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Iowa

Sales and Use Tax Manufacturing Exemptions Modified

Iowa Governor Terry Branstad has signed legislation modifying the sales tax exemptions related to the purchase of items used in manufacturing and other activities. The exemption for the sale or rental of certain computers, machinery and equipment, including materials used to construct them, now also includes replacement parts and supplies. The items must be directly and primarily used for any of the following: processing by a manufacturer, to maintain the integrity of the product or unique environmental conditions, in research and development of new products or processes, or recycling. Items may also be pollution-control equipment, or computers used in processing or storage of data or information by an insurance company, financial institution, or commercial enterprise.

H.F. 2433, Laws 2016, effective March 21, 2016

Michigan

Statute of Limitations Approaching for Certain MBT Overpayment Refund Claims

The Michigan Department of Treasury has issued a notice directed at taxpayers who have overpayments credited forward from the Michigan Business Tax (MBT). After the Corporate Income Tax (CIT) took effect in Michigan on January 1, 2012, certain businesses with certificated credits could elect to continue to file returns and pay the Michigan Business Tax instead of the CIT until the credits were exhausted. Also, some taxpayers upon filing the final MBT return for the 2011 tax year requested that all or part of a 2011 overpayment be credited forward, rather than requesting a refund. Many of these credit forwards remain unused. The Treasury is urging taxpayers to consult a tax professional to determine if they are subject to the CIT or are eligible to make an MBT election to claim the credit forward.

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Further, a taxpayer who is not subject to the MBT or the CIT after December 31, 2011, and who has payments remaining on an MBT account, may make a refund claim via letter to the Treasury's Customer Contact Section, MBT Unit. For most taxpayers, the statute of limitations to file a refund claim letter for a 2011 MBT filing obligation expires on April 30, 2016.

However, the statute of limitations expires on December 31, 2016 for taxpayers with an approved extension on their 2011 return.

Notice to Taxpayers Regarding Overpayments Remaining on Michigan Business Tax Accounts, Michigan Department of Treasury, April 8, 2016

Federal Constructive Ownership Rules Could Not Be Used to Make Unitary Business Determination

The Michigan Court of Appeals reversed and remanded a Court of Claim's decision, which found that the taxpayer was a member of a unitary business group under the Michigan Business Tax (MBT). The lower court had determined that the taxpayer was part of a unity business group under Sec. 208.1117(6), M.C.L., which required one member of the group to directly or indirectly own or control more than 50% of the ownership interest of the other members. As there was not more than 50% direct ownership or control, the lower court made the determination based upon the taxpayer's indirect ownership or control after looking at the federal "constructive" ownership rules. The Court of Appeals held that indirect ownership in Sec. 208.1117(6), M.C.L. meant ownership through an intermediary. In the taxpayer's case, no unitary business group existed because none of the entities involved owned, through an intermediary or otherwise, more than 50% of any other entity.

The taxpayer was a Michigan corporation owned by two brothers. Neither brother owned more than 50% of the taxpayer's common stock. Another Michigan corporation, Pixie, originally was the parent of the taxpayer. But Pixie sold off of its interest to the two brothers in 2008. Neither brother owned more than 50% of Pixie's common stock. A third entity, LaBelle, was a Michigan limited partnership. In forming the partnership, each of the brothers contributed $50 - $1 for a 1% general partnership and $49 for a 49% limited partnership. The partnership was later amended to add the brothers' children as limited partners.

The MBT did not define indirect ownership or control, but did provide that terms not defined should have the same meaning as when used in comparable context in the federal income tax laws. However, there was no federal income tax provision directly comparable to this MBT section. The lower court looked to international taxation and the federal "controlled foreign corporation" definition and rules of IRC Sec. 957 and 958. The Court of Appeals found that the lower court erred using the federal income tax definition of "constructive" ownership when defining Michigan's indirect ownership requirement. In the absence of a comparable context, the lower court should have resorted to normal rules of statutory construction to determine the meaning of the undefined term. IRC Sec. 958 applied to situations where stock was owned "directly or indirectly", indicating that while those rules of actual and constructive ownership applied to indirectly owned stock, the rules did not define the term. Further, the Court of Appeals noted that the federal statutes and regulations are careful to never to say that indirect ownership means constructive ownership and at times expressly distinguish between the two. To apply the constructive ownership rules to Sec. 208.1117(6), M.C.L. would have expanded that statute beyond the meaning intended by the Legislature.

Turning to what indirectly owned or controlled would mean using the normal rules of statutory construction, the Court of Appeals looked to the Black's Law Dictionary definition of "indirect possession". The Could also noted the Fletcher Cyclopedia of Law of Corporations' definition of "indirectly held shares", which stated that "most investors who hold publicly traded shares hold them indirectly through a broker-dealer or bank, which in turn holds its customers' shares indirectly through a clearing house or central depository". Thus, the Court of Appeals held that indirect ownership in Sec. 208.1117(6), M.C.L. meant ownership through an intermediary.

LaBelle Management, Inc. v. Department of Treasury, Michigan Court of Appeals, No. 324062, March 31, 2016

Backpay and Frontpay Awards Not Taxable

The Michigan Court of Appeals affirmed the Tax Tribunal's determination that the taxpayers were not subject to nonresident city income tax on their backpay and frontpay awards for the tax years at issue because these awards were not employee compensation for work rendered or services performed within the city. The taxpayers, who had served as police officers for the city, had been successful in proving their allegation that they were removed from their employment in retaliation for filing a sexual discrimination lawsuit against the city. Pursuant to federal court judgments, the city paid backpay and frontpay awards after deducting nonresident city income tax for the tax years at issue. The city chose not to reinstate taxpayers and instead opted to make the frontpay awards. According to City of Grand Rapids ordinance, a nonresident individual must pay tax on salary, bonus, wage, commission, and other compensation for services rendered as an employee for work done or services performed in the city. The city argued that since the taxpayers had not been terminated and technically remained employees, the payment of backpay and frontpay awards were for work done or services performed in the city. In this case, Court of Appeals found the taxpayers had not been working or performing services as police officers, and the awards were paid not for the performance of their services but because the city prohibited them from performing services.

LeClear-Gavin et al. v. City of Grand Rapids, Michigan Court of Appeals, No. 324933, 324934, March 24, 2016

Missouri

Mailing Catalogs From Another State Does Not Qualify as Using The Product

The taxpayer was entitled to a refund of Missouri use taxes it paid on catalogs that it printed and mailed outside the state to in-state customers because the taxpayer did not use the catalogs in Missouri. Use tax is imposed for the privilege of storing, using, or consuming within Missouri any article of tangible personal property. Merely mailing the catalogs from another state into Missouri is not the exercise of any right or power over the catalogs incident to the taxpayer's ownership or control over them. The taxpayer exercised that power outside Missouri when it caused the catalogs to be printed and mailed to particular customers in Missouri. Once the catalogs entered Missouri, however, the taxpayer did not take any action in regard to its ownership or control of the catalogs. Consequently, the taxpayer was entitled to a refund of the use tax it had paid on the catalogs.

Office Depot, Inc. v. Director of Revenue, Missouri Supreme Court, No. SC95029, April 5, 2016

New York

Enacted Budget Legislation Includes Middle Class Tax Cut, Other Changes

Enacted as part of New York's 2016-17 budget package, Ch. 60 (S.B. 6409) includes a variety of corporate franchise and personal income changes, as detailed below.

Middle class tax cut: Under the legislation's tax cut provisions, the personal income tax rate for affected taxpayers will drop beginning in 2018. Taxpayers eligible for a tax rate reduction to 5.5%, when fully implemented, include single filers with taxable income up to $75,000, head of household filers with taxable income up to $100,000, and married joint filers with taxable income up to $150,000. Taxpayers eligible for a tax rate reduction to 6%, when fully implemented, include single filers with taxable income between $75,000 and $200,000, head of household filers with taxable income between $100,000 and $250,000, and married joint filers with taxable income between $150,000 and $300,000.

Conformity to new federal filing dates: The legislation aligns various state and New York City tax filing deadlines with new deadlines at the federal level (i.e., generally changing the due date from March 15 to April 15 for corporations and from April 15 to March 15 for partnerships, for taxable years beginning on or after January 1, 2016).

Farm workforce retention credit: For taxable years beginning on or after January 1, 2017, and before January 1, 2022, the legislation creates a new farm workforce retention credit available against the corporate franchise and personal income taxes. The credit amount is determined by multiplying the total number of eligible farm employees by a dollar amount, which increases from $250 in 2017 to $600 in 2021.

STAR credit: The legislation provides for transitioning the school tax relief (STAR) property tax exemption into a personal income tax credit.

New York City school tax reduction credit: The legislation contains provisions converting the school tax relief credit for New York City taxpayers from a city personal income tax credit into a state personal income tax credit. The change applies to taxable years beginning on or after January 1, 2016.

Electronic filing mandate: Electronic filing mandate provisions are extended for three years, until December 31, 2019.

Low-income housing credit: Over a 5-year period, the legislation increases the aggregate dollar amount of credits available for the low-income housing credit from $64 million to $104 million.

Hire-a-veteran credit: The hire-a-veteran credit is extended for two years, through taxable years beginning before January 1, 2019. As extended, the credit is available for the hiring of qualified veterans who commence employment before January 1, 2018.

Empire state commercial production credit: The empire state commercial production credit is extended for two years, through taxable years beginning before January 1, 2019.

Credit for transporting disabled individuals: The credit for companies that provide transportation to individuals with disabilities is extended for six years, through 2022.

Enhanced EITC for noncustodial parents: The legislation makes the enhanced earned income tax credit (EITC) for noncustodial parents permanent. Previously, the credit was scheduled to expire after 2016.

Tax shelter reporting: The expiration date of tax shelter reporting provisions is delayed from July 1, 2015, until July 1, 2019.

Clean heating fuel credit: The clean heating fuel credit is extended so that it applies to purchases before January 1, 2020 (previously, 2017). In addition, the legislation provides that, beginning January 1, 2017, the credit does not apply to bioheat that is less than 6% biodiesel per gallon of bioheat.

Excelsior jobs program: The legislation provides that 100% of the unawarded amounts remaining at the end of 2024 can be allocated in subsequent years. However, no tax credits are allowed for taxable years beginning on or after January 1, 2027. In addition, the maximum aggregate credit components are reduced from $200 million to $183 million for 2016 through 2021, from $150 million to $133 million for 2022, from $100 million to $83 million for 2023, and from $50 million to $36 million for 2024.

Corporate tax reform technical corrections: The legislation makes a variety of technical corrections to the state and New York City corporate tax reform provisions.

New York City biotechnology credit: The New York City biotechnology credit is extended for three years, through taxable years beginning before January 1, 2019.

Beer production credit: For taxable years beginning on or after January 1, 2016, the beer production credit is renamed the alcoholic beverage production credit, and the credit is expanded to include cider, wine, and liquor.

Real property tax credit for manufacturers: Provisions regarding the real property tax credit for manufacturers are amended to specify that, in the case of a taxpayer principally engaged in the production of goods by farming, agriculture, horticulture, floriculture, viticulture, or commercial fishing, the taxpayer is eligible if the taxpayer (1) satisfies the required conditions and (2) leases the real property from a related or unrelated party.

Urban youth jobs program credit: The legislation enhances the urban youth jobs program tax credit by increasing the amount of money allocated to programs four and five.

Ch. 60 (S.B. 6409), Laws 2016, effective April 13, 2016, applicable as noted

Ohio

Taxpayer's Purchases Taxable as Business Fixtures

A taxpayer's purchase of certain items that includes a burglar/fire alarm, an outdoor illuminated sign, electrical wiring and switches, a security/surveillance system, store remodeling, and an air compressor were subject to Ohio use tax because the items were considered as business fixtures. The taxpayer argued that the items were tax exempt as they were incorporated into real property. According to the statute, signs and equipment that were permanently attached to the land and that benefit the specific business conducted thereon, are taxable. In this case, the taxpayer did not provide any documentation or supporting testimony to substantiate that the items were not business fixtures. Therefore, the taxpayer failed to meet its burden of demonstrating the error in the assessment.

Pep Boys - Manny, Moe & Jack of Delaware, Inc. v. Testa, Ohio Board of Tax Appeals, No. 2015-706 , April 4, 2016

South Dakota

Remote Seller Collection Requirement Enacted

South Dakota has enacted sales and use tax collection requirements for remote sellers who meet certain sales thresholds. A retailer is liable for the collection of sales and use tax in South Dakota, even if the seller does not have a physical presence in state, if the seller meets either of the following criteria in the previous or current calendar year: (1) the seller's gross revenue from the sale of tangible personal property, any product transferred electronically, or services delivered into South Dakota exceeds $100,000; or (2) the seller sold tangible personal property, any product transferred electronically, or services for delivery into South Dakota in 200 or more separate transactions. Sellers are responsible for collecting the tax beginning on May 1, 2016.

An expedited appeals process for any challenges to the constitutionality of the law is also provided.

S.B. 106, Laws 2016, effective March 22, 2016, and applicable as noted above

Texas

Taxpayer Not Required to Include Net Loss in Apportionment Formula

The Texas Supreme Court reversed an appellate court decision and held that a taxpayer was not required to include a net loss from the sale of investments and capital assets in its apportionment-factor denominator for purposes of calculating its Texas franchise tax liability.

The taxpayer initially brought suit against the Texas Comptroller when the taxpayer was required to include a net loss in the denominator of its apportionment factor which resulted in a higher ratio of Texas receipts to total receipts and therefore, a higher tax bill. The taxpayer argued that the Texas tax code provides that "only the net gain" from the sale of investments should be included in a key component of the statutory franchise-tax formula. However, the comptroller had adopted a rule that required businesses to include net gain or a net loss. The taxpayer paid an additional $200,000 in franchise taxes and then sued for a refund. The trial court and court of appeals both deferred to the comptroller's rule and ruled against the taxpayer. However, the Texas Supreme Court agreed with the taxpayer and reversed the lower court's decision.

The comptroller's rule states that "if the combination of net gains and losses results in a net loss, the taxable entity should net the loss against other receipts, but not below zero." The taxpayer incurred a net loss, rather than a net gain, and argued it adhered to the Tax Code by not including the net loss in its apportionment-factor denominator. Texas Tax Code Sec 171.105(b) states that "if a taxable entity sells an investment or capital asset, the taxable entity's gross receipts from its entire business for taxable margin includes only the net gain from the sale."

Neither party disputed that the taxpayer suffered only a net loss. The statute clearly requires taxpayers to include only the net gain and the high court held that there was no way to interpret net gain to include a net loss. Therefore, the Texas Supreme Court could not defer to the comptroller's rule requiring inclusion of a net loss in the taxpayer's apportionment-factor denominator because it conflicted with the plain language of Tax Code Sec. 171.105(b).

Therefore, the court held that Tax Code Sec. 171.105(b) does not require taxpayers to include a net loss from the sale of investments and capital assets in its apportionment-factor denominator. Accordingly, the court of appeals' judgment was reversed and remanded.

Hallmark Marketing Co. v. Hegar, Comptroller, Texas Supreme Court, No. 14-1075, April 15, 2016

Utah

Single Sales Factor Apportionment Formula Option Extended to Computer and Electronic Product Manufacturing Businesses

For taxable years beginning on or after January 1, 2016, an "optional sales factor weighted taxpayer" may apportion business income to Utah for corporate income tax purposes using an equally-weighted three factor formula, a double-weighted sales factor formula, or a single sales factor formula. "Optional sales factor weighted taxpayer" means (1) for a taxpayer that is not a unitary group, regardless of the number of economic activities the taxpayer performs, a taxpayer that has greater than 50% of its total sales everywhere generated by economic activities the taxpayer performs that are classified in a code within Subsector 334 (Computer and Electronic Product Manufacturing) of the 2002 or 2007 North American Industry Classification System (NAICS); or (2) for a taxpayer that is a unitary group, a taxpayer that has greater than 50% of its total sales everywhere generated by economic activities the taxpayer performs that are classified in a code within Subsector 334 of the 2002 or 2007 NAICS. A conforming amendment is made to the statutory provision concerning the amount of net loss that a corporation that is acquired by a unitary group may deduct. The State Tax Commission may make rules establishing procedures for making an apportionment formula election.

H.B. 61, Laws 2016, operative as noted

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