

Indiana passes legislation to adopt market sourcing and enact other tax law changes

Overview

Indiana has recently passed three pieces of legislation that impact Indiana tax law. On April 29, 2019, Indiana Governor Holcomb signed House Bill 1001¹ creating a new reporting requirement for the Indiana Research and Development (“R&D”) Credit. On May 1, 2019, Governor Holcomb signed Senate Bill 563,² which includes the following modifications:

- Adopts market-based sourcing for apportionment of receipts other than tangible personal property;
- Adds definitions of “telecommunication services” and “broadcast services” and prescribes special apportionment sourcing rules for each; and
- Enhances the definition of “adjusted gross income derived from sources within Indiana.”

Lastly, on May 5, 2019, Governor Holcomb signed Senate Bill 565,³ which includes the following modifications:

- Updates the state’s IRC conformity date to January 1, 2019;
- Clarifies the necessary state “addback” or “deductions” related to IRC sections 163 and 965; and
- Specifies how a taxpayer may petition to discontinue filing a combined income tax return.

This Tax Alert summarizes certain provisions of these law changes, which are effective retroactively to January 1, 2019.

Sales, other than sales of tangible personal property

S.B. 563 provides that receipts, other than receipts from the sale of tangible personal property, are sourced to Indiana if the market for the sales is in Indiana. Therefore, Indiana has switched from its historical cost of performance sourcing methodology to market-based sourcing for services, retroactive to January 1, 2019. Special industry rules have also been added for receipts from telecommunication services and broadcast services, and these rules are discussed in the section below.

S.B. 563 defines market for sales in Indiana as follows:

- Receipts involving real property, if the property is located in Indiana
- Receipts involving rental, lease or license of tangible personal property, if the property is located in Indiana
- Receipts from services are in Indiana if the benefit of the service is received in Indiana
- Receipts from intangible property that is rented, leased or licensed if and to the extent the intangible property is used in Indiana, provided that intangible property used in marketing a good or service to a consumer is used in Indiana if that good or service is purchased by a consumer in Indiana.⁴

¹ A copy of H.B. 1001 is accessible [here](#).

² A copy of S.B. 563 is accessible [here](#).

³ A copy of S.B. 565 is accessible [here](#).

⁴ S.B. 563, Section 7, adding I.C. 6-3-2-2 (f)(3).

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The bill adds that if the state(s) of attribution cannot be determined under the new rules, then receipts shall be sourced based on the state(s) in which the delivery occurs.⁵ Further, receipts that cannot be attributed based on the new rules are excluded from the denominator of the receipt factor.⁶

The bill allows for emergency administrative rulemaking to help implement the new market-based sourcing provisions, which “must be consistent with the Multistate Tax Commission model regulations for income tax apportionment including any specialized industry provisions as in effect on January 1, 2019.”⁷

The bill also states that receipts from the maturity, redemption, sale, exchange, loan, or other disposition of stocks, bonds, notes, options, forward contracts, futures contracts, and similar instruments generally are sourced to Indiana if the taxpayer’s commercial domicile is in Indiana.⁸

Telecommunication services and broadcast services definitions and sourcing of receipts

I.C. 6-3-1-37 is added to the Indiana tax code by S.B. 563 and defines “telecommunication services” as electronic transmission, conveyance, or routing of voice, data, audio, video, or any other information or signals to a point, or between or among points.⁹ Also included in the definition is data processing and information services that allow data to be generated, acquired, stored, processed or retrieved and delivered through electronic transmission, advertising associated with telecommunication services, internet access service, radio and television audio and video programming services, ancillary services associated with telecommunications services, music and video except to the extent the item consists of specified digital products.¹⁰

Similarly, I.C. 6-3-1-38 is added to the Indiana tax code and defines “broadcast services” as the transmissions, conveyance and routing of video broadcasts without regards to the medium. This definition applies to television broadcast networks, a cable program network or a television distribution company. It also includes any advertising or promotions activity provided in conjunction with broadcast services.¹¹

Pursuant to these provisions, the sourcing of receipts for telecommunication services and broadcast services shall be based on costs of performance. If the costs are incurred in multiple states, then receipts are sourced to Indiana if the greater portion of the costs are incurred in Indiana.¹²

Enhanced definition of income derived from Indiana sources

The meaning of “adjusted gross income derived from sources within Indiana” is expanded to include the following language: “Income derived from Indiana shall be taxable to the fullest extent permitted by the Constitution of the United States and federal law, regardless of whether the taxpayer has a physical presence in Indiana.”¹³

State modifications under IRC sections 163 and 965

In response to the Tax Cuts and Jobs Act of 2017 (P.L. 115-97) and Bipartisan Budget Act of 2018, S.B. 565 clarifies the necessary state “addback” or “deductions” related to IRC sections 163, and 965. With respect to related party interest, which may need to be added back for Indiana purposes as “intangible expenses,” any directly related interest expense that constitutes business interest within the meaning of IRC section 163(j) shall be considered to have reduced the taxpayer’s federal taxable income in the first taxable year in which the deduction otherwise would have been allowable under IRC Section 163 if the limitation under IRC section 163(j)(1) did not exist.¹⁴

S.B. 565 also clarifies that any amount deducted under IRC section 965(c) must be added back for Indiana purposes.¹⁵ If a foreign corporation had an earnings and profit (E&P) deficit, as defined in IRC section 965(b)(3)(B), and the E&P deficit, or a portion of the deficit, of the foreign corporation is permitted to reduce the federal adjusted gross income or federal taxable income of the taxpayer, the

⁵ S.B. 563, Section 7, adding I.C. 6-3-2-2 (f)(4).

⁶ S.B. 563, Section 7, adding I.C. 6-3-2-2 (f)(5).

⁷ S.B. 563, Section 7, adding I.C. 6-3-2-2 (u).

⁸ S.B. 563, Section 8, adding I.C. 6-3-2-2.2 (h).

⁹ S.B. 563, Section 5, adding I.C. 6-3-1-37.

¹⁰ S.B. 563, Section 5, adding I.C. 6-3-1-37 and I.C. 6-2.5-1-27.5.

¹¹ S.B. 563, Section 5, adding I.C. 6-3-1-38.

¹² S.B. 563, Section 7, amending I.C. 6-3-2-2 (f)(2).

¹³ S.B. 563, Section 7, amending I.C. 6-3-2-2 (a).

¹⁴ S.B. 565, Section 7, amending I.C. 6-3-1-3.5 (b)(8).

¹⁵ S.B. 565, Section 7, amending I.C. 6-3-1-3.5 (b)(13), (d)(12), (e)(12), (f)(9).

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deficit, or the portion of the deficit, shall also reduce the income taxable in Indiana. However, in no case can the amount taxable under IRC section 965 be reduced to less than zero.¹⁶

Procedure to request to discontinue combined filing

S.B. 565 adds a requirement that a petition be filed with the Department within 30 days after the taxpayer's year end to seek permission to discontinue filing a combined income tax return.¹⁷

Research and development credit

A new section was added to the Indiana tax code that provides a reporting requirement when claiming the Indiana R&D Credit. Taxpayers are required to report if an Indiana R&D credit was both determined and claimed under either IRC section 41(a)(1) or 41(c)(4). If an Indiana R&D credit was claimed under either of these sections, and a federal credit was not claimed for these same expenses, then an additional disclosure must be made as to why the Taxpayer is not claiming a federal credit.¹⁸

Considerations

The 2019 Indiana legislative session brought about a change in sourcing for receipts from other than tangible personal property, defined and implemented special sourcing rules for specific services, including telecommunications and broadcast services and certain receipts are sourced to Indiana if the taxpayer's commercial domicile is in Indiana. Additionally, the changes in law gave clarification around existing state modifications related to the Tax Cuts and Jobs Act of 2017 and added filing requirements for taxpayers claiming the Indiana R&D credit. Taxpayers potentially impacted by the enactment of these laws should consult with their Indiana tax advisors for further assistance.

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¹⁶ S.B. 565, Section 7, adding I.C. 6-3-1-3.5 (h).

¹⁷ S.B. 565, Section 10, adding I.C. 6-3-2-2 (r).

¹⁸ H.B. 1001, Section 121, adding I.C. 6-3.1-4-8.