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State Tax Matters

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In this issue:

Income/Franchise: Colorado: DOR Warns Taxpayers about Application of Combined Return Regulation to FSCs Only

Notice re: Revenue Regulation 39-22-303(12)(c), Colo. Dept. of Rev. (1/16). The Colorado Department of Revenue (Department) has issued an announcement warning taxpayers that they should not rely on Revenue Regulation 39-22-303(12)(c) until further notice. In doing so, the Department explains that it had adopted this regulation in 1994 to address the treatment of Foreign Sales Corporations (FSCs) under section 303-22-303(12)(c), C.R.S., which provides that only C corporations that have more than 20% of their property and payroll located inside the United States may be included in a corporate taxpayer's combined return. The Department additionally notes that FSCs may receive a reduction in US federal income tax related to certain foreign exports, but do not necessarily have property or payroll for Colorado combined reporting purposes. Regulation 39-22-303(12)(c) provides that corporations that have no property or payroll cannot have 20% or more of property or payroll located in the United States and therefore cannot be included in a combined report. According to the Department, while this

rule was intended to address FSCs in particular, some taxpayers have interpreted Regulation 39-22-303(12)(c) to apply to domestic holding companies with no foreign operations and have argued that they can exclude any domestic C corporation from their combined returns if it has no property or payroll – even if it does not do business in a foreign country. The Department states that it "disagrees with this interpretation" and this issue is currently being addressed in the Colorado courts. As such, the Department explains that it will wait for a final ruling from the courts on the application of section 39-22-303(12)(c), C.R.S., and Regulation 39-22-303(12)(c) before considering any further action on the rule – "pending that determination, taxpayers should not rely on this regulation except as it applies to an FSC."
URL: https://www.colorado.gov/pacific/tax/revenue-regulation-39-22-30312c-notice

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Income/Franchise:
Illinois: DOR Issues Amended Rule on Sales Factor Treatment of Gains/Losses from Hedging Transactions

Amended 86 Ill. Adm. Code Sec. 100.3380, Ill. Dept. of Rev. (eff. 1/5/16). The Illinois Department of Revenue (Department) has issued an amended rule prescribing the sales factor treatment of gains and losses from hedging transactions – i.e., transactions specifically identified by the taxpayer for federal income tax purposes as entered into by the taxpayer for purposes of hedging against the effect on profits or costs of business transactions that result from fluctuations in interest rates, prices or currency exchange rates. The rule requires taxpayers to treat these gains and losses as adjustments to the dollar amounts of the hedged transactions, rather than as separate transactions, in computing the sales factor.
URL: ftp://www.ilga.gov/JCAR/AdminCode/086/086001000M33800R.html

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Income/Franchise:
New York: Draft Proposed Article 9-A Business Corporation Franchise Tax Combined Report Regulations Issued

Draft Proposed Amended New York State Business Corporation Franchise Tax Regulations Subpart 6-2, Sections 6-2.1 through 6-2.7, N.Y. Dept. of Tax. & Fin. (1/22/16). The New York State Department of Taxation and Finance (Department) has released draft amendments to the New York State Business Corporation Franchise Tax Regulations Subpart 6-2, Combined Reports. In its 2014-2015 Budget Act, New York adopted full water's-edge unitary combined reporting with an ownership test of greater than 50%, and provided for an election to permit

combined filing for certain commonly owned groups (that were not otherwise unitary) with a seven-year lock-in. These draft regulations clarify New York's capital stock and unitary business requirements for combined reporting with specific sections addressing, among other things, indirect ownership and control, presumptions of unity (including instant unity), and holding companies, as well as provide additional detail on the commonly owned group election.
URL: https://www.tax.ny.gov/bus/ct/pending/Subpart%206-2%20v4.pdf

Draft Regulation Section 6-2.3(a) states that the term "unitary business" will be "construed to the broadest extent permitted under the US Constitution as interpreted by the US Supreme Court, the [New York State] courts and the New York State Tax Appeals Tribunal." Draft Regulation Section 6-2.3(b) adopts the 3-part test of unitary business outlined by the US Supreme Court in cases addressing the constitutional scope of the unitary business. Those attributes include functional integration, centralized management and economies of scale. The draft regulations also provide numerous examples illustrating how the voting power attributed to the direct and indirect ownership and control of capital stock determines whether the capital stock requirement is met. The examples shed light on the Department's unique understanding of control of a lower tier corporation through indirect voting power for purposes of possibly including such lower tier entity in a combined report. Moreover, the draft regulations provide presumptions that a unitary business exists in certain factual scenarios, where in each case the capital stock requirement is met. For example, the presumption of unity exists where corporations:

1. Are horizontally integrated (*i.e.*, are in the same general line of business);
2. Are vertically integrated (*i.e.*, are engaged in different steps in the same general production path);
3. Have "strong centralized management"; or
4. Are newly formed or, in certain circumstances, acquired by, a forming or acquiring corporation.

Either the Department or a taxpayer may overcome the presumption by "the presentation of clear and convincing evidence." In addition, passive holding companies are deemed to be engaged in a unitary business with any operating company or companies provided that the holding company and the operating company (or companies) satisfy the capital stock requirement.

Note that these draft regulatory amendments have been posted for public comment *prior to* the State Administrative Procedure process to formally propose and adopt these regulations. Accordingly, these draft proposed regulatory amendments "are not final and should not be relied upon." The Department is asking for public comments on these draft regulatory amendments to be provided by April 21, 2016. Please contact us with any questions.

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Income/Franchise:
Rhode Island: Division of Taxation Issues Revised Proposed Regulation on Mandatory Combined Reporting

Proposed Revised Regulation CT 15-15, R.I. Div. of Tax. (1/20/16). The Rhode Island Division of Taxation (Division) has issued a revised proposed regulation related to the implementation of mandatory combined reporting in Rhode Island, which has taken effect for tax years beginning on or after January 1, 2015. The Division has, once again, invited all interested parties to submit written or oral comments concerning the proposed combined reporting regulation by February 22, 2016; a public hearing on this proposed regulation will be held on February 22, 2016.
URL:
http://sos.ri.gov/documents/archives/regdocs/holding/DOTAX/Business_Corporation_Tax_Combined_Reporting_CT_15-15.pdf

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Sales/Use:
Alabama: Guidance on New "Economic Presence" Rule for Certain Out-of-State Sellers Making Threshold "Significant Sales" into Alabama

What's New: Guidance for persons, firms and corporations making retail sales of tangible personal property into the State of Alabama....applying to all transactions occurring on or after January 1, 2016, Ala. Dept. of Rev. (1/16). Referencing its previously issued Notice, the Alabama Department of Revenue (Department) reminds out-of-state sellers with "a substantial economic presence in Alabama" to collect and remit Alabama tax on their sales into the State for all transactions occurring on or after January 1, 2016 – regardless of whether they have an Alabama physical presence – pursuant to the Department's Amended New Rule 810-6-2-.90.03, which establishes dollar threshold conditions under which certain out-of-state sellers must collect and remit Alabama sellers use tax. More specifically, the Department explains that this administrative rule imposes a collection obligation on out-of-state sellers who engage in one or more activities subjecting out-of-state sellers to Alabama's seller use tax levy, and who

had $250,000 or more in retail sales sold into Alabama in the previous year. The Department additionally explains that such out-of-state sellers may satisfy the rule's requirements by collecting, reporting and remitting tax on sales made into Alabama pursuant to the provisions of Article 2, Chapter 23 of Title 40, Code of Alabama 1975, or by participating in Alabama's "Simplified Seller Use Tax Remittance Program."
URL: http://revenue.alabama.gov/
URL: http://revenue.alabama.gov/salestax/Notice-to-Sellers-with-Substantial-Economic-Presence.pdf
URL: http://revenue.alabama.gov/rules-fa/810-6-2-.90.03.pdf

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Sales/Use:
Washington: DOR Issues Emergency Amendments to B&O Tax Rule on Financial Institution Apportionment to Conform with MTC Changes

Emergency Amended WAC 458-20-19404, Wash. Dept. of Rev. (eff. 1/1/16). The Washington Department of Revenue ("Department") has issued emergency amendments to its administrative rule addressing how financial institutions must apportion gross income for state business and occupation (B&O) tax purposes when they engage in business both within and outside of Washington. These emergency amendments are issued pursuant to state law authorizing the Department to adopt financial institution apportionment rules that are consistent with the model adopted by the Multistate Tax Commission (MTC). Accordingly, the Department explains, its administrative rule has been amended on an emergency basis to remain consistent with the MTC's change in its model method of apportionment for financial institutions, which became effective for tax years starting on or after January 1, 2016.
URL: http://lawfilesext.leg.wa.gov/law/wsr/2016/02/16-02-010.htm

The Department has since correspondingly proposed to amend its rules on a non-emergency basis [*see proposed amended WAC 458-20-19404, and proposed new 458-20-19404A*] to remain consistent with the MTC's apportionment changes for the period of June 1, 2010, through December 31, 2015, and the period beginning January 1, 2016.
URL: http://lawfilesext.leg.wa.gov/law/wsr/2016/02/16-02-111.htm

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Multistate Tax Alerts

What's new in the States? Our Multistate Tax Alerts highlight selected state tax developments relevant to taxpayers, tax professionals, and other interested persons. Read our more recent alerts below or visit the archive for ones you may have missed.
Archive: http://www2.deloitte.com/us/en/pages/tax/articles/multistate-tax-alert-archive0.html?id=us:2em:3na:stm:awa:tax

No new alerts were issued this period. Be sure to refer to the archives to ensure that you are up to date on the most recent releases.

Have a question?
If you have needs specifically related to this newsletter's content, send us an email at clientsandmarketsdeloittetax@deloitte.com to have a Deloitte Tax professional contact you.