trade dress, service marks, mask works, trade secrets, patents, or any other similar types of intangible assets as determined by the comptroller.

(7) "Valid business purpose" means one or more business purposes, other than the avoidance or reduction of taxes, that alone or in combination constitute the primary motivation for a business activity or transaction that changes in a meaningful way, apart from tax effects, the economic position of the entity. A meaningful change in the taxable entity's economic position includes an increase in its market share or entry into new business markets.

(p) Notwithstanding any other provision of this section, a taxable entity shall add back to reportable federal taxable income any payments made to a related party that is an entity described in Section 171.001(b)(9-b)(G) during the period on which earned surplus is based to the extent deducted in computing reportable federal taxable income.

(q) The comptroller may distribute, apportion, or allocate gross income, deductions, credits, or allowances between or among two or more organizations, trades, or businesses, whether or not incorporated, whether or not organized in the United States, and whether or not affiliated, if:

(1) the organizations, trades, or businesses are owned or controlled directly or indirectly by the same interests; and

(2) the comptroller determines that the distribution, apportionment, or allocation is necessary to reflect an arm's-length standard, within the meaning of 26 C.F.R. Section 1.482-1, and to clearly reflect the income of those organizations, trades, or businesses.

(r) In administering Subsection (q), the comptroller shall apply the administrative and judicial interpretations of Section 482, Internal Revenue Code.

SECTION 2.15. Sections 171.112(b)-(f) and (h), Tax Code, are amended to read as follows:

(b) Except as otherwise provided in this section, a taxable entity [~~corporation~~] must compute gross receipts in accordance with generally accepted accounting principles. If generally accepted accounting principles are unsettled or do not specify an accounting practice for a particular purpose related to the computation of gross receipts, the comptroller by rule may establish rules to specify the applicable accounting practice.

(c) A taxable entity [~~corporation~~] whose taxable capital is less than $1 million may report its gross receipts according to the method used in the taxable entity's [~~corporation's~~] most recent federal income tax return originally due on or before the date on which the taxable entity's [~~corporation's~~] franchise tax report is originally due. In determining if taxable capital is less than $1 million, the taxable entity [~~corporation~~] shall apply the methods the taxable entity [~~corporation~~] used in computing that federal income tax return unless another method is required under this chapter.

(d) A taxable entity [~~corporation~~] shall report its gross receipts based solely on its own financial condition. Consolidated reporting is prohibited.

(e) Unless the provisions of Section 171.111 apply due to an election under that section, a taxable entity [~~corporation~~] may not change its accounting methods used to calculate gross receipts more often than once every four years without the express written consent of the comptroller. A change in accounting methods is not justified solely because it results in a reduction of tax liability.

(f) Notwithstanding any other provision in this chapter, a taxable entity [~~corporation~~] subject to the tax imposed by this chapter shall use double entry bookkeeping to account for all transactions that affect the computation of that tax.

(h) Except as otherwise provided by this section, a taxable entity [~~corporation~~] shall use the same accounting methods to apportion its taxable capital as it used to compute its taxable capital.

SECTION 2.16. Sections 171.1121(a)-(d), Tax Code, are amended to read as follows:

(a) For purposes of this section, "gross receipts" means all revenues reportable by a taxable entity [~~corporation~~] on its federal tax return, without deduction for the cost of property sold, materials used, labor performed, or other costs incurred, unless otherwise specifically provided in this chapter. "Gross receipts" does not include revenues that are not included in taxable earned surplus. For example, Schedule C special deductions and any amounts subtracted from reportable federal taxable income under Section 171.110(a) [~~171.110(a)(1)~~] are not included in taxable earned surplus and therefore are not considered gross receipts.

(b) Except as otherwise provided by this section, a taxable entity [~~corporation~~] shall use the same accounting methods to apportion taxable earned surplus as used in computing reportable federal taxable income.

(c) A taxable entity [~~corporation~~] shall report its gross receipts based solely on its own financial condition. Consolidated reporting is prohibited.

(d) Unless the provisions of Section 171.111 apply due to an election under that section, a taxable entity [~~corporation~~] may not

change its accounting methods used to calculate gross receipts more often than once every four years without the express written consent of the comptroller. A change in accounting methods is not justified solely because it results in a reduction of tax liability.

SECTION 2.17. Section 171.113, Tax Code, is amended to read as follows:

Sec. 171.113. ALTERNATE METHOD OF DETERMINING TAXABLE CAPITAL AND GROSS RECEIPTS FOR CERTAIN TAXABLE ENTITIES [~~CORPORATIONS~~]. (a) This section applies only to:

(1) a corporation organized as a close corporation under Part 12, Texas Business Corporation Act, that has not more than 35 shareholders;

(2) a foreign corporation organized under the close corporation law of another state that has not more than 35 shareholders; [~~and~~]

(3) an S corporation as that term is defined by Section 1361, Internal Revenue Code of 1986 (26 U.S.C. Section 1361); and

(4) a taxable entity other than a corporation that has 35 or fewer owners.

(b) A taxable entity [~~corporation~~] to which this section applies may elect to compute its surplus, assets, debts, and gross receipts according to the method the taxable entity [~~corporation~~] uses to report its federal income tax instead of as provided by Sections 171.109(b) and (g) and Section 171.112(b). This section does not affect the application of the other subsections of Sections 171.109 and 171.112 and other provisions of this chapter to a taxable entity [~~corporation~~] making the election.

(c) The comptroller may adopt rules as necessary to specify the reporting requirements for taxable entities [~~corporations~~] to which this section applies.

(d) This section does not apply to a subsidiary of a taxable entity [~~corporation~~] unless it applies to the parent [~~corporation~~] of the subsidiary.

(e) The election under Subsection (b) becomes effective when written notice of the election is received by the comptroller from the taxable entity [~~corporation~~]. An election under

Subsection (b) must be postmarked not later than the due date for the electing taxable entity's [~~corporation's~~] franchise tax report to which the election applies.

SECTION 2.18. Chapter 171, Tax Code, is amended by adding Subchapter C-1 to read as follows:

SUBCHAPTER C-1. TAXABLE WAGES

Sec. 171.131. TAXABLE WAGES. (a) In this section:

(1) "Employee" means an employee described by Section 171.133 or 171.134.

(2) "Wages" means:

(A) wages as defined under Subchapter F, Chapter 201, Labor Code, paid by a taxable entity and includes the amounts excluded by Sections 201.082(1) and (9), Labor Code; and

(B) wages, to the extent not covered by Paragraph (A), described under Section 171.132.

(b) The taxable wages of a taxable entity are the total amount of wages paid by the entity to all of the entity's employees during the reporting period as provided by Section 171.1533.

Sec. 171.132. LOCATION OF SERVICE. (a) Wages include wages for a service performed in this state or in and outside this state if:

(1) the service is localized in this state; or

(2) the service is not localized in any state and some of the service is performed in this state and:

(A) the base of operations is in this state, or there is no base of operations but the service is directed or controlled from this state; or

(B) the base of operations or place from which the service is directed or controlled is not in a state in which a part of the service is performed, and the residence of the person who performs the service is in this state.

(b) Wages include wages for a service performed anywhere in the United States, including service performed entirely outside this state, if:

(1) the service is not localized in a state;

(2) the service is performed by an individual who is one of a class of employees who are required to travel outside this

state in performance of their duties; and

(3) the individual's base of operations is in this state or, if there is no base of operations, the individual's service is directed or controlled from this state.

(c) Wages include wages for a service performed outside the United States by a citizen of the United States.

(d) For the purposes of this section, service is localized in a state if the service is performed entirely within the state or the service performed outside the state is incidental to the service performed in the state. In this section, a service that is "incidental" includes a service that is temporary or that consists of isolated transactions.

Sec. 171.133. FULL-TIME AND PART-TIME EMPLOYEES. (a) In this section, "contribution" has the meaning assigned that term by Section 201.011, Labor Code.

(b) An individual is an employee if the taxable entity pays or is required to pay a contribution for a reporting period without regard to whether:

(1) the individual is a full-time or part-time employee; or

(2) the wages paid were for the entire reporting period or a portion of the reporting period.

Sec. 171.134. DETERMINATION OF WHETHER CERTAIN INDIVIDUALS ARE EMPLOYEES. An individual is an employee of a taxable entity as provided by this section, without regard to whether the taxable entity pays a contribution for the individual, if the individual provides services in this state to the taxable entity for compensation and the taxable entity has a right to direct and control how the individual performs the services for which the individual is provided compensation, indicated by factors that include:

(1) whether the individual is subject to the taxable entity's instructions about when, where, and how to work;

(2) whether the individual is trained to perform services in a particular manner;

(3) the extent to which the individual has unreimbursed business expenses;

(4) the extent to which the individual has a significant investment in the facilities the individual uses in performing the services;

(5) the extent to which the individual makes the individual's services available to the relevant market by advertising, by maintaining a visible business location, or otherwise;

(6) the extent to which the individual can realize a profit or loss;

(7) the manner in which the individual is paid by the taxable entity;

(8) whether a written contract between the individual and the taxable entity provides that the individual is or is not an employee;

(9) whether the taxable entity provides the individual with employee-type benefits, including insurance, a pension plan, vacation pay, or sick pay;

(10) whether the relationship between the individual and the taxable entity is considered permanent or for a limited period; and

(11) the extent to which services performed by the individual are a key aspect of the affairs of the taxable entity.

SECTION 2.19. Section 171.151, Tax Code, is amended to read as follows:

Sec. 171.151. PRIVILEGE PERIOD COVERED BY TAX. The franchise tax shall be paid for each of the following:

(1) an initial period beginning on the taxable entity's [~~corporation's~~] beginning date and ending on the day before the first anniversary of the beginning date;

(2) a second period beginning on the first anniversary of the beginning date and ending on December 31 following that date; and

(3) after the initial and second periods have expired, a regular annual period beginning each year on January 1 and ending the following December 31.

SECTION 2.20. Section 171.152(c), Tax Code, is amended to read as follows:

(c) Payment of the tax covering the regular annual period is due May 15, of each year after the beginning of the regular annual period. However, if the first anniversary of the taxable entity's [~~corporation's~~] beginning date is after October 3 and before January 1, the payment of the tax covering the first regular annual period is due on the same date as the tax covering the initial period.

SECTION 2.21. Sections 171.153(a) and (c), Tax Code, are amended to read as follows:

(a) The tax covering the initial period is reported on the initial report and is based on the business done by the taxable entity [~~corporation~~] during the period beginning on the taxable entity's [~~corporation's~~] beginning date and:

(1) ending on the last accounting period ending date that is at least six months after the beginning date and at least 60 days before the original due date of the initial report; or

(2) if there is no such period ending date in Subdivision (1) [~~of this subsection~~], then ending on the day that is the last day of a calendar month and that is nearest to the end of the taxable entity's [~~corporation's~~] first year of business; or

(3) ending on the day after the merger occurs, for the survivor of a merger which occurs after the day on which the tax is based in Subdivision (1) or [~~Subdivision~~] (2), whichever is applicable, [~~of Subsection (a)~~] and before January 1, of the year an initial report is due by the survivor.

(c) The tax covering the regular annual period is based on the business done by the taxable entity [~~corporation~~] during its last accounting period that ends in the year before the year in which the tax is due; unless a taxable entity [~~corporation~~] is the survivor of a merger which occurs between the end of its last accounting period in the year before the report year and January 1 of the report year, in which case the tax will be based on the financial condition of the surviving taxable entity [~~corporation~~] for the 12-month period ending on the day after the merger. However, if the first anniversary of the taxable entity's [~~corporation's~~] beginning date is after October 3 and before January 1, the tax covering the first regular annual period is based

on the same business on which the tax covering the initial period is based and is reported on the initial report.

SECTION 2.22. Section 171.1532, Tax Code, is amended to read as follows:

Sec. 171.1532. BUSINESS ON WHICH TAX ON NET TAXABLE EARNED SURPLUS IS BASED. (a) The tax covering the privilege periods included on the initial report, as required by Section 171.153, is based on the business done by the taxable entity [~~corporation~~] during the period beginning on the taxable entity's [~~corporation's~~] beginning date and:

(1) ending on the last accounting period ending date that is at least 60 days before the original due date of the initial report; or

(2) if there is no such period ending date in Subdivision (1) [~~of this subsection~~], then ending on the day that is the last day of a calendar month and that is nearest to the end of the taxable entity's [~~corporation's~~] first year of business.

(b) The tax covering the regular annual period, other than a regular annual period included on the initial report, is based on the business done by the taxable entity [~~corporation~~] during the period beginning with the day after the last date upon which net taxable earned surplus on a previous report was based and ending with its last accounting period ending date for federal income tax purposes in the year before the year in which the report is originally due.

SECTION 2.23. Subchapter D, Chapter 171, Tax Code, is amended by adding Section 171.1533 to read as follows:

Sec. 171.1533. WAGES ON WHICH TAX ON TAXABLE WAGES IS BASED. (a) The tax covering the privilege periods included on the initial report, as required by Section 171.153, is based on the taxable wages paid by the taxable entity during the period beginning on the taxable entity's beginning date and:

(1) ending on the last accounting period ending date that is at least 60 days before the original due date of the initial report; or

(2) if there is no such period ending date in Subdivision (1), then ending on the day that is the last day of a

calendar month and that is nearest to the end of the taxable entity's first year of business.

(b) The tax covering the regular annual period, other than a regular annual period included on the initial report, is based on the taxable wages paid by the taxable entity during the period beginning with the day after the last date on which taxable wages on a previous report was based and ending with its last accounting period ending date for federal income tax purposes in the year before the year in which the report is originally due.

SECTION 2.24. Section 171.154, Tax Code, is amended to read as follows:

Sec. 171.154. PAYMENT TO COMPTROLLER. A taxable entity [~~corporation~~] on which a tax is imposed by this chapter shall pay the tax to the comptroller.

SECTION 2.25. Section 171.201, Tax Code, is amended to read as follows:

Sec. 171.201. INITIAL REPORT. (a) Except as provided by Section 171.2022, a taxable entity [~~corporation~~] on which the franchise tax is imposed shall file an initial report with the comptroller containing:

(1) information showing the financial condition of the taxable entity [~~corporation~~] on the day that is the last day of a calendar month and that is nearest to the end of the taxable entity's [~~corporation's~~] first year of business;

(2) the name and address of:

(A) each officer, [~~and~~] director, and manager of the taxable entity [~~corporation~~];

(B) for a limited partnership, each general partner;

(C) for a limited liability partnership, each managing partner or, if there is not a managing partner, each partner; or

(D) for a trust, each trustee;

(3) the name and address of the agent of the taxable entity [~~corporation~~] designated under Section 171.354; [~~and~~]

(4) a statement declaring the entity's election of rate required under Section 171.0011 or 171.0012, as applicable;

and

(5) other information required by the comptroller.

(b) The taxable entity [~~corporation~~] shall file the report on or before the date the payment is due under Subsection (a) of Section 171.152.

SECTION 2.26. Sections 171.202(a)-(f) and (i), Tax Code, are amended to read as follows:

(a) Except as provided by Section 171.2022, a taxable entity [~~corporation~~] on which the franchise tax is imposed shall file an annual report with the comptroller containing:

(1) financial and other information of the taxable entity [~~corporation~~] necessary to compute the tax under this chapter on both the rate provided by Section 171.002 and the alternate rate provided by Section 171.003;

(2) the name and address of each officer and director of the taxable entity [~~corporation~~];

(3) the name and address of the agent of the taxable entity [~~corporation~~] designated under Section 171.354; [~~and~~]

(4) if applicable, a statement declaring that the election period provided by Section 171.0011(b) has expired and the entity's election of rate under Section 171.0011 or 171.0012, as applicable, for the next election period; and

(5) other information required by the comptroller.

(b) The taxable entity [~~corporation~~] shall file the report before May 16 of each year after the beginning of the regular annual period. The report shall be filed on forms supplied by the comptroller.

(c) The comptroller shall grant an extension of time to a taxable entity [~~corporation~~] that is not required by rule to make its tax payments by electronic funds transfer for the filing of a report required by this section to any date on or before the next November 15, if a taxable entity [~~corporation~~]:

(1) requests the extension, on or before May 15, on a form provided by the comptroller; and

(2) remits with the request:

(A) not less than 90 percent of the amount of tax reported as due on the report filed on or before November 15; or

(B) 100 percent of the tax reported as due for the previous calendar year on the report due in the previous calendar year and filed on or before May 14.

(d) In the case of a taxpayer whose previous return was its initial report, the optional payment provided under Subsection (c)(2)(B) or (e)(2)(B) must be equal to the greater of:

(1) an amount produced by multiplying the net taxable capital, as reported on the initial report filed on or before May 14, by the rate of tax in Section 171.002(a)(1) that is effective January 1 of the year in which the report is due; [~~or~~]

(2) an amount produced by multiplying the net taxable earned surplus, as reported on the initial report filed on or before May 14, by the rate of tax in Section 171.002(a)(2) that is effective January 1 of the year in which the report is due; or

(3) an amount produced by multiplying taxable wages, as reported on the initial report filed on or before May 14, by the rate of tax in Section 171.003 that is effective January 1 of the year in which the report is due.

(e) The comptroller shall grant an extension of time for the filing of a report required by this section by a taxable entity [~~corporation~~] required by rule to make its tax payments by electronic funds transfer to any date on or before the next August 15, if the taxable entity [~~corporation~~]:

(1) requests the extension, on or before May 15, on a form provided by the comptroller; and

(2) remits with the request:

(A) not less than 90 percent of the amount of tax reported as due on the report filed on or before August 15; or

(B) 100 percent of the tax reported as due for the previous calendar year on the report due in the previous calendar year and filed on or before May 14.

(f) The comptroller shall grant an extension of time to a taxable entity [~~corporation~~] required by rule to make its tax payments by electronic funds transfer for the filing of a report due on or before August 15 to any date on or before the next November 15, if the taxable entity [~~corporation~~]:

(1) requests the extension, on or before August 15, on

a form provided by the comptroller; and

(2) remits with the request the difference between the amount remitted under Subsection (e) and 100 percent of the amount of tax reported as due on the report filed on or before November 15.

(i) If a taxable entity [~~corporation~~] requesting an extension under Subsection (c) or (e) does not file the report due in the previous calendar year on or before May 14, the taxable entity [~~corporation~~] may not receive an extension under Subsection (c) or (e) unless the taxable entity [~~corporation~~] complies with Subsection (c)(2)(A) or (e)(2)(A), as appropriate.

SECTION 2.27. Section 171.2022, Tax Code, is amended to read as follows:

Sec. 171.2022. EXEMPTION FROM REPORTING REQUIREMENTS. A taxable entity [~~corporation~~] that does not owe any tax under this chapter for any period is not required to file a report under Section 171.201 or[~~,~~] 171.202[~~, or 171.2021~~]. The exemption applies only to a period for which no tax is due.

SECTION 2.28. Section 171.204, Tax Code, is amended to read as follows:

Sec. 171.204. INFORMATION REPORT. (a) Except as provided by Subsection (b), to determine eligibility for the exemption provided by Section 171.2022, or to determine the amount of the franchise tax or the correctness of a franchise tax report, the comptroller may require [~~an officer of~~] a taxable entity [~~corporation~~] that may be subject to the tax imposed under this chapter to file an information report with the comptroller stating the amount of the taxable entity's [~~corporation's~~] taxable capital, [~~and~~] earned surplus, wages paid, or any other information the comptroller may request.

(b) The comptroller may require a taxable entity [~~an officer of a corporation~~] that does not owe any tax because of the application of Section 171.004(2) [~~171.002(d)(2)~~] to file an abbreviated information report with the comptroller stating the amount of the taxable entity's [~~corporation's~~] gross receipts from its entire business. The comptroller may not require a taxable entity [~~corporation~~] described by this subsection to file an information report that requires the taxable entity [~~corporation~~]

to report or compute its earned surplus, [~~or~~] taxable capital, or wages paid.

SECTION 2.29. Section 171.205, Tax Code, is amended to read as follows:

Sec. 171.205. ADDITIONAL INFORMATION REQUIRED BY COMPTROLLER. The comptroller may require a taxable entity [~~corporation~~] on which the franchise tax is imposed to furnish to the comptroller information from the taxable entity's [~~corporation's~~] books and records that has not been filed previously and that is necessary for the comptroller to determine the amount of the tax.

SECTION 2.30. Section 171.206, Tax Code, is amended to read as follows:

Sec. 171.206. CONFIDENTIAL INFORMATION. Except as provided by Section 171.207 [~~of this code~~], the following information is confidential and may not be made open to public inspection:

(1) information that is obtained from a record or other instrument that is required by this chapter to be filed with the comptroller; or

(2) information, including information about the business affairs, operations, profits, losses, or expenditures of a taxable entity [~~corporation~~], obtained by an examination of the books and records, officers, partners, trustees, agents, or employees of a taxable entity [~~corporation~~] on which a tax is imposed by this chapter.

SECTION 2.31. Section 171.208, Tax Code, is amended to read as follows:

Sec. 171.208. PROHIBITION OF DISCLOSURE OF INFORMATION. A person, including a state officer or employee or an owner [~~a shareholder~~] of a taxable entity [~~corporation~~], who has access to a report filed under this chapter may not make known in a manner not permitted by law the amount or source of the taxable entity's [~~corporation's~~] income, profits, losses, expenditures, or other information in the report relating to the financial condition of the taxable entity [~~corporation~~].

SECTION 2.32. Section 171.209, Tax Code, is amended to read as follows:

Sec. 171.209. RIGHT OF OWNER [~~SHAREHOLDER~~] TO EXAMINE OR RECEIVE REPORTS. If an owner [~~a person owning at least one share of outstanding stock~~] of a taxable entity [~~corporation~~] on whom the franchise tax is imposed presents evidence of the ownership to the comptroller, the person is entitled to examine or receive a copy of an initial or annual report that is filed under Section 171.201 or 171.202 [~~of this code~~] and that relates to the taxable entity [~~corporation~~].

SECTION 2.33. Section 171.211, Tax Code, is amended to read as follows:

Sec. 171.211. EXAMINATION OF [~~CORPORATE~~] RECORDS. To determine the franchise tax liability of a taxable entity [~~corporation~~], the comptroller may investigate or examine the records of the taxable entity [~~corporation~~].

SECTION 2.34. Subchapter E, Chapter 171, Tax Code, is amended by adding Section 171.213 to read as follows:

Sec. 171.213. ACCESS TO TEXAS WORKFORCE COMMISSION REPORTS. The comptroller shall have full access to reports filed by a taxable entity on wages paid with the Texas Workforce Commission.

SECTION 2.35. The heading to Subchapter F, Chapter 171, Tax Code, is amended to read as follows:

SUBCHAPTER F. FORFEITURE OF CORPORATE AND BUSINESS PRIVILEGES

SECTION 2.36. Subchapter F, Chapter 171, Tax Code, is amended by adding Section 171.2515 to read as follows:

Sec. 171.2515. FORFEITURE OF RIGHT OF PARTNERSHIP TO TRANSACT BUSINESS IN THIS STATE. (a) The comptroller may, for the same reasons and using the same procedures the comptroller uses in relation to the forfeiture of the corporate privileges of a corporation, forfeit the right of a partnership subject to a tax imposed by this chapter to transact business in this state.

(b) The provisions of this subchapter, including Section 171.255, that apply to the forfeiture of corporate privileges apply to the forfeiture of a partnership's right to transact business in this state.

SECTION 2.37. Section 171.351, Tax Code, is amended to read as follows:

Sec. 171.351. VENUE OF SUIT TO ENFORCE CHAPTER. Venue of a

civil suit against a taxable entity [~~corporation~~] to enforce this chapter is either in a county where the taxable entity's [~~corporation's~~] principal office is located according to its charter or certificate of authority or in Travis County.

SECTION 2.38. Section 171.353, Tax Code, is amended to read as follows:

Sec. 171.353. APPOINTMENT OF RECEIVER. If a court forfeits a taxable entity's [~~corporation's~~] charter or certificate of authority, the court may appoint a receiver for the taxable entity [~~corporation~~] and may administer the receivership under the laws relating to receiverships.

SECTION 2.39. Section 171.354, Tax Code, is amended to read as follows:

Sec. 171.354. AGENT FOR SERVICE OF PROCESS. Each taxable entity [~~corporation~~] on which a tax is imposed by this chapter shall designate a resident of this state as the taxable entity's [~~corporation's~~] agent for the service of process.

SECTION 2.40. Sections 171.362(a), (d), and (e), Tax Code, are amended to read as follows:

(a) If a taxable entity [~~corporation~~] on which a tax is imposed by this chapter fails to pay the tax when it is due and payable or fails to file a report required by this chapter when it is due, the taxable entity [~~corporation~~] is liable for a penalty of five percent of the amount of the tax due.

(d) If a taxable entity [~~corporation~~] electing to remit under [~~Paragraph (A) of Subdivision (2) of Subsection (c) of~~] Section 171.202(c)(2)(A) [~~171.202 of this code~~] remits less than the amount required, the penalties imposed by this section and the interest imposed under Section 111.060 [~~of this code~~] are assessed against the difference between the amount required to be remitted under [~~Paragraph (A) of Subdivision (2) of Subsection (c) of~~] Section 171.202(c)(2)(A) [~~171.202~~] and the amount actually remitted on or before May 15.

(e) If a taxable entity [~~corporation~~] remits the entire amount required by [~~Subsection (c) of~~] Section 171.202(c) [~~171.202 of this code~~], no penalties will be imposed against the amount remitted on or before November 15.

SECTION 2.41. Sections 171.363(a) and (b), Tax Code, are amended to read as follows:

(a) A taxable entity [~~corporation~~] commits an offense if the taxable entity [~~corporation~~] is subject to the provisions of this chapter and the taxable entity [~~corporation~~] wilfully:

(1) fails to file a report;

(2) fails to keep books and records as required by this chapter;

(3) files a fraudulent report;

(4) violates any rule of the comptroller for the administration and enforcement of the provisions of this chapter; or

(5) attempts in any other manner to evade or defeat any tax imposed by this chapter or the payment of the tax.

(b) A person commits an offense if the person is an accountant or an agent for or an officer or employee of a taxable entity [~~corporation~~] and the person knowingly enters or provides false information on any report, return, or other document filed by the taxable entity [~~corporation~~] under this chapter.

SECTION 2.42. Subchapter H, Chapter 171, Tax Code, is amended by adding Sections 171.364-171.366 to read as follows:

Sec. 171.364. TAX NOT DEDUCTED FROM WAGES. A taxable entity may not deduct the tax imposed under this chapter from any wages of the taxable entity's employees.

Sec. 171.365. CRIMINAL PENALTY. (a) A person who violates Section 171.364 commits an offense.

(b) An offense under this section is a Class A misdemeanor.

Sec. 171.366. CIVIL PENALTY. (a) A person who violates Section 171.364 is liable to the state for a civil penalty not to exceed $500 for each violation. Each day a violation continues may be considered a separate violation for purposes of a civil penalty assessment.

(b) On request of the comptroller, the attorney general shall file suit to collect a penalty under this section.

SECTION 2.43. Section 171.401, Tax Code, is amended to read as follows:

Sec. 171.401. REVENUE DEPOSITED IN GENERAL REVENUE FUND.

The revenue from the tax imposed by this chapter [~~on corporations~~] shall be deposited to the credit of the general revenue fund.

SECTION 2.44. Chapter 171, Tax Code, is amended by adding Subchapter I-1 to read as follows:

SUBCHAPTER I-1. APPLICATION OF REFUNDS AND CREDITS TO NONCORPORATE TAXABLE ENTITIES

Sec. 171.451. APPLICATION OF REFUNDS AND CREDITS TO NONCORPORATE TAXABLE ENTITIES. Except as provided by Section 171.452, a taxable entity that is not a corporation but that, because of its activities, would qualify for a specific refund or credit under this chapter if it were a corporation qualifies for the refund or credit in the same manner and under the same conditions as a corporation.

Sec. 171.452. TAXABLE ENTITIES ELECTING ALTERNATE RATE NOT ELIGIBLE FOR CREDITS. Notwithstanding any other provision of this chapter, a taxable entity that elects to pay the tax under this chapter at the alternate rate provided by Section 171.003 is not entitled to a credit under Subchapters J-U.

SECTION 2.45. Chapter 171, Tax Code, is amended by adding Subchapter X to read as follows:

SUBCHAPTER X. TAX CREDIT FOR CERTAIN PROVIDERS OF HEALTH CARE SERVICES

Sec. 171.941. DEFINITION of HEALTH CARE PROVIDER. In this subchapter, "health care provider" means:

(1) an ambulatory surgical center;

(2) an assisted living facility licensed under Chapter 247, Health and Safety Code;

(3) an emergency medical services provider;

(4) a home and community support services agency;

(5) a hospice;

(6) a hospital;

(7) a hospital system;

(8) an intermediate care facility for the mentally retarded or a home and community-based services waiver program for persons with mental retardation adopted in accordance with Section 1915(c) of the federal Social Security Act (42 U.S.C. Section 1396n);

(9) a nursing home;

(10) an end stage renal disease facility licensed under Section 251.011, Health and Safety Code; or

(11) a taxable entity providing health care services, including physician's services, that participates in the Medicaid program, the Medicare program, or the Children's Health Insurance Program (CHIP) as a provider of health care services.

Sec. 171.942. QUALIFICATION. A health care provider is entitled to a credit in the amount provided by Section 171.943 against the taxes imposed under this chapter for the period on which earned surplus is based if, for that period, the provider received not less than 15 percent of the provider's revenue from payments received under the Medicaid program, the Medicare program, or the Children's Health Insurance Program (CHIP).

Sec. 171.943. AMOUNT OF CREDIT. The amount of credit for a health care provider is equal to an amount computed by:

(1) determining a fraction:

(A) the numerator of which is the total amount of payments the provider received under the Medicaid program, the Medicare program, or the Children's Health Insurance Program (CHIP), for the period on which earned surplus is based; and

(B) the denominator of which is the gross receipts of the provider from business done in this state as determined under Section 171.1032 for the period on which earned surplus is based; and

(2) multiplying the fraction determined under Subdivision (1) by the tax liability of the provider under this chapter for the period on which earned surplus is based.

Sec. 171.944. LIMITATIONS. (a) A health care provider may not receive a credit in an amount that exceeds the amount of the tax or assessment due after applying any other credits.

(b) A health care provider may not convey, assign, or transfer the credit allowed under this subchapter to another entity unless all of the assets of the provider are conveyed, assigned, or transferred in the same transaction.

(c) A health care provider that participates in the Medicaid program, the Medicare program, or the Children's Health Insurance

Program (CHIP) as a provider of durable medical equipment or as a vendor of pharmaceuticals may not count payments for those services for purposes of qualifying for or receiving the exemption under this subchapter.

Sec. 171.945. RULES. The comptroller shall adopt rules to implement this subchapter. The Health and Human Services Commission shall assist the comptroller in the formulation and adoption of the rules.

SECTION 2.46. If a credit under Chapter 171, Tax Code, is found by a court in a final judgment upheld on appeal or no longer subject to appeal to be unconstitutional, the credit is disallowed for all entities on or after the date of the judgment, and an entity is not entitled to and may not apply for the credit the entity has not received on or after that date for any reporting period beginning before, on, or after that date.

SECTION 2.47. (a) For an entity becoming subject to the franchise tax under this Act:

(1) income or losses, and related gross receipts, earned, paid, or accrued before January 1, 2005, may not be considered for purposes of the earned surplus component, or for apportionment purposes for the taxable capital component;

(2) an entity subject to the franchise tax on January 1, 2006, for which January 1, 2006, is not the beginning date, shall file an annual report due May 15, 2006, based on the period:

(A) beginning the later of:

(i) January 1, 2005; or

(ii) the date the entity was organized in this state, or, if a foreign entity, the date it began doing business in this state; and

(B) ending on the date the entity's last accounting period ends in 2005 or, if none, on December 31, 2005; and

(3) an entity subject to the earned surplus component of the franchise tax at any time after October 31, 2005, and before January 1, 2006, but not subject to the earned surplus component on January 1, 2006, shall file a final report computed on net taxable earned surplus, for the privilege of doing business at any time

after October 31, 2005, and before January 1, 2006, based on the period:

(A) beginning the later of:

(i) January 1, 2005; or

(ii) the date the entity was organized in this state, or, if a foreign entity, the date it began doing business in this state; and

(B) ending on the date the entity became no longer subject to the earned surplus component of the tax.

(b) For purposes of this article, an existing partnership is considered as continuing if it is not terminated.

(c) A partnership is considered terminated only if no part of any business, financial operation, or venture of the partnership continues to be carried on by any of its partners in a partnership.

(d) For a merger or consolidation of two or more partnerships, the resulting partnership is, for purposes of this article, considered the continuation of any merging or consolidating partnership whose members own an interest of more than 50 percent in the capital and profits of the resulting partnership.

(e) For a division of a partnership into two or more partnerships, the resulting partnerships, other than any resulting partnership the members of which had an interest of 50 percent or less in the capital and profits of the prior partnership, are, for purposes of this article, considered a continuation of the prior partnership.

SECTION 2.48. This article takes effect November 1, 2005, and applies to reports originally due on or after that date.