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State Tax Matters
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January 6, 2017

In this issue:

Amnesty:
Coming in April, Pennsylvania's Amnesty Program Offering Potential 100% Penalty Waiver and 50% Interest Waiver; 5% Non-Participation Penalty May Apply

Fact Sheet: Pennsylvania 2017 Tax Amnesty Program, Penn. Dept. of Rev. (12/16). Pursuant to legislation enacted in 2016 [*H.B. 1198* (Act 84)] requiring the Pennsylvania Department of Revenue (Department) to establish a 60-day amnesty program ending no later than June 30, 2017, the Department has issued a fact sheet reminding that such tax amnesty program will run from April 21, 2017 through June 19, 2017. The 2017 tax amnesty program will generally apply to all taxes administered by the Department that are delinquent as of December 31, 2015, whether known or unknown to the Department. Under this program, amnesty will be granted for eligible taxes to qualifying taxpayers, and potentially will permit 100% waiver of the underlying penalties and 50% waiver of the underlying interest. Individuals, businesses and other entities that participated in Pennsylvania's 2010 tax amnesty program are ineligible to participate in this upcoming 2017 tax amnesty program. The Department also reminds that this 2017 tax amnesty program includes a non-participation penalty of 5% of the unpaid eligible tax liability and penalties and interest.
URL: http://www.revenue.pa.gov/taxamnesty/Documents/tax_amnesty_fact%20sheet.pdf
URL: http://www.legis.state.pa.us/cfdocs/billinfo/billinfo.cfm?syear=2015&sind=0&body=H&type=B&bn=1198

Note that a recently posted Department webinar also provides an overview of this upcoming 2017 tax amnesty program. Please contact us with any questions.
URL: https://www.youtube.com/watch?v=fhs51KsTabc

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Credits / Incentives:
California Competes Tax Credit Application Period Now Open through January 23

Notice: California Competes Tax Credit Application Periods for Fiscal Year 2016-2017, California Governor's Office of Business and Economic Development (6/29/16). The California Governor's Office of Business and Economic Development (GO-Biz) previously announced that, for fiscal year 2016/2017, the second application for the California Competes Tax Credit (CCTC) will be accepted online beginning January 2, 2017, and is scheduled to close January 23, 2017. Accordingly, a taxpayer that is contemplating creating net new fulltime jobs in California, retaining jobs in California, or relocating to California may now wish to consider submitting an application during the second application round (in the State's 2016/2017 fiscal year) to obtain the CCTC.
URL: http://businessportal.ca.gov/Portals/1/Files/Notice%20California%20Competes%20Tax%20Credit%20Fiscal%20Year%202016-17.pdf

The CCTC is an income tax credit enacted on July 11, 2013, and was first available to taxpayers in 2014 for fiscal year 2013/2014. In fiscal year 2015/2016, GO-Biz allocated approximately $160 million to 259 companies that are projected to create over 20,000 jobs and make almost $3.2 billion in investments. For fiscal year 2016/2017, GO-Biz has authorized $243.3 million in available CCTC to be allocated over three application periods.

According to GO-Biz's previously issued notice, for fiscal year 2016/2017, there was only one application period during 2016; the remaining two application periods will run in 2017. The second application period for fiscal year 2016/2017 opened online on January 2, 2017 and will run through January 23, 2017. During this application period, there will be $100 million in negotiated funds available. The third and final application round in fiscal year 2016/2017 is scheduled to open on March 6, 2017 and run through March 27, 2017, and $68.3 million in negotiated funds will be available during this period.

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Income/Franchise:
California Court of Appeal Upholds Cable Company's Win on Unitary Issue

ComCon Production Services I, Inc. v. California Franchise Tax Board, Cal. Ct. App. (12/14/16). A California Court of Appeal (Court) has affirmed a 2014 trial court ruling that a cable service company did *not* operate as a unitary business with its commonly owned cable television home shopping channel in 1998 and 1999, and thus the latter did *not* have to be included in the cable service company's California combined report. In dispute were the nature, extent, and significance of the intercompany transactions occurring between the two companies, as well as whether and/or to what degree the cable service company exercised control over or influenced the cable television home shopping channel. The Court agreed with the cable service company's claims on the unitary issue that the two companies were not vertically integrated, lacked a centralized management, generated no economies of scale, and produced no other flow of values that justified the California Franchise Tax Board's unitary business treatment. Moreover, the Court found that the two companies were not dependent upon or contributed to the other within the meaning of the legal standards for determining a unitary business. The Court additionally upheld that a $1.5 billion payment received by the cable service company from a third-party cable television system operator as a "termination fee" in connection with an agreement/merger plan between the two parties in 1999 constituted apportionable business income for state corporation franchise tax purposes.
URL: http://www.courts.ca.gov/opinions/nonpub/B259619.PDF

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Income/Franchise:
Taxpayer Asks US Supreme Court to Review Decision Affirming that Subsidiary Qualifying as "Financial Institution" Must Attribute its Securitized Student Loan Portfolio Entirely to Massachusetts for Property Factor Purposes

First Marblehead Corp. v. Comm'r of Revenue, US (petition for certiorari filed December 15, 2016). The taxpayer has asked the US Supreme Court to review the Massachusetts Supreme Judicial Court's 2016 decision which affirmed – on remand from the US Supreme Court "for further consideration in light of" the US Supreme Court's 2015 decision in *Comptroller of the Treasury of Maryland v. Wynne* [see previously issued Multistate Tax Alert for more details on the *Wynne* case] – that a subsidiary qualifying as a "financial institution" subject to the state financial institution excise tax (FIET), rather than a "foreign corporation" that must be included on its parent company's combined Massachusetts corporate excise tax return, was required to determine the situs of its property factor using only its own activities and was *not* permitted to include the activities of third parties that performed activities on the subsidiary's behalf. As a result, the subsidiary was required to attribute its securitized student loan portfolio entirely to Massachusetts for

purposes of computing its FIET property factor. In doing so, the Massachusetts Supreme Judicial Court held that the FIET taxation scheme, as applied to the subsidiary at issue, did *not* violate the internal consistency test discussed and affirmed in *Wynne*, and that the FIET taxation scheme as applied to the subsidiary satisfied the internal consistency test and therefore did not contravene the dormant Commerce Clause.
URL: https://www.supremecourt.gov/search.aspx?filename=/docketfiles/16-777.htm
URL: https://www2.deloitte.com/us/en/pages/tax/articles/multistate-tax-alert-supreme-court-rules-maryland-individual-income-tax-scheme-unconstitutional.html?id=us:2em:3na:stm:awa:tax:010617

In its filed petition, the taxpayer now asks the US Supreme Court whether:

1. An apportionment factor reflects a reasonable sense of how income is generated when it disregards the activities and entities that actually generate the income and instead arbitrarily assigns the income to the commercial domicile of an owner of the income-producing entities; and
2. The Massachusetts Supreme Judicial Court properly followed US Supreme Court precedent when it based its conclusion that an apportionment formula was internally consistent on an assumption that other states would apply an apportionment formula different from the formula in the statute it upheld.

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Income/Franchise:
Massachusetts DOR Issues Working Draft Release on Corporation Excise Tax Treatment of Offshore Investment Companies

Working Draft TIR 16-XX: Massachusetts Corporation Excise Treatment of Offshore Investment Companies, Mass. Dept. of Rev. (12/20/16). The Massachusetts Department of Revenue has issued a working draft technical information release that explains application of the Massachusetts corporation excise tax to offshore investment companies described in IRC Sec. 864(b)(2)(A)(ii) that conduct certain activities in Massachusetts – including “safe harbor” rules under which certain offshore investment companies will *not* be subject to the Massachusetts corporation excise tax. The working draft release also describes potential security corporation treatment for offshore investment companies that are subject to the corporation excise tax.
URL: http://www.mass.gov/dor/businesses/help-and-resources/legal-library/tirs/tirs-by-years/2016-releases/working-draft-tir-16-xx-offshore-investment.html

The draft release explains that if an offshore investment company conducts activities in Massachusetts, it may be considered to be doing business in Massachusetts and therefore subject to the Massachusetts corporation excise tax. Additionally, an offshore investment company that pursuant to IRC Sec. 864(b)(2)(A)(ii) is not engaged in the conduct of a US trade or business would not have effectively connected income (ECI) that would be subject to federal income tax. Therefore, if such an offshore investment company also had no non-ECI from US sources, it would have no federal gross income and thus would not be subject to the net income measure of the state corporation excise tax. However, the draft release explains that such an offshore investment company, if it is doing business in Massachusetts, would be subject to state tax on its net worth or tangible property or be subject to the minimum state excise tax.

The draft release also explains that if an offshore investment company described in IRC Sec. 864(b)(2)(A)(ii) is doing business in Massachusetts and subject to the Massachusetts corporation excise tax, it may apply for “security corporation” classification if it is engaged exclusively in buying, selling, dealing in, or holding securities on its own behalf and not as a broker. A security corporation generally is subject to the higher of an excise on its gross income (based on federal gross income subject to certain modifications), or a minimum excise of $456. If such an offshore investment company, in addition to having no ECI (pursuant to I.R.C. § 864(b)(2)(A)(ii)), also has no US-source non-ECI, it would have no federal gross income. Thus, it would be subject only to the minimum excise imposed under G.L. c. 63, § 38B.

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Income / Franchise:
New Hampshire: Proposed Rule Revisions Reflect New Law Addressing "Phantom Tax" Issue for Business Profits Tax Purposes

Proposed Amended Rev 303.05, N.H. Dept. of Rev. Admin. (12/2/16). The New Hampshire Department of Revenue Administration has released proposed rule changes reflecting legislation enacted in 2016 [S.B. 342] that no longer requires the inclusion in the New Hampshire business profits tax (BPT) of the net increase in the basis of the assets for one or more of the parties to a transaction due to certain sales or exchanges of an interest or beneficial interest in a business organization, with the apparent intent of addressing the so-called "phantom tax" issue. This new rule is applicable for sales or exchanges of interests in business organizations that occur on and after January 1, 2016. The proposed rule reflects new law that no longer requires the addition to BPT of the step up in basis of assets, but then also requires the modification of the New Hampshire basis in such assets for purposes of computing the depreciation/amortization expense claimed for BPT purposes. The proposed rule also sets forth the method by which taxpayers may formally and irrevocably elect to report the addition to BPT as was required under prior law, and consequently claim the additional depreciation/amortization deductions claimed for federal tax purposes.
URL: http://revenue.nh.gov/laws/documents/iprev300bpt.pdf

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Sales / Use / Indirect:
Indiana: Updated Bulletin Addresses Cloud Computing and Other Issues Related to Remotely Accessed Software

Information Bulletin No. 8, Ind. Dept. of Rev. (12/16). A recently updated Indiana Department of Revenue bulletin addresses sales and use taxation issues related to Software as a Service (SaaS), cloud computing, and various other matters involving remotely accessed software – including underlying definitions and illustrative working examples. The guidance generally explains that the taxability of software that can be electronically accessed via the Internet, either by remote access from a hosted computer or server or through a pool of shared resources from multiple computers and servers (i.e., cloud computing), without having to download the software to the user's computer, is not specifically addressed in the Indiana Code. In this respect, "whether a transaction involving the use of 'cloud-based' software is subject to Indiana sales or use tax depends on the facts and circumstances of each transaction, particularly with regards to the amount of control or possession the purchaser is granted in the software, the object of the transaction, and the ownership rights, if any, the purchaser has in the software." To this end, the bulletin explains, SaaS may or may not be subject to tax depending on the factors of the transaction and arrangement. For example, charges for accessing prewritten computer software maintained on the vendor's or a third party's computer or servers are not subject to tax when accessed electronically via the Internet if the customer is not transferred the software, does not have an ownership interest in the software, and does not control or possess the software or the server. Other addressed items involve digital goods, remote storage, web hosting and design, and web training.
URL: http://www.in.gov/dor/reference/files/sib08.pdf

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

Amended WAC 458-20-19404, Wash. Dept. of Rev. (eff. 12/19/16). The Washington Department of Revenue (Department) has issued another emergency amended 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://dor.wa.gov/Docs/Rules/draft/20-19404cr3efrmdraft4thDec2016.pdf

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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.

US Supreme Court Denies Petition for Certiorari in *DMA v. Brohl*

On December 12, 2016, the United States Supreme Court denied a petition for writ of certiorari in the case *Direct Marketing Association v. Brohl*.

This Multistate Tax Alert summarizes the latest holding in the case (a February 2016 decision of the US Court of Appeals for the Tenth Circuit) and also provides considerations for taxpayers in the wake of the US Supreme Court's denial of review.
[Issued: December 15, 2016]
URL: https://www2.deloitte.com/us/en/pages/tax/articles/us-supreme-court-denies-petition-for-certiorari-in-dma-v-brohl.html?id=us:2em:3na:stm:awa:tax:010617

Practical State Tax Considerations Arising from Final/Temporary Intercompany Debt Regulations

On October 21, 2016, the US Treasury and the IRS published final and temporary regulations under section 385 of the Internal Revenue Code (the 385 Regulations) that generally would allow for certain debt instruments to be recast as equity. Extensive comments were submitted to these Proposed Regulations that had been issued in April, 2016, and the 385 Regulations addressed several of the issues raised by those comments. In many respects these changes are expected to facilitate taxpayer compliance with the 385 Regulations. However, the Proposed Regulations raised various issues for state corporate income and franchise taxes, and the updated provisions of the 385 Regulations continue to raise some of the same issues.

This Multistate Tax Alert discusses several of the practical state tax considerations for taxpayers that arise from the 385 Regulations.
[Issued: December 20, 2016]
URL: https://www2.deloitte.com/us/en/pages/tax/articles/practical-state-tax-considerations-arising-from-final-temporary-intercompany-debt-regulations.html?id=us:2em:3na:stm:awa:tax:010617