

State Tax Alert
12/22/2023

State corporate income and franchise tax developments in the fourth quarter of 2023

This alert provides a summary of the significant legislative, administrative and judicial actions that affected US state and local income/franchise and other business taxes for the period Oct. 1, 2023 through Dec. 22, 2023. These developments are compiled from the EY Indirect/State Tax Weekly and Indirect/State Tax Alerts issued during that period.

Key developments

Massachusetts adopts single-sales factor apportionment, makes other tax changes

Provisions of [H. 4104](#) (enacted Oct. 4, 2023), among other tax changes, adopt a single-sales factor apportionment formula for all industries and change how financial institutions source receipts from investment and trading activity for sales factor purposes.

Massachusetts currently requires manufacturing companies, qualifying defense contractors and qualifying mutual fund service corporations to use a single-sales factor apportionment formula for Corporate Excise Tax purposes. Beginning Jan. 1, 2025, a single-sales factor apportionment formula applies to all industries, with express application to financial institutions. If both the numerator and the denominator are zero, then the corporation's net income will be fully taxable in the state.

Starting in 2025, H. 4104 changes how financial institutions source receipts from interest, dividends, net gains, other income from investment assets and activities, and income from trading assets. Currently, those receipts are sourced to the taxpayer's regular place of business. H. 4104 changes this sourcing to apply a fraction that is based on other receipts, which generally follow the location of the property, customer or borrower. If the statutory application does not reasonably approximate a financial institution's net income from business carried on in Massachusetts, the financial institution can apply to the commissioner to use, or the commissioner may require use of, an alternative method to determine net income. (See Tax Alert [2023-1655](#).)

Legislative developments

New York City: [Int 1070](#) (enacted Dec. 4, 2023) renews the biotechnology tax credit, which lapsed in 2018. The credit can be claimed against the General Corporation Tax, the Unincorporated Business Tax, and the Corporate Tax of 2015 and it is available for tax years beginning on or after Jan. 1, 2023 and before Jan. 1, 2026. A taxpayer that is a qualified emerging technology company located in New York City, engages in biotechnologies and meets eligibility requirement will be allowed to claim the credit. (See SALT Weekly for [Dec. 1](#) and [Dec. 8, 2023](#).)

North Carolina: [HB 259](#) (enacted Oct. 3, 2023) establishes a \$500 cap on the franchise tax imposed on the first \$1 million of a corporation's tax base. The tax rate on the tax base that exceeds \$1 million is \$1.50 per \$1,000. This change is effective for tax years beginning on or after Jan. 1, 2025 and applies to the calculation of the franchise tax reported on the corporate income tax return for 2024 and later.

Effective for tax years beginning on or after Jan. 1, 2022, HB 259 modifies the elective pass-through entity tax (PTET) provisions to expand taxed partnership eligibility. In addition to publicly traded partnerships, the PTET election cannot be made by a partnership that had, at any time during the tax year, a partner who was not one of the following: (1) an individual; (2) an estate; (3) a trust described in Internal Revenue Code (IRC) § 1361(c)(2) or a trust if such trust does not have as a beneficiary any person other than an individual, an estate, a trust or an organization described in IRC § 1361(c)(6); (4) an organization described in IRC § 1361(c)(6); (5) a partnership, including an entity that is classified as a partnership for federal income tax purposes, or an entity that is classified as a corporation for federal income tax purposes.¹ This expansion allows additional trusts and any entity classified

¹ Italics indicate HB 259 changes to the statute as previously enacted.

as a corporation for federal income tax purposes to qualify as eligible partners for purposes of the PTET election. (See SALT Weekly for [Sept. 29 and Oct. 6, 2023](#).)

Pennsylvania: [SB 815](#) (enacted Dec. 14, 2023) amends the corporate net income tax (CNIT) manufacturing, innovation and reinvestment deduction, by changing the eligibility requirements. To qualify for the deduction, a taxpayer must show a private capital investment exceeding \$50 million (from \$60 million) for the creation of new or refurbished manufacturing capacity within the applicable time-period (changed from three years of a designated start date). The calculation of eligible expenses for a qualified manufacturing innovation and reinvestment deduction must include payments made in advance of a project's start date if the payments are for the purchase of, or partial payment for, new equipment for the project that exceeds \$1 million in value. The maximum allowable deduction for a project with a private capital investment exceeding \$50 million (from \$100 million) equals 25% of the private capital investment used in the creation of new or refurbished manufacturing capacity. A taxpayer can use the deduction in an amount not to exceed 5% of the private capital investment used in the creation of the new or refurbished manufacturing capacity in any one year. The maximum allowed deduction of 37.5% for private capital investment exceeding \$60 million but less than \$100 million only applies to applications made before Jan. 1, 2024. These changes apply to tax years beginning after Dec. 31, 2023.

The law also conforms to the federal grantor trust rules for Pennsylvania personal income tax purposes. Beginning on or after Jan. 1, 2025, certain enumerated classes of income received by a resident or nonresident trust from Pennsylvania sources are taxable to the grantor of the trust or another person to the extent the grantor/other person is treated as the trust's owner under IRC §§ 671 through 679, whether or not such income is distributed or distributable to the trust's beneficiaries or accumulated. Trust taxability provisions do not apply to the extent the grantor/other person is taxable on the income of the trust under the aforementioned grantor trust change. (See SALT Weekly for Dec. 15 and Dec. 22, 2023.)

Texas: On Nov. 7, 2023, Texas voters approved Proposition 4, a Constitutional amendment authorizing property tax relief for individuals and certain non-homestead real property. Because Proposition 4 was approved, the increase of the franchise tax exemption to \$2.47 million (from \$1 million) will take effect, starting with reports originally due on or after Jan. 1, 2024.² (See SALT Weekly for [Nov. 10 and Nov. 17, 2023](#).)

Wisconsin: [Act 36](#) (enacted Oct. 25, 2023) updates Wisconsin's conformity to the IRC. For tax years beginning after Dec. 31, 2022, Wisconsin conforms to the IRC as amended to Dec. 31, 2022, with exceptions.³ Amendments to the IRC enacted after Dec. 31, 2022, do not apply for Wisconsin purposes. Act 36 updates certain references for 2023 and clarifies which IRC updates enacted in 2020 and 2021 do or do not apply for Wisconsin purposes. (See Tax Alert [2023-1926](#).)

Judicial developments

California: A California appeals court upheld the 2012 voter-approved Proposition 39, which mandated the use of a single-sales factor apportionment formula, eliminated the option to use a three-factor (property, payroll and sales) formula, and allowed certain cable companies to exclude a portion of in-state states in apportioning their income.⁴ (See SALT Weekly for [Oct. 27 and Nov. 3, 2023](#).)

A California Superior Court (court) has found California [Technical Advice Memorandum 2022-01](#) (TAM 2022-01) and revised Publication 1050⁵ — in which the California Franchise Tax Board (FTB) discussed the application of P.L. 86-272⁶ to activities conducted over the internet — to be “invalid ‘underground regulations’” in violation of the California Administrative Procedure Act (APA).⁷ The San Francisco Superior Court in granting American Catalog Mailers Association's Motion for Summary Adjudication, rendered TAM 2022-01 and revised Publication

² The increase to the exemption was enacted under See SB 3 (2nd Special Sess.), but only took effect with voter approval of Proposition 4.

³ For tax years beginning after Dec. 31, 2020 and before Jan. 1, 2023, the conformity date is generally Dec. 31, 2020.

⁴ *One Technologies, LLC v. Franchise Tax Board*, No. B318787 (Cal. Ct. App., 2nd App. Dist., Div. 1, Oct. 23, 2023).

⁵ For more on the TAM, see Tax Alert [2022-0281](#).

⁶ P.L. 86-272 is a federal law that prohibits states from imposing state income tax on out-of-state sellers whose in-state activities do not exceed soliciting orders of tangible personal property.

⁷ *American Catalog Mailers Association v. Franchise Tax Board*, Case No. CGC-22-601363 (Cal. Superior Ct., San Francisco Cnty., Dec. 13, 2023).

1050 void, saying both were regulations within the meaning of the California APA but neither was adopted in compliance with the APA's requirements. (See Tax Alert [2023-2109](#).)

Minnesota: In *Cities Management, Inc.*,⁸ the Minnesota Supreme Court affirmed the Minnesota Tax Court's ruling that income derived from the goodwill generated by the sale of company stock was apportionable business income. (See Tax Alert [2023-2000](#).)

Administrative developments

Colorado: The Colorado Department of Revenue, in response to recent litigation, [repealed](#) Colo. Regs. § 39-22-103(5.3), which had clarified that Colorado's definition of "IRC" incorporates federal changes on a prospective basis only. Specifically, the rule had provided that "[the IRC for Colorado tax law purposes] does not, for any taxable year, incorporate federal statutory changes that are enacted after the last day of that taxable year." In 2022, a Colorado appeals court determined that the rule was contrary to the statutory language. Amendments repealing the rule were adopted on Nov. 8, 2023, and take effect on Dec. 30, 2023. (See SALT Weekly for [Nov. 10](#) and [Nov. 17, 2023](#).)

Hawaii: The Hawaii Department of Taxation issued updated guidance⁹ on the state's elective PTET, which applies to tax years beginning after Dec. 31, 2022. The election to be subject to the PTET is made annually, and once made it is irrevocable for that tax year and is binding on all eligible members of the electing pass-through entity. (See SALT Weekly for [Dec. 1](#) and [Dec. 8, 2023](#).)

Indiana: The Indiana Department of Revenue issued [guidance](#) on the state's new elective PTET, which can be claimed starting in 2022.¹⁰ The guidance includes examples reflecting the application of the PTET. (See SALT Weekly for [Oct. 13](#) and [Oct. 20, 2023](#).)

Iowa: The Iowa Department of Revenue [extended](#) the deadline to make the 2022 election to be subject to the PTET from Jan. 2, 2024 to the later of April 30, 2024 or the due date for filing the 2022 Form IA 1065 or 2022 Form IA 1120S, including extensions. (See SALT Weekly for [Dec. 1](#) and [Dec. 8, 2023](#).)

Mississippi: The Mississippi Department of Revenue issued [guidance](#)¹¹ on the changes HB 1733 (Miss. Laws 2023) made to depreciation methods that can be used for (1) specified research or experimental expenditures, (2) expenditures for business assets that are qualified property (QP) or qualified improvement property (QIP), and (3) IRC § 179 property. For tax years beginning after Dec. 31, 2022, taxpayers can treat specified research or experimental expenditures that it paid or incurred during the tax year in connection with its trade or business as an expense that is not chargeable to the capital account. The taxpayer can also elect to take a full and immediate deduction for such expenditures and/or depreciate such expenditures in accordance with IRC § 174 as it existed on Jan. 1, 2021. In addition, for that same period, expenditures for business assets that are QP or QIP are eligible for 100% "bonus" depreciation and can be deducted as an expense incurred during the tax year in which the property was placed in service. Taxpayers can elect to take a bonus depreciation deduction for such expenditures and/or to depreciate the expenditures under IRC § 168. Regarding IRC § 179 property, taxpayers can elect to treat the cost of IRC § 179 property that was placed in service during the tax year as an expense that is not chargeable to a capital account. Such costs are allowed as a deduction for that year; the treatment of the deduction conforms to IRC § 179 in effect for that year. (See SALT Weekly for [Oct. 27](#) and [Nov. 3, 2023](#).)

Montana: The Montana Department of Revenue issued [guidance](#) on the state's new PTET.¹² (See SALT Weekly for Dec. 15 and Dec. 22, 2023.)

Nebraska: The Nebraska Department of Revenue issued updated [frequently asked questions](#) on the state's PTET.¹³ (See SALT Weekly for Dec. 15 and Dec. 22, 2023.)

⁸ *Cities Management, Inc. v. Comm'r. of Rev.*, Case No. A23-0222 (Nov. 22, 2023).

⁹ Haw. Dept. of Taxn., [Tax Information Release No. 2023-03](#) (Oct. 31, 2023) (supersedes TIR 2023-01 (July 21, 2023)).

¹⁰ Ind. Dept. of Rev., Income Tax Info. Bulletin #72B (Oct. 2023).

¹¹ Miss. Dept. of Rev., Notice 8-23-003 "Depreciation Notice" (Oct. 20, 2023).

¹² Mont. Dept. of Rev., Montana Pub. 4 "Pass-Through Entity Tax Guide" (Nov. 2023).

¹³ Neb. Dept. of Rev., PTET FAQs (updated Dec. 8, 2023).

New Hampshire: On Nov. 1, 2023, the New Hampshire Commission on Worldwide Combined Reporting for Unitary Business Under the Business Profits Tax issued its final [report](#), recommending against removing water's edge limitations and against the adoption of worldwide combined reporting. (See SALT Weekly for [Oct. 27 and Nov. 3, 2023](#).)

New Jersey: In response to recently enacted corporation business tax reform, the New Jersey Division of Taxation (Division) has issued revised guidance on the following:

- the state's conformity to IRC § 1502, regarding federal consolidated return rules, for combined returns – [TB-103\(R\)](#) (revised Oct. 13, 2023)
- income reporting and accounting methods of non-U.S. corporate members of a combined group – [TB-101\(R\)](#) (revised Oct. 13, 2023)
- net operating losses (NOLs) and combined groups – [TB-95\(R\)](#) (revised Oct. 11, 2023)
- general information on the NOL regime for tax years ending on and after July 31, 2019 – [TB-94\(R\)](#) (revised Oct. 11, 2023)
- changes to the dividend exclusion and the historic ordering of NOLs, the dividend exclusion, and the international banking facility deduction – [TB-111](#) (issued Oct. 11, 2023)
- gross income tax allocation and uniformity with corporation business tax sourcing for receipts business income – [TB-112](#) (issued Oct. 11, 2023)
- included and excluded business entities in the combined group and the minimum tax of a taxpayer that is a member of a combined group ([TB-86\(R\)](#) – revised Nov. 1, 2023)
- banking corporations and combined returns ([TB-91\(R\)](#) – revised Nov. 1, 2023)
- income reporting and returns for banking corporations for privilege periods ending on and after July 31, 2020 ([TB-99\(R\)](#) – revised Nov. 1, 2023).

The Division issued new guidance on captive investment companies, captive real estate investment trusts and captive regulated investment companies and combined groups ([TB-113](#) – issued Nov. 1, 2023). (See SALT Weekly for [Oct. 13 and Oct. 20, 2023](#) and for [Nov. 10 and Nov. 17, 2023](#).)

Pennsylvania: The Pennsylvania Department of Revenue (PA DOR) issued revised [guidance](#)¹⁴ on the application of the net loss deduction limitation under IRC §§ 381 and 382 in computing the Pennsylvania CNIT. The PA DOR explained that IRC § 382(d)(3) incorporates disallowed interest under IRC § 163(j) within the term “pre-change loss”. Because of this, the PA DOR added a discussion on IRC § 163(j) interest expense limitation carryforwards to address the impact on the amount of net loss deductible for CNIT purposes for the tax periods beginning after the initial period affected by the TCJA's changes to IRC § 163(j). The guidance provides a detailed discussion on the appropriate application of IRC § 382 and the amount of the IRC § 163(j) carryforward interest that can be deducted. (See SALT Weekly for [Oct. 13 and Oct. 20, 2023](#).)

The PA DOR issued updated [guidance](#)¹⁵ on the CNIT treatment of IRC § 163(j) to provide additional information to taxpayers filing a federal consolidated return regarding limits to the Pennsylvania separate company interest expense deduction. For tax years 2019 and later, taxpayers with an IRC § 163(j) limitation for an earlier period and that participate in a current year federal consolidated return with no IRC § 163(j) interest expense limitation on current year interest expenses can fully deduct on their CNIT return current year separate company interest expenses, as well as prior year interest expense limitation carryforwards. The PA DOR said that while it did not expect exceptions to this policy to be common, it noted that exceptions could arise where the current year limitation on the deduction of a carryforward amount of previously denied interest expense is limited by a Code section other than IRC § 163(j), such as IRC § 382, or to the extent the current/former year limitation is determined at the partnership level. In addition, the PA DOR said that carried forward related-party interest addback would have to be added back for CNIT purposes in the same year as the remaining federal interest expenses are deducted on the taxpayer's federal pro-forma IRS Form 1120. (See SALT Weekly for [Oct. 13 and Oct. 20, 2023](#).)

¹⁴ PA DOR, Corporation Tax Bulletin 2008-03 (updated Oct. 11, 2023).

¹⁵ PA DOR, Corporation Tax Bulletin 2019-03 (updated Oct. 12, 2023).

Texas: The Texas Comptroller of Public Accounts (Comptroller) issued [guidance](#) on costs that may be included as benefits for the compensation subtraction under the franchise (“margin”) tax.¹⁶ The Comptroller determined that the following items, provided that they are deductible for federal income tax purposes and not already included in wages or cash compensation, may be included as benefits in the compensation subtraction: immigration expenses, meals, relocation-travel expenses, personal use of a company-provided vehicle, health checkups, sports club, cell phones, entertainment (i.e., tickets to events or other similar items), book and journal subscriptions, dues, and studies/tuition reimbursement. The Comptroller determined that the following items may not be included as a benefit: business use of a company-provided vehicle, recruiting referral fees, travel per diems, other entertainment (i.e., expenses for internal taxpayer celebrations for employees), and training. (See SALT Weekly for [Nov. 10](#) and [Nov. 17, 2023](#).)

Utah: The Utah State Tax Commission (UTC) updated its “Recent Info and Tax Law Changes” [webpage](#) to provide guidance on the employee retention credit (ERC). The UTC explained that, for federal income tax purposes, employers claiming the ERC must reduce their income tax payroll deduction by the amount of the ERC for the tax year. Utah taxable income is calculated based on federal adjusted gross income for individuals and federal taxable income for corporations. Thus, ERC associated payroll expenses are not deductible on the Utah income tax returns to the extent they are not deductible on the federal return. (See SALT Weekly for [Dec. 1](#) and [Dec. 8, 2023](#).)

Developments to watch

New York: On Aug. 9, 2023, the New York (NY) Department of Taxation and Finance, in accordance with the NY State Administration and Procedures Act, [proposed](#) regulations under Article 9-A corporate franchise tax and Article 33 insurance corporation franchise tax.¹⁷ The proposed regulations, when finalized, will implement comprehensive franchise tax reform for corporations, banks and insurance companies, which was enacted in 2014, with subsequent technical and conforming amendments enacted in 2015 and 2016. The proposed regulations cover a wide range of areas, such as imposition of tax (nexus) and activities protected/unprotected under P.L. 86-272; apportionment; computation of tax; combined unitary reporting; and qualified NYS manufacturers. These and other areas addressed in the proposed regulations may impact NYS taxpayers in various industries. First Impressions Alert [2023-1397](#) outlines our observations around certain key provisions in the latest proposed regulations. The regulations may be finalized in the near future.

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¹⁶ Tex. Comp. of Pub. Accts., STAR No. 202310005L (Oct. 13, 2023).

¹⁷ The notice of proposed rulemaking was [published](#) in the Aug. 9, 2023 NYS Register.

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