

STATE OF DELAWARE
DEPARTMENT OF FINANCE

DIVISION OF REVENUE
INFORMATION CIRCULAR NO. 76-4

September 2, 1976

SUBJECT: Pre-1971 Capital Loss Carryovers
Pre-1971 Net Operating Loss Carryovers
Director's Ruling No. 71-10 dated November 16, 1971
Director's Ruling No. 72-1 dated January 31, 1972

In Jacqueline D. Fox and Richard P. Fox v. Director of Revenue, (Docket No. 573 and 574), decided by the Tax Appeal Board on March 12, 1975, the Division of Revenue had assessed a deficiency in personal income tax against the petitioners (residents of Delaware) for the taxable year 1971, based on including in Delaware taxable income certain distributions received by the taxpayers in 1971 out of pre-1971 earnings of a Subchapter S Corporation of which both taxpayers were shareholders. The assessment was based on the Division of Revenue position set forth in Tax Newsgram 71-7, issued on December 7, 1971, holding that Subchapter S Corporation distributions made out of pre-1971 earnings were to be included in Delaware taxable income in the year of receipt.

The Tax Appeal Board, holding in favor of the petitioners, concluded:

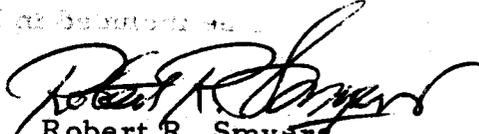
- (1) Section 1105, 30 Delaware Code, provides that taxable income for Delaware purposes is Federal adjusted gross income with the modifications specified in Section 1106, and
- (2) The Subchapter S distributions in question were properly not included in Federal adjusted gross income, and
- (3) None of the modifications specified in Section 1106 is applicable to such distributions, and
- (4) Tax Newsgram 71-7 is invalid since there is no basis in the law (Chapter 11) for requiring such adjustment.

The decision in Fox was not appealed and the Division of Revenue acquiesced in the decision by revoking Tax Newsgram No. 71-7. (Tax Newsgram No. 75-21 issued October 20, 1975).

Identical issues have been raised by taxpayers filing protest to assessments and claims for refund based on the carryover of pre-1971 capital losses and pre-1971 net operating losses. Director's Ruling 71-10 dated November 16, 1971, (relating to net operating losses) and Director's Ruling 72-1 dated January 31, 1972, (relating to capital losses) took the position that since the tax law in effect in 1970 contained no provision for allowing such carryovers, that net operating losses and unused capital losses incurred prior to the year beginning January 1, 1971, were not allowed to be carried forward to 1971 and subsequent years. The current "piggy back" law, which became effective January 1, 1971, allows such carryovers.

On the basis of the decision and reasons in the Fox case, it is concluded that Director's Ruling 71-10 and Director's Ruling 72-1, supra, should no longer be followed. Timely filed claims for refund based on the disallowance of such carryovers will be allowed to the extent such losses are unused and otherwise properly available for carryover. Deficiency assessments based solely on the disallowance of such carryovers, upon timely filed protest, will be abated.

For the Director of Revenue,


Robert R. Smyers
Deputy Director

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