JURISDICTION: **OKLAHOMA TAX COMMISSION**
CITE: **2012-02-07-12 / NON-PRECEDENTIAL**
ID: **P-11-538-H**
DATE: **FEBRUARY 7, 2012**
DISPOSITION: **DENIED**
TAX TYPE: **INCOME**
APPEAL: **NO APPEAL TAKEN**

FINDINGS OF FACT AND CONCLUSIONS OF LAW

COMPANY ("Protestant") appears through its Chief Financial Officer ("CFO"), CFO, CPA. The Corporate Income Tax Section, Compliance Division ("Division") of the Oklahoma Tax Commission, appears through OTC ATTORNEY 1, Assistant General Counsel, and OTC ATTORNEY 2, Assistant General Counsel, Office of General Counsel, Oklahoma Tax Commission.

PROCEDURAL HISTORY

On August 25, 2011, the protest file was received by the Office of Administrative Law Judges for further proceedings consistent with the *Uniform Tax Procedure Code*[1] and the *Rules of Practice and Procedure Before the Office of Administrative Law Judges*.[2] On August 30, 2011, OTC ATTORNEY 1 and OTC ATTORNEY 2 filed an Entry of Appearance as Co-Counsel of record for the Division. On August 31, 2011, a letter was mailed to CFO stating this matter had been assigned to ALJ, Administrative Law Judge, and docketed as Case Number P-11-538-H. The letter also advised CFO that a Notice of Prehearing Conference would be sent by mail and enclosed a copy of the *Rules of Practice and Procedure Before the Office of Administrative Law Judges.*[3]

On September 12, 2011, the Notice of Prehearing Conference was mailed to the last-known address of CFO, setting the prehearing conference for October 11, 2011, at 9:30 a.m.[4] On September 23, 2011, a Status Report In Lieu of Prehearing Conference was filed with the Court Clerk, as more fully set forth therein.[5] On September 26, 2011, a Scheduling Order was issued for submission of this matter on stipulations and briefs, as more fully set forth therein.[6]

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[1] OKLA. STAT. ANN. tit. 68, § 201 et seq. (West 2001).

[2] OKLA. ADMIN. CODE §§ 710:1-5-20 through 710:1-5-47.

[3] *Id.*

[4] OKLA. STAT. ANN. tit. 68, § 208 (West Supp. 2012).

[5] OKLA. ADMIN. CODE § 710:1-5-10(c)(2) (June 25, 1999).

[6] OKLA. ADMIN. CODE § 710:710:1-5-38(a) (June 25, 2009).

On October 28, 2011, the parties filed Joint Stipulations of Facts and Issues, with Exhibits A through G attached thereto.

The Protestant's brief-in-chief was due November 15, 2011, but the brief was not filed with the Court Clerk.

On December 2, 2011, the Brief of the Compliance Division was filed with the Court Clerk. According to the Scheduling Order, the Protestant could file a response to the Division's Brief-In-Chief on or before December 12, but a response brief was not filed with the Court Clerk. The record in this matter was closed and this case was submitted for decision on December 14, 2011.

JOINT STIPULATION OF FACTS AND ISSUES

On October 28, 2011, the parties filed Joint Stipulation of Facts and Issues,[7] with Exhibits A through G attached thereto, as follows, to-wit:

STATEMENT OF FACTS

1. On or about March 7, 2005, Protestant filed its 2004 Small Business Corporation Income Tax Return. The 2004 Return is attached hereto as **Exhibit A**. On Line 1, Protestant claimed that its nonresident share of income was a loss in the amount of $5,400.00. The 2004 return did not contain a statement electing to forego the standard statutory carryback period for a net operating loss ("NOL").

2. On or about March 14, 2006, Protestant filed its 2005 Small Business Corporation Income Tax Return. The 2005 Return is attached hereto as **Exhibit B**. On Line 1, Protestant claimed that its nonresident share of income was loss in the amount of $135,914.00. The 2005 return did not contain a statement electing to forego the standard statutory carryback period for a NOL.

3. On or about March 11, 2008, Protestant filed its 2007 Small Business Corporation Income Tax Return. The 2007 Return is attached hereto as **Exhibit C**. On Line 1b, Protestant claimed a deduction in the amount of $225,445.00. This deduction was comprised of the NOLs generated by Protestant in tax years 2004, 2005, and 2006.

4. By letter dated February 18, 2009, the Compliance Division notified Protestant of adjustments made to Protestant's 2007 Return. The 2007 adjustment letter is attached hereto as **Exhibit D**. The letter explained that the adjustments were made because Protestant did not make a "timely" election…to forego the carry back period for net operating losses sustained." The letter further showed that, because of Protestant's failure to make the timely election, the 2004

[7] The text of the stipulated facts is set out *in haec verba*. "***in haec vega***" (in heek v<<schwa>>r-b<<schwa>>). [Latin] In these same words; verbatim. BLACK'S LAW DICTIONARY (8TH ed. 2004), available at http://westlaw.com.

NOL in the amount of $5,400.00 was carried back to tax year 2002 and the 2005 NOL in the amount of $135,914.00 was carried back to tax year 2003.

5. The Division's adjustment to Protestant's 2007 Return did not result in an assessment of additional tax against Protestant, and Protestant did not protest the 2007 adjustment.

6. On or about March 8, 2011, Protestant filed its 2010 Oklahoma Small Business Corporation Income Tax Return. The 2010 Return is attached hereto as **Exhibit E**. On Line 1b, Protestant claimed a deduction in the amount of $299,438.00. The deduction was comprised of NOLs for tax years 2004 through 2009, as shown on "Attachment A" to the 2010 Return.

7. By letter dated August 9, 2011, the Compliance Division issued its assessment of additional income tax against Protestant for the 2010 tax year in the amount of $4,618.00 in income tax, $378.00 in interest, and $462.00 in penalty for a total of $5,458.00. The assessment letter, with attachments, is attached hereto as **Exhibit F**.

8. The workpaper attached to the August 9, 2011, assessment showed that the NOL available for tax year 2010 was reduced from $299,438.00 as filed to $158,124.00 as adjusted. The adjusted NOL amount applied to 2010 is equal to the sum of the NOLs generated in tax years 2006 through 2009. The Division disallowed the portion of the NOL attributable to losses generated in tax years 2004 and 2005 for which Protestant did not elect to forego the carryback period. The workpaper referred to the adjustment letter issued by the Division on February 18, 2009, for the 2007 tax year for further explanation regarding disallowance of the 2004 and 2005 NOL amounts.

9. On or about August 15, 2011, Protestant filed a protest letter disagreeing with the Division's adjustments. The protest letter is attached hereto as **Exhibit G**.

STATEMENT OF ISSUES

10. At issue in this matter is whether Protestant is entitled to apply a Net Operating Loss generated in tax years 2004 and 2005 to tax year 2010.

11. Protestant maintains that the adjustments to its 2010 return were unwarranted because it should not be penalized for following the Oklahoma Form 512-S instructions which make no reference to a NOL carryback, and that Form 512-S filers are subjected to punitive treatment for not following NOL instructions that are provided for Form 512 filers.

12. The Division maintains that its adjustments disallowing the NOL carryforward for 2004 and 2005 were correct because Protestant failed to comply with the procedural requirement that an election to forego the statutorily proscribed NOL carryback period must be part of the timely filed tax return for that year. Therefore, the Division maintains that the losses for 2004 and 2005 must be carried back two years before being carried forward.

CONCLUSIONS OF LAW

1. The Oklahoma Tax Commission is vested with jurisdiction over the parties and subject matter of this proceeding.[8]

2. The rules promulgated pursuant to the Administrative Procedures Act are presumed to be valid and binding on the persons they affect and have the force of law.[9]

3. In all proceedings before the Tax Commission, the taxpayer has the burden of proof.[10] A proposed assessment is presumed correct and the taxpayer bears the burden of showing that it is incorrect and in what respect.[11]

4. The carryover and carryback of Net Operating Losses ("NOLs") are governed by Section 2358(A)(3) of Title 68,[12] ("Statute") which provides in pertinent parts, as follows, to-wit:

> For all tax years beginning after December 31, 1981, taxable income and adjusted gross income shall be adjusted to arrive at Oklahoma taxable income and Oklahoma adjusted gross income as required by this section.
>
> A. The taxable income of any taxpayer shall be adjusted to arrive at Oklahoma taxable income for corporations and Oklahoma adjusted gross income for individuals, as follows:

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[8] OKLA. STAT. ANN. tit. 68, § 221(D) (West Supp. 2012). *See* OKLA. ADMIN. CODE § 710:1-5-38(a) (June 25, 1999).

[9] OKLA. STAT. ANN. tit. 75, § 250 et seq. (West 2002). *See Toxic Waste Impact Group, Inc. v. Leavitt*, 1988 OK 20, 755 P.2d 626.

[10] OKLA. ADMIN. CODE § 710:1-5-47 (June 25, 1999):

> In all administrative proceedings, unless otherwise provided by law, the burden of proof shall be upon the protestant to show in what respect the action or proposed action of the Tax Commission is incorrect. If, upon hearing, the protestant fails to prove a prima facie case, the Administrative Law Judge may recommend that the Commission deny the protest solely upon the grounds of failure to prove sufficient facts which would entitle the protestant to the requested relief.

OKLA. ADMIN. CODE § 710:1-5-77(b) (June 25, 1999), provides in pertinent part:

> …"preponderance of the evidence" means the evidence which is of greater weight or more convincing than the evidence which is offered in opposition to it; evidence which as a whole shows that the fact sought to be proved is more probable than not.

[11] *See Enterprise Management Consultants, Inc. v. State ex rel Oklahoma Tax Com'n*, 1988 OK 91, 768 P.2d 359.

[12] OKLA. STAT. ANN. tit. 68, § 2358(A)(3) (West Supp. 2012).

…

3. The amount of any federal net operating loss deduction shall be adjusted as follows:

…

(b) …For tax years beginning after December 31, 2000, and ending before January 1, 2008, the years to which such losses may be carried shall be determined solely by reference to Section 172 of the Internal Revenue Code, 26 U.S.C., Section 172, with the exception that the terms "net operating loss" and "taxable income" shall be replaced with "Oklahoma net operating loss" and "Oklahoma taxable income". For tax years beginning after December 31, 2007, and ending before January 1, 2009, years to which such losses may be carried back shall be limited to two (2) years. For tax years beginning after December 31, 2008, the years to which such losses may be carried back shall be determined solely by reference to Section 172 of the Internal Revenue Code, 26 U.S.C., Section 172, with the exception that the terms "net operating loss" and "taxable income" shall be replaced with "Oklahoma net operating loss" and "Oklahoma taxable income".

5. Section 172 of the Internal Revenue Code ("IRC") provides in pertinent part, as follows, to-wit:

(a) Deduction allowed.--There shall be allowed as a deduction for the taxable year an amount equal to the aggregate of (1) the net operating loss carryovers to such year, plus (2) the net operating loss carrybacks to such year. For purposes of this subtitle, the term "net operating loss deduction" means the deduction allowed by this subsection.

(b) Net operating loss carrybacks and carryovers.--

(1) Years to which loss may be carried.--

(A) General rule.--Except as otherwise provided in this paragraph, a net operating loss for any taxable year--

(i) shall be a net operating loss carryback to each of the 2 taxable years preceding the taxable year of such loss, and

(ii) shall be a net operating loss carryover to each of the 20 taxable years following the taxable year of the loss. (Emphasis original.)

6. The Tax Commission Rule for "Adjustments to Arrive at Oklahoma Taxable Income for Corporations" ("Rule") provides in pertinent parts,[13] as follows, to-wit:

> The following is a partial list and not inclusive of all the allowable and unallowable adjustments that may be made to Federal taxable income to arrive at Oklahoma taxable income for corporations: [**See:** 68 O.S. § 2358]
>
> …
>
> (3) **Federal loss carryback/carryforward.** A Federal net operating loss carryover or carryback will not be utilized in determining Oklahoma taxable income. For the allowance of Oklahoma Net Operating Loss deduction refer to (4) of this Section.
>
> (4) **Oklahoma net operating loss carryback/carryover.** An election may be made to forego the Net Operating Loss (NOL) carryback period. A written statement of the election must be part of the timely filed Oklahoma loss year return.
>
> (A) **Oklahoma net operating loss.** [**See:** 68 O.S. § 2358(A)(3)]
>
> …
>
> (V) For net operating losses incurred for tax years beginning on or after January 1, 2001, and before December 31, 2006 the loss **carryback** shall be for a period as allowed in the Internal Revenue Code.
>
> (VI) For net operating losses incurred for tax years beginning on or after January 1, 2007, and before December 31, 2007 the loss **carryback** shall be for a period of two (2) years. (Emphasis original.)

STATEMENT OF ISSUE

At issue in this matter is whether Protestant is entitled to apply a Net Operating Loss generated in tax years 2004 and 2005 to tax year 2010.

DISCUSSION

Protestant maintains that the adjustments to its 2010 return were unwarranted because it should not be penalized for following the Oklahoma Form 512-S instructions which make no reference to a NOL carryback, and that Form 512-S filers are subjected to punitive treatment for not following NOL instructions that are provided for Form 512 filers.

The Division maintains that its adjustments disallowing the NOL carryforward for 2004 and 2005 were correct because Protestant failed to comply with the procedural requirement that an election to forego the statutorily proscribed NOL carryback period must be part of the timely filed tax return for that year. Therefore, the Division maintains that the losses for 2004 and 2005 must be carried back two years before being carried forward.

[13] OKLA. ADMIN. CODE § 710:50-17-51 (July 11, 2010).

Statutes are interpreted to attain that purpose and end[14] championing the broad public policy purposes underlying them.[15] Only where the legislative intent cannot be ascertained from the statutory language, i.e. in cases of ambiguity or conflict, are rules of statutory construction employed.[16] However, where the statutory language is ambiguous or uncertain, a construction is applied to avoid absurdities.[17] Statutory construction presents a question of law.[18] Only where the intent cannot be ascertained from a statute's text, as occurs when ambiguity or conflict with other statutes is shown to exist, may rules of statutory construction be employed.[19] On this question, the Division's position is supported by the plain and unambiguous language of the Statute and the Rule. In addition, this specific issue has been previously decided by the Tax Commission in OTC (Precedential) Order No. 1995-03-23-017 (March 23, 1995),[20] which states in pertinent parts, as follows, to-wit:

> Generally, elections of a taxpayer for federal income tax purposes are bind[ing] on the taxpayer for all taxable periods and all purposes under the Oklahoma Income Tax Act. 68 O.S. 1981, §2353(3). An exception to the general rule exists where the Oklahoma Income Tax Act specifically provides otherwise. Id.
>
> Section 172 of the Internal Revenue Code allows taxpayers to elect to relinquish the entire carryback period with respect to a NOL for any taxable year ending after December 31, 1975. I.R.C. §172(b)(3)(C). Such election must be made by the due date of the loss year return and is irrevocable. Id.
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> The election under I.R.C. §172(b)(3)(C) for federal income tax purposes is not effective for Oklahoma income tax purposes since Section 2358(A)(3)(b) specifically provides otherwise. Section 2358(A)(3)(b) specifically provides for an Oklahoma NOL separate from a federal NOL which NOL shall be separately determined by reference to I.R.C. §172 and specifically provides for the separate determination by reference to I.R.C. §172 of the years to which such loss may be carried. Accordingly, a separate election to forego the carryback period for any Oklahoma NOL must be filed with the Oklahoma income tax return. See, Rule 710:50-17-51(4) of the Oklahoma Administrative Code.

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[14] *Keating v. Edmundson*, 2001 OK 110, 37 P.3d 882, ¶8. (Citations omitted).

[15] *Id.* at ¶8.

[16] *Id.* at ¶8.

[17] *Id.* at ¶8.

[18] *Blitz U.S.A., Inc. v. Oklahoma Tax Com'n*, 2003 OK 50, 75 P.3d 883.

[19] *Id.*

[20] *See* OTC Order No. 1997-03-18-017 (March 18, 1997).

> In this matter, Protestant filed its election to forego the carryback period and to carryover the 1987 federal NOL with its 1987 federal return. Protestant, however, failed to file the same election with its 1987 Oklahoma return for the 1987 Oklahoma NOL. This failure results in the required carryback of the 1987 Oklahoma NOL prior to the carryover of any portion of the 1987 Oklahoma NOL in accordance with I.R.C. §172(b)(1)(A) and (B) and (b)(2). Accordingly, the Division properly allocated a portion of Protestant's 1987 Oklahoma NOL to Protestant's 1986 Oklahoma return before allocating any portion of the 1987 Oklahoma NOL to Protestant's 1988 Oklahoma return.
>
> Protestant urges the waiver of the election requirement arguing the punitive effect on Protestant and its good faith effort to comply with the Oklahoma Statutes. Rule 23.09VII (currently Rule 710:50-17-51(4)) implements the provisions of Section 2358(A)(3)(b) and is neither beyond the scope of Section 2358(A)(3)(b) nor in conflict therewith. Section 2358(A)(3)(b) provides for a separate Oklahoma NOL independent of a federal NOL and requires the carryover and/or carryback of such losses to the years determined by reference to I.R.C. §172. Section 172(b)(3)(C) permits the forbearance of the carryback period in favor of a carryover. Without Rule 710:50-17-51(4), the implementation of Section 172(b)(3)(C) within the scheme of Section 172 and Section 2358(A)(3)(b) would be abrogated.
>
> Further, Rule 710:50-17-51(4) and its predecessors are reasonable. Out of the amount of income taxes received each month, the Tax Commission is under a duty to transfer an amount which is estimated to be necessary to make tax refunds and to make appropriations of the amount considered to be available for distribution as income taxes collected. 68 O.S. Supp. 1985, §2385.16. Without Rule 710:50-17-54(4), the ability of the Tax Commission to estimate the amount needed for refunds and the amount available for appropriation would be infringed.
>
> Finally, Rules promulgated pursuant to the provisions of the Administrative Procedures Act are presumed to be valid and binding on persons they affect, and shall have the force of law. 75 O.S. Supp. 1987, §308.2(B). Rule 23.09VII and the subsequent codifications of such rule have been promulgated in accordance with the provisions of the Administrative Procedure Act… Accordingly, notwithstanding the punitive effect Protestant's failure to file an election to forego the carryback period for its 1987 Oklahoma NOL may have, the election requirement under Rule 23.09VII should not be waived.
>
> …

In this matter, the Protestant failed to make the election to forego the carryback period for the 2004 and 2005 Tax Years by attaching a "Statement of Election" to its Oklahoma tax returns in compliance with the Statute and the Rule.

As to the Protestant's position that the 512-S instructions did not inform the Protestant specifically about the Statute and the Rule, Taxpayers are charged with knowledge of the laws that affect them.[21] Ignorance of the law, standing alone, is no defense. The rule, long-standing and well-known, "We know of no case where mere ignorance of the law, standing alone, constitutes any excuse or defense against its enforcement. It would be impossible to administer the law if ignorance of its provisions were a defense thereto."[22]

The Protestant has failed to meet its burden of proof that the Division's proposed adjustment to income tax for the 2010 Tax Year (disallowing the NOL carryforward for the 2004 and 2005 Tax Years) is incorrect, and in what respect.

DISPOSITION

It is the ORDER of the OKLAHOMA TAX COMMISSION, based upon the facts and circumstances of this case that the protest should be denied.

OKLAHOMA TAX COMMISSION

CAVEAT: This decision was NOT deemed precedential by the Commission. This means that the legal conclusions are generally applicable or are limited in time and/or effect. Non-precedential decisions are not considered binding upon the Commission. Thus, similar issues may be determined on a case-by-case basis.

NOTE: The distinction between a Commission Order designated as "Precedential" or "Non-Precedential" has been blurred because all OTC Orders resulting from cases heard by the Office of Administrative Law Judges are now published, not just "Precedential" Orders. *See* OKLA. STAT. ANN. tit.68, § 221(G) (West Supp. 2009) and OKLA. STAT. ANN. tit. 75, § 302 (West 2002). *See also* OTC Orders 2009-06-23-02 and 2009-06-23-03 (June 23, 2009), which also conclude the language of the Statute is "clear and unambiguous."

[21] OTC (Precedential) Order No. 2006-03-23-07 (March 23, 2006), citing *Ponder v. Ebey*, 1944 OK 271, 152 P.2d 268; *Anderson Nat'l Bank v. Luckett*, 321 U.S. 233 (1994).

[22] *Campbell v. Newman*, 1915 OK 538, ¶3, 151 P. 602, 603, *citing Utermehle v. Norment*, 197 U.S. 40, 25 S.Ct. 291, 49 L.Ed. 655 (1905).