



STATE OF DELAWARE
DEPARTMENT OF FINANCE
DIVISION OF REVENUE
DELAWARE STATE BUILDING
820 N. FRENCH STREET
WILMINGTON, DELAWARE 19801

DIVISION OF REVENUE
TAX RULING 78-3

March 10, 1978

- Corporation Income Tax
- Small Business Corporations (Subchapter S Corporations)

A question has been raised as to whether a small business corporation may carryback a net operating loss for purposes of the Delaware Corporation Income Tax.

Section 1902 (b) (9), Chapter 19, Title 30, Delaware Code, relating to the Corporation Income Tax, provides as follows:

"(b) The following corporations shall be exempt from taxation under this Chapter:

(9) A small business corporation having a valid election under Subchapter S of the Internal Revenue Code of 1954 in effect for any entire income year beginning on or after January 1, 1971; provided that if on the last day of such income year any of the stockholders of such corporation are non-resident individuals (as defined in Section 1104 of this Title), such corporation shall be subject to the tax imposed by this Chapter on that percentage of its taxable income equal to the percentage of its stock owned by non-resident individuals on such day."

Under the law, an electing small business corporation is exempt from the corporation income tax if all of its shareholders are Delaware residents. If one or more of its shareholders are non-residents of Delaware, it is subject to the corporation income tax on that portion of its Federal taxable income which is equal to the percentage of stock owned by such non-residents.

In the case of corporations, the starting point for computing

the Delaware tax is "Federal taxable income." Under Federal Law (Section 1372 (d) (1), I. R. C.), a Subchapter S Corporation is denied any net operating loss deduction in computing its taxable income; for Federal income tax purposes, the undistributed taxable income and net operating losses flow through to the shareholders. Under Delaware Law, resident shareholders are subject to Delaware income tax on their portion of the undistributed taxable income, and are also entitled to the benefit of any net operating loss deductions. Section 1122 (e), 30 Del. C., provides that non-resident shareholders are not subject to tax on the undistributed taxable income of the corporation, and are likewise not allowed the benefit of net operating loss deductions.

Since "Federal taxable income" is the starting point for computing Delaware taxable income, and net operating loss deductions are not allowed in computing Federal taxable income of a small business corporation, such a corporation is not entitled to adjust its taxable income for Delaware purposes by a net operating loss carryback deduction. Accordingly, it is the position of the Division of Revenue that a claim for refund of corporation income tax paid by a small business corporation which is based on the carryback of a net operating loss deduction is not allowable. There is no statutory modification or adjustment to Federal taxable income that permits such deduction to be taken into account in computing Delaware taxable income under Chapter 19, 30 Del. C.


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