State Tax Alert
01/07/2025

State corporate income and franchise tax developments in the fourth quarter of 2024

This alert provides a summary of the significant legislative and administrative actions that affected US state and local income/franchise and other business taxes for the fourth quarter of 2024. These developments are compiled from the EY Indirect/State Tax Weekly and Indirect/State Tax Alerts issued during that period.

Key developments

Louisiana's tax reform legislation affects businesses and individuals

Louisiana Governor Jeff Landry on December 4, 2024, signed into law a package of tax reform bills, which make several changes that will impact all Louisiana business and individual taxpayers.

Franchise tax: HB 3 repeals the Louisiana franchise tax effective for franchise tax periods beginning on or after January 1, 2026. The law amends several tax incentive statutes to remove references to the franchise tax.

Corporate income tax: HB 2 makes several changes to the corporate income tax. These changes, unless otherwise specified, take effect for tax years beginning on or after January 1, 2025.

Rates: Prior to 2025, Louisiana had a graduated corporate income tax rate of 3.5% (first $50,000), 5.5% (next $100,000) and 7.5% (excess over $150,000). Starting in 2025, a flat 5.5% corporate income tax rate applies. Corporate taxpayers may also claim a newly created $20,000 standard business deduction.

Full expensing: The law adopts permanent full expensing under Internal Revenue Code (IRC) Section 168(k) and (e)(6) and IRC Section 174. Starting in 2025, taxpayers (corporate, pass-through entity (PTE) and individual) may elect to deduct the full cost of qualified property, qualified improvement property (collectively, "qualified property") and research and experimental (R&E) expenditures. Expenditures for qualified property placed in service, or R&E expenditures paid or incurred, on or after January 1, 2025, are eligible for bonus depreciation or bonus amortization, respectively. If the election is made, such expenditures must be deducted as expenses incurred by the taxpayer during the tax year in which the expenditure was incurred.

Foreign trade zones (FTZs): Preferential apportionment treatment for companies with sales and inventory in FTZs is eliminated. Prior to the change made HB 2, taxpayers can exclude from the numerator of the corporate income tax apportionment factor property and sales attributable to property located in an FTZ.

Inventory tax credit (ITC) repeal: The ITC for C corporations is repealed for tax periods beginning on July 1, 2026. The refundability of the ITC, however, is repealed for C corporations for tax periods beginning on or after January 1, 2025. Unused ITCs may be carried forward for an additional five years. The ITC remains unchanged for individuals and PTEs.

IRC Section 280C: HB 2 repeals the deduction for expenses disallowed by IRC Section 280C.

Tax credits: HB 2 accelerates the sunset of, or immediately eliminates, many corporate income tax credits. Credit certifications to enter into new, or renew already existing, contracts requested after June 30, 2025, will not be granted for the following credits: (1) angel investor tax credit, (2) enterprise zone program credits, (3) Louisiana quality jobs program credits, (4) sound recording investor tax credit, and (5) retention and Modernization Act investment credit.

Tax credits that are repealed for tax periods beginning on and after January 1, 2025, and for franchise tax periods beginning on or after January 1, 2026, include certain jobs tax credits (e.g., credits similar to the federal work opportunity tax credit), new markets tax credit, low-income housing tax credit, brownfields investor tax credit, and solar energy tax credit.

HB 2 lowers the annual aggregate caps for the motion picture tax credit to $125 million (from $150 million) beginning July 1, 2025, and the historic rehabilitation tax credit to $85 million (from $125 million) beginning January 1, 2025. HB 2 imposes a $12 million annual aggregate cap on the research and development (R&D) tax credit effective each fiscal year beginning July 1, 2025. R&D tax credit claims are "allowed on a first-come, first-served basis."

PTEs: HB 10 shifts the rate of the elective PTE tax from a graduated rate to the 3% flat rate for individuals. For nonresidents computing taxable income, HB 10 repeals deductions for (1) expenses disallowed by IRC Section 280C, and (2) net capital gains.

HB 10, like HB 2, adopts full expensing under IRC Section 168(k) and (e)(6) and IRC Section 174 for individual income tax purposes, repeals many business tax credits, and retains other specified credits. A similar deduction is allowed for trusts and estates.

For more on this development and other tax changes enacted in Louisiana, see Tax Alert 2024-2266.

San Francisco voters approve changes to the City's business taxes

Proposition M (Prop M), effective January 1, 2025, drastically changes San Francisco’s business taxes, including the gross receipts tax, the homelessness gross receipts tax, the overpaid executive gross receipts tax and the administrative office tax. Changes made by Prop M include, but are not limited to, the following:

- Reducing the number of business activity classifications from 14 to seven for the gross receipts and homelessness gross receipts taxes, each with their own rate schedules
- Changing the gross receipts tax rates applicable to the new categories of business activities, with future rate increases
- Applying the homelessness gross receipts tax to business activities – the same business activity categories that apply to the gross receipts tax – with San Francisco gross receipts over $25 million
- Shifting the calculation of San Francisco gross receipts, so it is based more on sales and less on payroll expenses, depending on the type of business
- Increasing the small business exemption to the gross receipts tax to exempt a person or combined group with gross receipts within the city that do not exceed $5 million
- Establishing a small business exemption from the homelessness gross receipts tax
- Modifying the calculation of the overpaid executive gross receipts tax

For a more detailed discussion on the changes in Prop M, see Tax Alert 2024-1825.

Legislative developments

Illinois: HB 4636 (enacted December 20, 2024) modifies the tax credit for hiring returning citizens, by providing that for tax years ending before December 31, 2025 (from tax years ending before December 31, 2024) the amount of credit allowed for each qualified returning citizen hired is limited to $1,500. A previously enacted law change increases the amount of the credit that can be claimed to $7,500 effective for tax years ending on or after December 31, 2025. (See SALT Weekly for December 20, 2024 and January 3, 2025.)

Massachusetts: H. 5077 (enacted December 4, 2024) includes a fix to the commonwealth's single sales factor apportionment provisions. Under a law enacted in 2023, Massachusetts will require the use of a single sales factor apportionment formula for corporate excise tax purposes by all industries effective for tax years beginning on or after January 1, 2025. The 2023 law modified statutory provisions on factor drop out (e.g., when there is no denominator). As originally enacted, a missing sales factor (i.e., both the numerator and the denominator are zero) meant that a corporation's net income would be fully taxable in the state.

As amended, and effective for tax years beginning on or after January 1, 2025, a corporation's taxable net income will be apportioned to Massachusetts based on the corporation's property and payroll in the state if the sales factor does not apply. The law specifies that the sales factor does not apply if: (1) both the numerator and the denominator are zero, (2) the denominator is less than 10% of one-third of a corporation's taxable net income,

or (3) the commissioner determines that the sales factor is insignificant in producing income. The sales factor, however, may apply when only the sales factor numerator is zero. (See Tax Alert 2024-2331.)

H. 5100 (enacted November 20, 2024) establishes the climatetech tax incentive program. An owner or tenant of a certified climatetech company, to the extent authorized, may claim a refundable credit against its corporate excise/personal income tax in an amount not exceeding 50% of the owner's total capital investment in a climatetech facility. The credit will be distributed in equal parts over five tax years that correspond with the owner's or tenant's certification period. The amount of credit available to a tenant may not exceed the tenant's total lease payments for occupancy of the climatetech facility for the tax year. The aggregate amount of climatetech credits available is capped at $30 million per year. The climatetech tax incentive program also provides for: (1) a refundable jobs credit that can be taken against the corporate excise and personal income taxes, and (2) credits for certain qualified research expenses and basic research payments that can be taken against the corporate excise tax. Excess research credit is not refundable but may be carried over for up to 15 years.

The law also creates a refundable internship tax credit equal to the lesser of $5,000 or 50% of the wages paid to each net-new qualified intern employed in the tax year. The amount of credit an employer can claim per year is capped at $100,000. (See SALT Weekly for December 6 and 13, 2024.)

S. 2967 (enacted November 20, 2024) modifies the refundable income tax credit for capital investment in an offshore wind facility by reducing the number of new full-time employees the facility must employ from "not less than 200" to "not less than 50." This change takes effect February 18, 2025. (See SALT Weekly for December 6 and 13, 2024.)

Administrative developments

Florida: In TIP No. 24C01-02 (November 6, 2024) the Florida Department of Revenue (FL DOR) discusses the state's conformity to the IRC. While Florida adopts the IRC in effect as of January 1, 2024, the state continues to decouple from certain provisions, including bonus depreciation; qualified improvement property placed in service on or after January 1, 2018; business meal expenses; and film, television and live theatrical production expenses. The FL DOR further explained that Florida law allows a deduction for wages and salaries paid in Florida when the federal deduction for wages and salaries is disallowed under IRC Section 280C(a), but it does not allow a deduction for other federal credits. (See SALT Weekly for November 1 and 8, 2024.)

Illinois: In response to a ruling request of a combined unitary group, the Illinois Department of Revenue (IL DOR) said that based on the facts presented, under 35 ILCS Section 5/304(a) the group's sales of certain tangible personal property (hereafter "products") that are shipped to a third-party distributor warehouse in Illinois terminate in, and are sourced to, Illinois, regardless of whether the distributor later distributes and ships the product outside Illinois. These sales, the IL DOR, explained are included in the Illinois' sales factor numerator. Sales of the group's products that are shipped to a distributor's warehouse located outside Illinois terminate outside of, and are not sales in, Illinois, even if the distributor subsequently moves the goods to locations in Illinois. Ill. Dept. of Rev., IT 24-0008-GIL (Sept. 17, 2024). (See SALT Weekly for November 1 and 8, 2024.)

Iowa: The Iowa Department of Revenue announced[1] that the corporate income tax rate for 2025 will stay the same as the rate for 2024 because the net corporate income tax receipts for fiscal year 2024 did not reach the $700 million threshold required to reduce the rate. Thus, the 2025 tax rate is 5.5% on the first $100,000 and 7.1% on all income over $100,000. (See SALT Weekly for October 18 and 25, 2024.)

Massachusetts: In TIR 24-16 (November 26, 2024), the Massachusetts Department of Revenue describes two recently enacted credits – the Massachusetts homeownership credit and the qualified conversion project credit – and changes to the historic rehabilitation credit and to the community investment credit. The Massachusetts homeownership credit is available starting in 2025 for qualified homeownership development projects authorized by the Massachusetts Housing Finance Agency. The qualified conversion project credit is available 2025 through 2029 for conversion projects certified by the commonwealth's Executive Office of Housing and Livable Communities. The historic rehabilitation credit has been extended through 2030 (from 2027). The community

[1] IA Dept. of Rev., Order 2024-01 "Certifying Iowa Corporate Income Tax Rates for 2025 under Iowa Code section 422.33(1)(b)" (Oct. 15, 2024).

investment credit, which was set to expire in 2025, has been made permanent. (See SALT Weekly for November 15 and 29, 2024.)

Michigan: The Michigan Department of Treasury (MI DOT) issued RAB 2024-23 (December 4, 2024) to corporations reporting business income under Part 2 of the Michigan Income Tax Act (MITA) on computing federal taxable income (FTI), net operating losses (NOLs) and business losses for purposes of calculating its corporate income tax (CIT) liability under the MITA. In computing FTI, Michigan decouples from IRC Section 168(k) (bonus depreciation) and Section 199 (domestic production activities deduction). Taxpayers will have to adjust for these amounts in computing FTI. After computing FTI, the adjustments under MCL 206.623(2)(c) are applied, including the add-back of NOLs deducted in computing FTI. The MI DOT explained that a CIT business loss is not the same as a federal NOL or a Michigan Business Tax (MBT) business loss. Under the CIT, only business losses incurred after December 31, 2011, may be deducted. Business losses incurred under the former MBT may not be claimed on a CIT return. (See SALT Weekly for December 6 and 13, 2024.)

In RAB 2024-24 (December 17, 2024) the MI DOT provides updated guidance on the state's alternative apportionment provisions to address recent judicial developments. The guidance describes the procedures and standards governing the use of an alternative apportionment formula, including the criteria for evaluating requests for alternative apportionment such as proving the statutory method does not fairly reflect the taxpayer's business activity in the state, showing quantitative and qualitative distortion, and proving the proposed alternative apportionment formula is reasonable. (See SALT Weekly for December 20, 2024 and January 3, 2025.)

Tennessee: In Letter Ruling # 24-09 (November 5, 2024), the Tennessee Department of Revenue (TN DOR) discussed a taxpayer's use of Tennessee NOLs and tax credits against future Tennessee franchise and excise tax liabilities following an IRC Section 368(a)(1)(F) reorganization. The TN DOR explained that, in the case of a merger, consolidation or like transaction, the successor taxpayer generally may not use the qualified NOLs and tax credits generated by the predecessor taxpayer; however, an exception to this general rule applies in certain circumstances – the Tennessee Carryover Exception. Under this exception the predecessor's qualified NOLs and Tennessee tax credits may be carried over and used on the successor taxpayer's franchise and excise tax return when the "predecessor taxpayer merges out of existence and into a successor taxpayer that has no income, expenses, assets, liabilities, equity, or net worth." In this case, the predecessor merged into a "shell company," which "accounts for the restructuring while also preventing the NOLs and tax credit from merging into an already existing company." Based on the facts presented, the TN DOR found that the Tennessee Carryover Exception applies, and, as such, the taxpayer may use the Tennessee NOLs and tax credits generated by the operating company. (See SALT Weekly for December 6 and 13, 2024.)

Developments to watch

California: The California Franchise Tax Board (FTB) on September 13, 2024, issued a Notice of Proposed Rulemaking to adopt amendments to its market-based sourcing rules for California corporate franchise and income tax purposes. (The rules would be codified at California Code of Regulations, title 18, Section 25136-2 (Proposed Regulation.))The FTB released an "Initial Statement of Reasons" for the amendments, as well as draft language of the Proposed Regulation, which would affect asset managers, government contractors, research and development companies, and taxpayers in many other industries. (See Tax Alert 2024-1784.) On January 6, 2025, the FTB announced that a public hearing on the Proposed Regulation would be held on January 30, 2025. The FTB also issued modified text of the Proposed Regulation; notably, the FTB revised the proposed applicable date of the amended regulation to tax years beginning on or after January 1, 2025 (from January 1, 2024).

The validity of a recent law changes to California's corporate income tax apportionment provisions made by SB 167 (enacted June 27, 2024) are being challenged. SB 167 added new statutory provision Cal. Rev & Tax Code Section 24831.6, which provides that when a corporation receives income that is excluded from taxable business income, it must also exclude this income from its apportionment factor.[2] In creating this provision, the Legislature stated that its intent is that (1) FTB Legal Ruling 2006-1 on the treatment of apportionment factors attributable to income exempt from California's corporate income tax "apply with respect to apportionment factors attributable

[2] For purposes of this provision, "not included in 'net income'" is defined as "income from transaction and activities that is not included in net income subject to apportionment for any reason, including … exclusion, deduction, exemption, elimination, or nonrecognition."

to the income of taxpayers subject to tax under the Corporation Tax Law," and (2) new Cal. Rev & Tax Code Section 24831.6 "apply to any apportionment formula currently and formerly allowed…" This change applies to tax years beginning before, on or after the effective date of SB 167, and took effect immediately. The plaintiff is seeking an order adjudicating that the new statutory provision "is not a clarification of, or statement of, prior law under the separation of powers doctrine …" and it "violates due process limitations on retroactive tax legislation."[3]

District of Columbia: On December 20, 2024, the Deputy Chief Financial Officer of the District of Columbia Office and Tax Revenue (OTR) gave public notice of its second proposed amendment to rules (Prop. D.C. Mun. Regs. tit. 9, Section 105.14) that would require taxpayers filing returns with the District of Columbia to submit a copy of their federal income tax return (including any schedules or other information provided to the Internal Revenue Services), subject to certain income thresholds. This change was first proposed in October 2024. The December notice indicates that the regulations are being re-proposed to specify that the copy of the federal income tax return must be in electronic form. The OTR intends to adopt the second proposed amendment no less than 30 days from the publication of its notice. (See SALT Weekly for December 20, 2024 and January 3, 2025.)

Maine: The Maine Revenue Services has proposed amendments to Rule 801 "Apportionment" to modify provisions regarding sales other than sales of tangible personal property. Receipts from the performance of services generally are sourced to the state where the services are received. A proposed amendment would provide that a service may be received by a person that did not pay, or contract, for them. The determination of where services are received would be based on all available facts including the books and records of the taxpayer and related parties. Another proposed amendment would make clear that there is a distinction between determining where the service is received and determining the amount of gross receipts from the performance of services in Maine. Proposed amendments would add several examples of sourcing receipts from the performance of services under the general rule, including for: (1) in-person services, (2) services concerning real property, (3) services concerning tangible personal property, (4) services concerning teaching and training, (5) advertising and related services, (6) cable TV services, and (7) pharmacy benefit management services. (See SALT Weekly for December 6 and 13, 2024.)

Massachusetts: The Massachusetts Department of Revenue issued proposed amendments to 830 CMR 62.5A.1: Non-Resident Income Tax, specifically to the rules for non-resident members of PTEs on how to allocate and apportion income to Massachusetts. Proposed amendments reflect that a single sales factor apportionment formula is adopted for tax years beginning on or after January 1, 2025. Proposed amendments also would repeal 830 CMR 62.5A.1(6)(e) – the special apportionment rules for gain on the sale of an ownership interest in a partnership that holds real property in Massachusetts. (See SALT Weekly for November 1 and 8, 2024.)

Michigan: Bills approved by the General Assembly – HB 5100 and HB 5101 – if signed into law would create an R&D tax credit that may be claimed against the corporate income tax and the withholding tax for flow-through entities. Effective for tax years beginning on or after January 1, 2025, a taxpayer in an authorized business would be able to the claim the credit for R&D expenses incurred during the calendar year. For an authorized business with 250 or more employees, the credit would equal 3% of the taxpayer's qualifying R&D expenses incurred during the year up to the base amount and 10% of such expenses in excess of the base amount; the total amount of credit that could be claimed by the taxpayer would be capped at $2 million per year. For authorized businesses with less than 250 employees, the credit would equal 3% of the taxpayer's qualifying R&D expenses incurred for the year up to the base amount and 15% of such expenses in excess of the base amount; the total amount of credit that could be claimed by the taxpayer would be capped at $250,000 per year. Certain taxpayers would be eligible to claim an additional credit equal to 5% of its qualifying R&D expenses used to calculate the above credit. The additional credit would be capped at $200,000 per year. The aggregate amount of all R&D credits would be capped at $100 million per year. A taxpayer would not be able to assign or transfer the R&D credit. The amount of credit that exceeds the taxpayer's tax liability would be refunded.

Virginia: Tax changes in Virginia Governor Glenn Youngkin's amendments to the biennial budget announced on December 18, 2024, include the adoption of market-based sourcing for sourcing sales from services. (See SALT Weekly for December 20, 2024 and January 3, 2025.)

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[3] *Cal. Taxpayers Association v. Cal. Franchise Tax Bd.*, Case No. 24CECG03564 (*Notice of Motion and Motion for Summary Adjudication*, filed Dec. 12, 2024 with the Cal. Superior Ct., Cnty. of Fresno).

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