The following provides a summary of the significant legislative, administrative and judicial actions that affected state and local income/franchise taxes from 1 July 2017 through 21 September 2017.

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Key developments

Illinois enacts income tax rate hikes, other corporate income tax changes

The revenue bill, SB 9, as part of the FY 2018 budget enacted 6 July 2017 by the Legislature’s override of Governor Rauner’s veto, contains corporate income tax changes. The most significant change is the permanent 33% increase of the corporate income tax rate to 7.00% (from 5.25%) and the individual income tax rate to 4.95% (from 3.75%), effective 1 July 2017. Consequently, Illinois corporations are subject to a 9.50% rate on income apportioned or allocated to Illinois when the corporate income tax rate is combined with the 2.50% personal property replacement tax determined on the same tax base.

In addition to the rate increases, the bill does the following:

- Restores the R&D credit through 2021
- Requires, for purposes of determining Illinois taxable income, the addback of amounts deducted for federal income tax purposes under the Internal Revenue Code (IRC) Section 199 production deduction, effective for taxable years ending on or after 31 December 2017
- Eliminates, for combined reporting purposes, the like-apportionment rule for all taxpayers – the like apportionment rule is in place only for tax years ending before 31 December 2017. (The like apportionment rule generally only allowed taxpayers that used the same method of apportionment to join in the filing of a combined report. Elimination of this requirement removes this barrier to filing combined reports by members of the same unitary group even if they are required to file using different methods of apportionment.)
- Extends the definition of “United States” for purposes of the composition of the unitary business group to cover any area where the United States has asserted jurisdiction or claimed exclusive rights to the exploration or exploitation of natural resources, effective for tax years ending on or after 31 December 2017

Since these new tax rates were effective in the middle of the tax year for calendar-year taxpayers (and other taxpayers whose year did not end on 30 June 2017), the vast majority of Illinois taxpayers will be subject to two different rates on income earned during calendar year 2017. Recognizing this complexity, the bill allows taxpayers to elect one of either two methods to determine which portion of their income during their tax year is subject to the old rate and which is subject to the new rate. The Illinois Department of Revenue (IL DOR) describes both methods in Information Bulletin FY 2018-02 (July 2017). Under the first method, taxpayers can elect to use a blended rate multiplying the old rate and the new rate by a fraction based on the number of days in the tax year before and after 1 July 2017. Under the second alternative method, taxpayers can specifically allocate their income earned in periods before and after 1 July 2017 to determine their 2017 tax liabilities. Taxpayers should be aware that the specific allocation method has special rules for addressing periods with losses.

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Fiscal year-end and 52-/53- week year-end taxpayers with tax years commencing after 1 July 2016 may be immediately affected by the rate increase, as they may have income earned after 1 July 2017. Guidance from the IL DOR instructs a taxpayer to choose the allocation method it intends to use on or before the extended due date of its return. Moreover, taxpayers must realize that the specific allocation election, if made, is irrevocable. Most calendar-year taxpayers will not need to select a method until filing their 2017 returns.

Taxpayers should review the composition of their unitary business groups, evaluate the impact of the elimination of the like-apportionment rule on such groups and then consider the utilization of net loss deductions, credits and other attributes in light of this significant change in the Illinois combined reporting rules. Taxpayers also should evaluate whether the key corporation of their unitary business group needs to change.

Virginia Supreme Court holds the “subject to tax” related party add back safe harbor exception applies on a post-apportionment basis

In Kohl’s Department Stores, the Virginia Supreme Court (Va. S. Ct.) in a 4-3 ruling held that a multistate retailer is required to add back royalties paid to an out-of-state related corporation (Illinois entity) because these payments did not qualify for the “subject to tax” safe harbor exception to Virginia’s related party addback statute. In so holding, the Va. S. Ct. upheld a lower court ruling and concluded the “subject to tax” exception “applies only to the extent that the royalty payments were actually taxed by another state” (i.e., it applies on a post-apportionment basis only).

Turning to the retailer’s alternative argument, the Va. S. Ct. agreed that the Virginia Department of Taxation (Va. DOT) erred in calculating the amount of royalties that fall within the “subject to tax” exception. The Va. DOT only allowed a partial exception to the extent the royalty payments were apportioned and taxed in the separate return states in which the Illinois
entity filed returns. The Va. DOT asserted that “the ‘subject to tax exception’ only applies to [t]he corresponding item of income received by the related member.” The Va. S. Ct. rejected this assertion, finding no such statutory requirement. Thus, to the extent the royalties were actually taxed by another state (including separate return states, combined return states or addback states) the “subject to tax” exception applies, regardless of which entity paid the tax. The Va. S. Ct. remanded the case for determination of the portion of the royalty payments excepted from the addback requirement.

Three Justices in a vigorous dissent asserted that the majority of the Va. S. Ct. “inserted an apportionment calculation” unsupported by the statute. The dissent found the statutory language unambiguous and would not have deferred to the Va. DOT’s interpretation. Moreover, the dissent found the majority in adopting the Va. DOT’s interpretation, inserted apportionment language reflected in proposed legislative amendments that were not enacted.

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This ruling clarifies the scope of the Virginia “subject to tax” exception under its related member addback law. The ruling, however, still leaves open the precise calculation of what is subject to tax, since the case was remanded to the circuit court for a determination of what portion of the royalty payments was actually taxed by another state and, therefore, excepted from the addback statute. In particular, it is not clear how the circuit court will deal with income apportioned to combined reporting states for purposes of the post-apportionment exception. Taxpayers that have claimed this exception should review the ruling to determine whether they still qualify for the exception, and to see if additional royalty payments may fall within the exception.

Separate return states such as Virginia have enacted their own versions of addback statutes, and while the “subject to tax” provision is common, the legislative language varies widely. The ruling in this Virginia case could be useful in interpreting the ambiguities in the statutes that may exist in other states with similar provisions, although taxpayers should use great care in construing the provisions in other states to that in Virginia.

Wisconsin Tax Appeals Commission grants tech company’s petition on receipts situsing rule

The Wisconsin Tax Appeals Commission (TAC) recently issued its decision in Microsoft Corp., in which it determined that a multistate tech company’s sales factor does not include receipts from royalties received from original equipment manufacturers (OEMs) to the extent no income-producing activity occurred in Wisconsin. In so holding, the TAC rejected the Wisconsin Department of Revenue’s (WI DOR) arguments asserting a “look-through” approach in situsing the royalties based on where end-users utilized the software that was the subject of the royalties.

The TAC first that stated this case was a matter of statutory interpretation and that both parties agreed that the receipts at issue were not from the sale of tangible personal property. The TAC then turned to the issue of whether Wis. Stat. Section 71.25(9)(d) (which provides that receipts from the use of computer software are situs to Wisconsin if the purchaser or licensee uses the software in Wisconsin) applied. Since the OEMs did not “use” the software (the TAC finding that “[t]he OEMs are not creating documents or running spreadsheets”) as contemplated by the statute, the TAC concluded the tech company sold licenses that allowed the OEMs to replicate the tech company’s software onto some, but not necessarily all, of the computers they built for potential sale to end-users or retail customers. The OEMs, and not the end-users or retail customers down the line, were the tech company’s customers. Therefore, since: (1) the royalties received by the tech company were not a function of use by actual end-users, and (2) the royalties were due without regard to whether the software was ever used by any end-users, the TAC rejected the WI DOR’s look-through approach to situs the revenues based upon the location of the end user. Instead, the TAC found that Wis. Stat. Section 71.25(9)(d) (which addresses the situsing of royalties from intangibles) applied and found that because none of the income-producing activities performed by the tech company occurred in Wisconsin, the royalties could not be sourced there.

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It is not known at this time whether the WI DOR will appeal this decision.

For taxable years beginning on or after 1 January 2009, Wisconsin changed the rules for situsing sales of intangible property, adding Wis. Stat. Section 71.25(9)(d)(j). Under this provision, receipts from royalty income are situs to Wisconsin if the purchaser or licensee uses the intangible property in the operation of a trade or business at a location in Wisconsin. If the purchaser or licensee uses the intangible property in more than one state, the royalties from the use of the intangible property are divided in proportion to the use of the intangible property in those states. The 2009 law change would not seem to change the result in this case, as the situsing rule still is applied by reference to the customer and does not seem to provide any means to apply the “look-through” approach advocated by the WI DOR.
Other noteworthy developments

Legislative

Delaware: HB 175 (enacted 2 July 2017) increases the annual maximum franchise tax rate and establishes a new maximum rate for “large corporate filers.” Effective 1 January 2017, the maximum franchise tax is increased to $200,000 (from $180,000), and a new maximum franchise tax of $250,000 is imposed on large corporate filers.

District of Columbia: Emergency law (B22-341) modifies various income tax-related provisions. In February 2017, the District of Columbia’s Chief Financial Officer certified that the revised revenue estimates for the FY 2017-21 District of Columbia Budget and Financial Plan will allow the remaining tax reform measure enacted in 2015 to be implemented — reducing the rate of incorporated and unincorporated business franchise tax to 8.25% (from 9.00%) starting in 2018. B22-341 incorporates this rate change (and prior-year rate changes) into the statute. As implemented, the rate of incorporated and unincorporated business franchise tax is 9.40% for 2015, 9.20% for 2016, 9.00% for 2017, and 8.25% for 2018 and thereafter. B22-341 was signed by the mayor on 20 July 2017 and expires 18 October 2017. A bill (B22-244) that would make these changes permanent was approved by the mayor on 31 July 2017 and will next be sent to Congress for a 30 in-session day mandatory review period.

Hawaii: SB 1002 (enacted 5 July 2017) updates the state’s conformity to the IRC to 31 December 2016, applicable to taxable years beginning after 2016.

Illinois: HB 162 (enacted 18 September 2017) restores the Economic Development for a Growing Economy (EDGE) tax credit, which can be claimed against the corporate income tax, through 30 June 2022. The bill also modifies the manner in which the maximum amount of credit allowed is determined, changes the requirements that must be met in order to qualify for the credit, prohibits EDGE credits from being credited against the taxpayer’s withholding tax liability and establishes clawback provisions.

North Carolina: SB 628 (enacted 11 August 2017) modifies franchise tax and corporate income tax provisions. In regard to the franchise tax, SB 628 reinstates the deduction (repealed in 2015) allowing taxpayers to reduce the tangible property base by the amount of any debt owed on the property (applicable to franchise tax reported on the 2019 and later year returns). Effective 11 August 2017, the base of the franchise tax is modified to be the greatest of: (1) the proportion of its net worth, (2) 55% of the corporation’s appraised value as determined for ad valorem taxation of all the real and tangible personal property in North Carolina or (3) the corporation’s total actual investment in tangible property in North Carolina. The rate of franchise tax for C corporations is $1.50 per $1,000 of the tax base, while for S corporations, it is $200 for the first $1 million of the corporation's tax base, and $1.50 per $1,000 of its tax base that exceeds $1 million. A minimum tax of $200 applies to both C and S corporations.

In addition, various definitions under North Carolina’s corporate income allocation and apportionment provisions were amended. For instance, the term “apportionable income” now includes “income that arises from either transactions and activities in the regular course of the taxpayer’s trade or business, or tangible and intangible property if the acquisition, management, employment, development, or disposition of the property is or was related to the operation of the taxpayer’s trade or business.” Additionally, the limitation imposed on “qualified interest expense” paid or accrued to a related member in a taxable year is modified so that it is limited to the taxpayer’s proportionate share of interest paid or accrued to a person who is not a related member during the same taxable year (previously, the qualified interest expense was limited to either this proportionate share or 15% of the taxpayer’s adjusted taxable income). Finally, in determining whether a nominal debt instrument creates deductible interest, the revenue secretary will not apply the covered debt instrument rules contained in the IRC Section 385 debt-equity regulations. These changes are effective for taxable years beginning on or after 1 January 2017.

Oregon: SB 28 (enacted 3 July 2017) replaces the current cost of performance method for sourcing sales of intangible property and services with a market-based sourcing method, applicable to tax years beginning on or after 1 January 2018. Under the revised law, a taxpayer’s market for sales of services is in Oregon to the extent the service is delivered in Oregon. In general, a taxpayer’s market for sales of intangible property that is rented, leased or licensed is in Oregon to the extent the intangible property is used in the state. Intangible property utilized in marketing a good or service to a consumer is deemed to be used in Oregon if the good or service is purchased by an in-state consumer. If the intangible property is sold, the following guidance is provided: (1) a contract right, government license or similar item of intangible property that authorizes the holder to conduct a business activity in a specific geographic area is deemed to be used in Oregon if the geographic area includes all or part of the state; (2) intangible property sales that are contingent on the productivity, use or disposition of intangible property are treated as the rental, lease or licensing of intangible property (as described above); (3) all other intangible property sales are excluded from the...
sales factor. Reasonable approximation will be used if the state(s) of assignment cannot be determined.

HB 2273 (enacted 2 August 2017) eliminates the functional test for purposes of determining a corporation's apportionable income. In addition, the definition of "sales" under ORS 314.610(7) is amended to mean “all gross receipts of the taxpayer that are not allocated ... and that are received from transactions and activity occurring in the regular course of the taxpayer’s trade or business.” Sales specifically exclude receipts from hedging and securities transactions; property or money received or acquired by a person acting on another’s behalf in excess of the recipient’s commission, fee or other remuneration; or amounts received from others and held in trust by the taxpayer. These changes are effective for taxable years beginning on and after 1 January 2017.

HB 2066 (enacted 2 August 2017) makes permanent the prohibition on using any tax credit to reduce, pay or otherwise satisfy the minimum tax on C corporations, specifically superseding the recent ruling in Con-way by the Oregon Supreme Court. As originally enacted, this prohibition was set to sunset in 2021.

Rhode Island: Legislation (HB 5175, Sub. A, enacted 3 August 2017) establishes a 75-day tax amnesty program that will run from 1 December 2017 through 15 February 2018. Amnesty applies to taxable periods ending before 31 December 2016. For taxpayers participating in, and complying with the terms of, the amnesty program, the Rhode Island Department of Revenue will waive penalties and 25% of interest. Taxes covered under the amnesty program include corporate income taxes.

Wisconsin: AB 64 (enacted 21 September 2017) makes various changes to the corporate income tax. Effective for taxable years beginning after 31 December 2016, Wisconsin's date of conformity to the IRC is updated to the IRC as amended to 31 December 2016 (from 2013), while decoupling from certain provisions for Wisconsin tax purposes.

The bill modifies sourcing rules under Wis. Stat. Section 71.25(9)(dh)2.b and c and creates a new section (dh)4. State law sources gross receipts from services to Wisconsin if the purchaser of the service received the benefit of the service in the state. Under the revised clause 2.b, the benefit of the service is received in Wisconsin if the service related to tangible personal property delivered directly or indirectly to Wisconsin customers (under prior law, the benefit was in the state if the service relates to tangible personal property located in Wisconsin at the time the service is received). Under revised clause 2.c, the benefit of the service is in Wisconsin if the service is purchased by an individual who is physically present in the state at the time the service was provided (under prior law, this provision applied if the service was provided to an individual). These changes first apply to taxable years beginning on 1 January 2017. New clause 4 establishes sourcing rules for broadcasters, providing that effective for taxable years beginning 31 December 2018, a broadcaster's gross receipts from advertising are in Wisconsin only if the advertiser’s commercial domicile is in the state. If the broadcaster is a member of a combined group, this provision does not apply to members that are not broadcasters.

The bill also creates Wis. Stat. Section 71.80(25), which provides that a net operating loss (NOL) or business loss carryforward is not allowed unless the incurred loss was computed on a return filed within four years of the unextended due date for filing the original return for the taxable year in which the loss was incurred. In addition, an NOL carryback is not allowed unless it is claimed within four years of the unextended due date for filing the original return for the taxable year to which the loss is carried back. Changes to the NOL rules first apply to a loss claimed on 23 September 2017, regardless of the year in which it was incurred.

Judicial

Alabama: A multinational beverage affiliated group that began filing an Alabama consolidated return in 2007 is allowed to deduct NOLs it incurred since 1999, the year in which Alabama allowed the filing of a consolidated return, because the filing of an Alabama consolidated return is not a prerequisite to the existence of an Alabama affiliated group.\(^5\)

Indiana: In E.I. DuPont de Nemours and Co., the Indiana Tax Court (IN Tax Ct.) held the Indiana Department of Revenue (IN DOR) has the authority to make adjustments to a manufacturer's NOLs, without accompanying assessment, in closed years resulting in lower NOL carryforwards, which the manufacturer may deduct in future years. The IN Tax Ct. also found that the gain from the sale of a subsidiary does not qualify as business income under the transactional test (manufacturing was the company's regular trade or business, not sales of subsidiaries) or functional test (the acquisition, management and disposition of the subsidiary were not an integral part of the company's business) and, as such, the income is appropriately treated as nonbusiness income allocated outside Indiana. Further, the IN Tax Ct. ruled that the IN DOR improperly denied the manufacturer’s interest expense deductions from intercompany loans because the transactions had a valid business purpose and economic substance.
Minnesota: The Minnesota Supreme Court, in *Ashland Inc. and Affiliates*, affirmed the decision of the Minnesota Tax Court that Minnesota state law clearly provides for conformity with the status of an eligible foreign entity electing to check the box to be disregarded as a separate entity from its parent, and that Minnesota's water's edge provisions could not render the conformity provisions superfluous. Accordingly, the income and apportionment factors of the disregarded foreign entity were properly included in the taxpayer's Minnesota unitary combined report.

North Carolina: A bank is not allowed to deduct as interest the Market Discount Income that it received on discounted bonds that matured during 2001 because such deduction is not provided for under the North Carolina corporate income tax law.

Oregon: In *Apollo Education Group, Inc. and Subs.*, the Oregon Tax Court held that an online college's receipts from online course offerings, for purposes of calculating the Oregon sales factor numerator, could be computed using only faculty cost data for the periods ending in 2009 and 2010. Under the state's cost of performance sourcing method (Ore. Rev. Stat. Section 314.665(4)), the “income-producing activity” of providing online course sections was composed of faculty, curriculum development and eCampus activities, but only faculty costs were “direct costs.”

Pennsylvania: The Pennsylvania Commonwealth Court rejected exceptions filed by the Commonwealth and taxpayer to its 15 June 2016 order in *RB Alden Corp.*, thus leaving in place its ruling that Pennsylvania's $2 million statutory cap on net loss carryforwards in place for tax year 2006 is unconstitutional in violation of the Pennsylvania Constitution's Uniformity Clause.

South Carolina: In *DIRECTV, Inc.*, the South Carolina Court of Appeals determined that 100% of the corporation's subscription receipts from South Carolina customers should be included in the numerator of its the gross receipts ratio, because all of the corporation's income-producing activities related to South Carolina customers (i.e., delivery of the signal into the homes and onto the television screens of corporation's customers) occurred entirely within South Carolina.

Texas: In *Gulf Copper*, the Texas Court of Appeals (TX Ct. App.) affirmed the trial court's ruling that a corporation primarily engaged in the business of surveying, manufacturing, upgrading and repairing offshore drilling rigs is entitled to include all of its subcontractors' payments in the revenue exclusion under Tex. Tax Code Section 171.1011(g)(3) for certain flow-through funds (the (g)(3) revenue exclusion), but held the trial court erred in ruling the corporation was entitled to include the entire amount of its subcontractor payments in its cost of goods sold (COGS) deduction. Citing Titan Transportation, the TX Ct. App. determined the corporation's contracts with its subcontractors satisfy the statutory requirement that qualifying payments be contractually mandated to someone other than the corporation. Turning to the COGS issue, the TX Ct. App. explained the plain language of Tex. Tax Code Section 171.1012 requires the Texas COGS deduction be calculated using a cost-by-cost analysis to determine whether the cost fits one of the types and categories eligible to be included in the calculation. The corporation's use of its federal income tax COGS deduction as the “starting point” for its Texas calculation failed to provide evidence that the included expenses are deductions allowed for state purposes, while the Comptroller's calculation of the COGS deduction was incorrect as a matter of law since it failed to use a cost-by-cost basis to determine the corporation's eligibility for the COGS deduction.

Virginia: A circuit court held that a multinational corporation, with a Virginia headquarters, was not entitled to use an alternative apportionment method to source its income to Virginia because it failed to prove that its proposed formula (i.e., a single sales factor apportionment formula and using a destination-based method to source its service revenues) more accurately assigned its income to the commonwealth.

Administrative

Arkansas: In Admin. Dec. No. 17-396 (issued 7 August 2017), an Administrative Law Judge for the Arkansas Department of Finance and Administration (AR ALJ) determined a company's sale of tax credits are an integral part of its business under the functional test; thus, the proceeds generated from the sales are apportionable business income. Citing *Getty Oil Exploration Co.*, the AR ALJ did not address whether the credits constituted business or nonbusiness income under the transactional test, stating such analysis was not necessary because satisfaction of either the transactional test or functional test is determinative. Further, the AR ALJ rejected the company's questioning of the validity of a separate functional test after a 2015 law change requiring a narrow construction of the statute, finding this change “did not operate to repeal or reverse” the Arkansas Supreme Court's interpretation of business income in *Getty Oil*.

Colorado: The Colorado Department of Revenue (Department) adopted amendments to Rule 1 CCR 201-2, 39-22-303(11)(c), clarifying that an affiliated group of corporations should use the post-apportionment method for combined reporting and consolidated return purposes when group members do not use...
the same apportionment methodology. Under the amended rule, members of an affiliated group filing a combined report must derive a single apportionment factor for the combined group by summing the numerator of each affiliated corporation doing business in Colorado. Intercompany transactions are eliminated before calculating income, gross sales, apportionment or de minimis determinations under this rule. When members of an affiliated group are subject to multiple apportionment methodologies and the gross sales of one commercial activity are less than 1% of the taxpayer’s total gross sales, the activity is conclusively de minimis. Taxpayers must apportion income from de minimis activity in the same ratio they apportion their gross sales, using the sales factor they use for the remainder of the commercial activity. If that amount is less than 5% of the taxpayer’s total gross sales, the commercial activity may be de minimis depending on the facts. If it is de minimis, the taxpayer will apportion that income as described. If the multiple activities give rise to gross sales that are not de minimis, then the taxpayers must use the apportionment methodology most applicable to each commercial activity and separately allocate and apportion Colorado income for all commercial activity. Colorado taxable income for each commercial activity is computed on a separate apportionment schedule and then combined. NOL carryforwards are applied, and tax and credits are computed, on a combined basis. The rule includes examples of the application of these provisions. The amended rule took effect on 14 September 2017.

**Illinois:** Amended regulation (86 Ill. Adm. Code 100.3370) was updated to reflect the 1999 and 2008 statutory changes to Illinois’ sales factor rules, most notably the enactment of a market-based sourcing provision. The final amended sales factor regulation contains technical corrections throughout and adds substantive interpretive guidance on: (1) rules governing receipts from patents, copyrights, trademarks and other similar items of intangible personal property (the underlying statute was enacted for tax years ending on or after 31 December 1999); (2) rules governing market-based sourcing (the underlying statute was enacted for tax years ending on or after 31 December 2008). In addition, the final amended sales factor regulation recognizes the Illinois Supreme Court decision in Exelon Corp.; by adding a provision clarifying that sales of electricity are not considered sales of tangible personal property for apportionment purposes until tax years ending on or after 15 July 2009. The amended regulation became final 3 August 2017.

Amended regulations (86 Ill. Adm. Code 100.3380 and .3390), related to alternative apportionment, were modified to reflect statutory changes and to reflect current Illinois Department of Revenue (IL DOR) policy. Other amendments to the alternative apportionment regulation (specifically the exclusion of gross receipts from incidental or occasional sales found in 86 Ill. Adm. Code 100.3380(c)(2)) make clear that gross receipts from the sale of stock in a subsidiary also are excluded from the sales factor. The regulation lists various reasons why exclusion of incidental or occasional gross receipts from the sales factor is appropriate with a common theme among the reasons being that such sales are not usually in the market for the taxpayer’s goods or services and inclusion would not reflect the taxpayer’s market. Adopted amendments further state that sales of intangibles and gross receipts in the regular course of business are disregarded and only the net gain (loss) is included in the sales factor. For tax years ending on or after 31 December 2008, however, only net gains are included in the sales factor for sales sourced under 35 ILCS 5/304(a)(3)(C-5)(iii) (dealing with interest on net gains and other items from the sale of intangible personal property). These rules became final on 3 August 2017.

**Indiana:** In Letter of Finding No. 02-20160336R (issued 30 August 2017), the IN DOR determined an out-of-state corporation operating in Indiana and worldwide that licensed intellectual property to foreign affiliates in various countries was entitled to reduce its Indiana sales factor because sales into foreign jurisdictions in which it had nexus should not have been sourced to Indiana under the throwback rule. In Letters of Findings Nos. 02-20150399-02-20150401 (issued 26 July 2017), the IN DOR determined for-profit higher education institutions in computing their Indiana corporate income tax must include tuition payments for online courses paid by Indiana students in the numerator of their sales factor. The income from the online courses is Indiana source income because all of the income-producing activity (i.e., sales of online courses, including giving class instructions to Indiana students) is rendered in Indiana when the Indiana students attend the online courses.

**Massachusetts:** In TIR 17-7 (issued 25 August 2017) the Massachusetts Department of Revenue revised TIR 10-16: Non-US Corporation with US Income Exempt from US Tax Pursuant to a Bilateral US Income Tax Treaty to reflect a change in its policy. The revisions focus on the calculation of the non-income measure of the corporate excise tax and the exclusion of receipts, property or payroll related to treaty-exempt income from the corporation’s Massachusetts apportionment formula. The changes in TIR 17-7 apply going forward and to open tax years.
Minnesota: In Revenue Notice #17-04 (issued 5 September 2017), the Minnesota Department of Revenue issued revised guidance on how an unrelated business income taxpayer should calculate NOL carryforwards. Minnesota law defines “unrelated business income” by cross-reference to IRC Sections 511 to 515; Section 512 allows an NOL deduction in calculating unrelated business income as provided in IRC Section 172. Thus, in calculating Minnesota unrelated business income, an exempt entity must use the federal attribute calculation and timing provision in IRC Section 172. The NOL limitations and modifications provided for under Minn. Stat. Sections 290.0133 (subd. 5) and 290.095 do not apply to unrelated business income taxpayers.

New Mexico: A multistate corporation's interest income from payment-in-kind notes it received as part of the sale and disposition of its grain elevator business is nontaxable nonbusiness income under the Uniform Division of Income for Tax Purposes Act and the requirements of both the Commerce and Due Process clauses of the US Constitution.19

New York: In Whole Foods Market Group,20 the New York Tax Appeals Tribunal (NYTAT) affirmed the New York Division of Tax Appeals (NYDTA) ruling that a corporation operating a multistate grocery store chain and a related intangible holding company should have filed tax returns on a combined basis for the audit period (2008-2010 tax years), instead of adding back the related party royalty payments. Here, the parties stipulated that the intangible holding company received more than 50% of its total receipts from the corporation for each of the years in the audit period. Thus, under the New York Department of Taxation and Finance (the NYDOTF) guidance, combined filing was required rather than merely adding back the related-party royalty payments. The NYTAT, however, reversed the NYDTA finding that the corporation was not entitled to abatement of the substantial understatement tax penalty, instead finding that the corporation's interpretation of the statute after the 2007 amendment, although erroneous, was reasonable.

In In the Matter of the Petitions of Catalyst Repository Systems, Inc.,21 the NYDTA held a corporation's receipts from online litigation support are services sourced to the location where they were performed under the law (N.Y. Tax Law former Section 210(3)(a)(2)(B)) applicable for the years at issue, 2008 through 2010. The services were performed in Colorado, where the corporation's servers, computer infrastructure and the majority of its employees were located. The NYDTA noted that the New York Division of Taxation's allocation sourcing approach of the corporation's receipts based on customers' addresses did not become effective until 2015, when the state revised its law.

In In the Matter of Stewart's Shops Corporation,22 the NYTAT upheld an NYDTA's decision that a parent company cannot deduct premiums paid to a subsidiary captive insurance company from its New York entire net income because the arrangement for which the premiums were paid did not constitute insurance for federal income tax purposes.

In NYT-G-17(2)C (issued 2 August 2017) the NYDOTF determined that direct and indirect owners of a registered broker-dealer cannot use the broker-dealer rules to assign their own service receipts to New York, as neither were registered broker-dealers eligible for the market-sourcing treatment under the pre-2014 rules. This ruling is merely the NYDOTF's interpretation of the law, and may not be used as precedent.

Virginia: In P.D. 17-156 (issued 5 September 2017), the Va. DOT announced that its tax amnesty program will run from 13 September 2017 through 14 November 2017. The amnesty program is open to individuals and businesses for tax assessments issued before 15 June 2017 that are related to an amnesty eligible period (for corporate income tax the period is taxable year 2015 and prior, and for bank franchise tax the period is taxable year 2016 and prior). In exchange for participating in, and fully complying with the terms of, the amnesty program, the Va. DOT will waive all civil and criminal penalties assessed or assessable and one-half of the interest assessed or assessable. Eligible tax liabilities that remain unpaid at the end of the amnesty program will be subject to a 20% penalty. Further, any tax liability associated with a decision in Kohl’s Department Stores Inc.23 regarding the related-party intangible expense addback provisions, and Corporate Executive Bd.24 regarding a denied request to use an alternative apportionment formula, is not eligible for amnesty.

Developments to watch

Texas: On 13 September 2017, the Texas Supreme Court heard oral arguments in Graphic Packaging. At issue in this case is whether the franchise tax (i.e., Margin Tax) is an income tax within the meaning of the Multistate Tax Compact (Compact) statute and whether the Compact's equally weighted three-factor apportionment formula election is available under the Margin Tax.25

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