Multi-State Tax Update

Texas CPA Society - Dallas
20th Annual Convergence
Sheraton Dallas Hotel
May 2, 2025

Jordan Goodman
KILPATRICK TOWNSEND & STOCKTON LLP

TXCPA DALLAS

Agenda

Nexus

- P.L. 86-272, third-party nexus, pre-*Wayfair* nexus and corporate income tax nexus.

Income Tax and Gross Receipts Tax

- Unitary analysis and combined reporting, Ohio CAT and Washington B&O Tax

Apportionment

- Calculating the apportionment factor and alternative apportionment

Sale and Use Tax

- Base and Situsing Updates

Unclaimed Property and Other Fun Stuff

NEXUS

P.L. 86-272 Death by a Thousand Cuts.

In *Santa Fe Natural Tobacco Co. v. Department of Revenue*, Or. Sup. Ct., No. SC S069820 (6/20/24), Petition For Certiorari denied December 16, 2024.

The Oregon Supreme Court held a taxpayer's activity of providing "prebook orders" exceeded the protection of P.L. 86-272.

The Taxpayer was a New Mexico corporation selling branded tobacco products to wholesalers, who would in turn sell to Oregon retailers. Taxpayer representatives traveled to Oregon to market its products to Oregon retailers. A representative provided a retailer with a "prebook order" which required the wholesaler to fulfill the order.

The Court held that the prebook order process facilitated sales and exceeded P.L. 86-272 protection.

P.L. 86-272 Does the Second Thousand Cuts Matter?

Uline, Inc. v. Commissioner of Revenue, MN. Sup. Ct., No. A23-1561 (8/7/24). The Minnesota Supreme Court ruled employees who collected and reported market data exceeded P.L. 86-272 protection.

Taxpayer was a catalog and internet-based distributor of shipping and packaging supplies. The Tax Court found that the following activity exceeded 86-272 protection when performed in the state of Minnesota because the activities were not de minimis and served a separate business purpose independent from the solicitation of orders: Collecting and reporting market data concerning competitors on a twice-monthly basis at minimum.

On appeal to the Minnesota Supreme Court, the Court agreed with the Tax Court and found that "the preparation of Market News Notes by Uline's sales representatives is not exclusively the "solicitation of orders," and is consequently not protected from state taxation by [P.L. 86-272]."

Pre-*Wayfair* Nexus – Washington Edition

Orthotic Shop, Inc. & S&F Corp. v. State of Washington Dept. of Revenue, No. 39321-6-III (Wash. Ct. App. 2024). The Washington Court of Appeals held in that two merchants were responsible for Washington sales and business and occupation ("B&O") tax assessments.

The tax dispute involved a retailing B&O tax and a retailing sales tax assessment against two merchants for sales they made on an online retailer's website. The audit report asserted that the merchants were "retailers" who maintained a nexus to Washington because they maintained a stock of goods in the online retailer's warehouses located there.

The merchants admitted before the Court of Appeals that they sold their goods to consumers and not to the online retailer. However, the merchants challenged the assessment and argued that the online retailer's provision of fulfillment services necessarily rendered it a "consignee" responsible for remitting retailing B&O tax and sales tax on transactions facilitated through its website.

Economic Nexus…It's a thing!

Mastercard Int'l Inc. v. S.C. Dep't of Revenue, No. 20-ALJ-17-0008-CC (S.C. Admin. Law Ct. June 3, 2024) Appeal pending Appellate Court.

The South Carolina Administrative Law Court held that Mastercard had nexus with the state for Corporate Income Tax purposes based on transactions between South Carolina merchants and Mastercard credit and debit cardholders.

Mastercard processes transactions using a network of payment systems. Prior to the Department's 2017 audit, the Taxpayer had never filed a South Carolina corporate income tax return. The Department claimed that Taxpayer was present in the state because it operates by acquiring contracts with banks and placed advertisements targeting cardholders and merchants to use or accept their cards within its borders. They further argue that income is produced within the state every time a fee is charged when a card is used within South Carolina.

The Court held that the record demonstrated that the source of the Taxpayer's fees are the transactions between the merchants and cardholders within its network. As such, it affirmed the Department's imposition of the tax.

Pre-*Wayfair* Nexus – South Carolina Edition

Amazon Servs., LLC v. S.C. Dep't of Revenue, 442 S.C. 313 (Ct. App. 2024), Appeal pending South Carolina Supreme Court.

The South Carolina Appellate Court held Amazon, a marketplace facilitator, was required to collect and remit sales tax for third-party sellers in 2016 prior to the U.S. Supreme Court's decision in *South Dakota v. Wayfair, Inc*.

In 2019, the Department audited Amazon, specifically targeting sales made by third-party sellers on Amazon's marketplace. Amazon argued that it was not a "seller" of third-party products, and that the Department's assessment retroactivity applied the State's 2019 marketplace facilitator law in violation of the Due Process and Equal Protection Clauses.

The Court disagreed, stating that the statute unambiguously defined a "seller" as any individual or entity who sells or auctions tangible personal property ("TPP"), whether owned by such person or others.

Finally, the court noted that there was no violation of Due Process or Equal Protections because the Department was not attempting to apply the 2019 amendment retroactively but instead applied the language of the law as it appeared in the 2016 statute. The court in rejecting the Taxpayer's constitutional arguments found that the 2019 legislation was a clarification of existing law.

INCOME TAX AND GROSS RECEIPTS TAX

Ultimate Boxing...Sourcing Receipts for Ohio CAT – Part I

VVF Intervest LLC v. Harris, No. 2019-1233 (Ohio Bd. Tax App. 2023) Appeal pending OH Supreme Court.

The Ohio Board of Tax Appeals held a Kansas-based soap manufacturer does not owe Ohio gross receipts tax on sales of products that were initially stored at a third-party warehouse in Ohio before being shipped to other states.

The Board of Tax Appeals reasoned that Ohio is not the ultimate delivery point because the bars are temporarily held in a distribution center owned by an unrelated third party in Ohio.

After ruling for VVF, the Board stated the Department had been applying the law too narrowly by requiring that a company have contemporaneous knowledge of where the item's ultimate destination will be at the time of initial shipment.

Ultimate Boxing...Sourcing Receipts for Ohio CAT – Part II

Jones Apparel Group/Nine West Holdings v. McClain, Nos. 2020-53, 2020-54 (Ohio Bd. Tax App. 2023) Appeal pending OH Supreme Court.

The Ohio Board of Tax Appeals (BTA) ruled in that the apparel company; Nine West was not entitled to a commercial activity tax (CAT) refund on products it failed to prove were received outside Ohio.

Nine West, originally filed their CAT returns from 2010 until 2016, to include all income from product shipped from Ohio locations to Ohio distribution centers, including orders where product was to be delivered outside of Ohio. The Department granted refunds of taxes for shipments that specifically indicated final addresses outside of Ohio.

For two wholesale customers, DSW and Dressbarn, the shipping records for the audit period did not indicate the specific final delivery locations, and the Department did not accept Nine West's allocation of these products to locations outside of Ohio based on a sample of more recent shipping data.

Don’t Ask…Don’t Get

Nationwide Agribusiness Ins. Co. v. Mich. Dep't of Treasury, No. 364790 (Mich. Ct. App. June 20, 2024). The Michigan State Court of Appeals held Nationwide Insurance and its various subsidiaries can file its Michigan insurance premiums tax returns as a unitary business to share tax credits across group members.

Nationwide originally filed its Michigan insurance premiums tax returns on a separate return basis but subsequently filed amended returns on a combined basis. There was no form available to file on a combined basis, so the Company created their own combined reporting schedule. Although the Department initially granted the refund requests, the Department reversed course and ordered the return of the refunds with interest and penalties.

The Department argued that unitary returns were not allowed because there was no explicit statutory authority for the filing of such returns under the premiums tax. The Court rejected the argument based on the statutory definition of taxpayer. The Court went on to hold that when companies are a unitary business, the individual entities have “no meaningful existence.” The individual entities that make up the unitary group cease to be separate taxpayers and only one taxpayer remains—the unitary business group.

Poop or Get Off the Pot!

CarMax Auto Superstores, Inc. v. S.C. Dep't of Revenue, No. 21-ALJ-17-0182-CC (S.C. Admin. Law Ct. July 12, 2024) Appeal pending S.C. Appellate Court.

The South Carolina Administrative Law Court held in that CarMax must file combined South Carolina income tax returns.

From 2016 through 2018, the taxpayer and its subsidiaries utilized separate reporting. The Department determined that this use of separate reporting did not fairly represent the extent of the Taxpayer's business activity within the state and that unitary reporting was a reasonable and more accurate representation of their income.

The Court agreed, noting specifically that forced combined unitary reporting reduced the distortion. The Court further held that this case clearly demonstrated the importance of correcting transfer prices in distortive intercompany transactions. As such, the court affirmed the Department's assessment and required the Taxpayer to file a Combined Unitary Report.

Finally, the Poop and the Pot Meet!

S.B. 298, enacted on March 11, 2024, allows the Department to require a taxpayer to file a combined return if the Department "has reason to believe that any taxpayer conducts its trade or business in a manner as to fail to fairly represent the extent of the taxpayer's business activity in this State through the use of transactions that lack economic substance or are not at fair market value between members of an affiliated group of entities."

A transaction has "economic substance" if: the transaction, or the series of transactions of which the transaction is a part, has one or more reasonable business purposes other than the creation of state income tax benefits; and the transaction, or the series of transactions of which the transaction is a part, has economic effects beyond the creation of state income tax benefits.

The bill provides additional guidance regarding what qualifies as a transaction with "economic substance."

The bill provides that "In determining whether transactions between members of the affiliated group of entities are not at fair market value, the department shall apply the standards contained in the regulations adopted under Section 482 of the Internal Revenue Code."

Prior to the enactment of S.B. 298, there was no statutory framework providing guidelines for the Department to exercise its power to require the filing of a combined return. The Department now has certain requirements it needs to satisfy before requiring combined reporting.

Florida Appellate Court Rejects Conformity!

Verizon Commc'ns Inc. v. Fla. Dep't of Revenue, 386 So. 3d 599 (Fla. Dist. Ct. App. 2024), review denied, No. SC2024-0737, 2024 WL 3964918 (Fla. Aug. 28, 2024)

On February 28, the Florida District Court of Appeals issued two companion decisions in *Verizon Commc'ns Inc. v. Dep't of Revenue*, addressing Florida's conformity with federal tax code's treatment on NOL Exception to Limitations.

In the first ruling, the court held that Florida's general conformity with federal tax laws does not extend to the federal tax mitigation rules that allow reopening expired tax years for NOL adjustments. Florida enforces a strict three-year limitation under Fla. Stat. §215.26, preventing the court emphasized that Florida's tax statutes provide no exception to its strict non-claim statute (Fla. Stat. §220.02(3)), making it powerless to create an exception where none exists.

In the second ruling, the court addressed whether Florida may deviate from federal rules when calculating NOLs for state tax purposes. It ruled in favor of Verizon, affirming that Florida tax law follows the federal Internal Revenue Code (IRC § 172) for NOL calculations. The court rejected the Florida Department of Revenue's attempt to impose a proportional limitation methodology not supported by Fla. Stat. § 220.13(1)(b)1.

TXCPA DALLAS

Illinois Denies "Substance" of 80/20 Company

PepsiCo Inc. and Affiliates v. Illinois Department of Revenue et al., case number 2022TX000155 (January 9, 2025). The Circuit Court of Sangamon County agreed with the Illinois Department of Revenue holding that PepsiCo could not exclude Frito-Lay from the Illinois combined unitary group.

The court stated "expatriates are not the common law employees" of PepsiCo Global Mobility LLC, ("PGM") which the court found to be a shell company. Thus, the payroll could not be included in a calculation to determine the 80/20 status of Frito-Lay. An 80/20 company — an entity that conducts 80% or more of its business activities outside the U.S. — is excluded from a combined group when filing Illinois income tax returns. Frito-Lay did not qualify for that exclusion.

The court's order states, "The evidence at trial was clear that PGM was created to operate and was, in fact, operating as a 'shell' company for purposes of tax benefits for Frito-Lay. . .The evidence presented at trial, including the examination and cross-examination of witnesses, established that PGM was an entity on paper, established for and existing to shield Frito-Lay from tax liability."

Further the court found "Frito-Lay derives the majority of its profits from the purchase and resale of products in the United States, Frito-Lay is not an 80/20 company and should not have been excluded from PepsiCo's 2016 and 2017 combined Illinois tax returns."

See also: *PepsiCo Inc. and Affiliates v. The Illinois Department of Revenue,* No. 1-23-0913 Appellate Court First Judicial District (March 19, 2025). The court affirmed the Tax Tribunal holding Frito Lay was not an 80/20 company and upheld the imposition of penalties.

Not Everything is Unitary...Even if it Generates More Tax Revenue!

Dep't of Taxation v. FJ Management Inc., Case No. 0701-23-2 (Va. Ct. App. Nov. 12, 2024). The Virginia Appellate Court affirmed the trial court's decision that the taxpayer and PTC did not form a unitary business, stating that (1) the taxpayer and Pilot Travel Center ("PTC") were engaged in separate and discrete lines of businesses, (2) the taxpayer did not have any significant management authority over PTC because it only had a 17% ownership interest, and (3) the taxpayer and PTC did not derive any economies of scale through their relationship.

Taxpayer operated interstate travel centers which provided various services to long-distance truckers. In 2008, taxpayer filed for bankruptcy and sold all of its travel centers to Pilot Corp. in return for a minority stake in PTC and cash to satisfy its creditors.

Taxpayer originally reported the income it earned from PTC as apportionable income, but later sought refunds, claiming the income was allocable.

The Department denied the refund claims and the taxpayer filed suit arguing that it was not in a unitary business with PTC and thus was not required to include the income from PTC in its apportionable income.

No Facial Discrimination in the Big Apple

The *Walt Disney Co. v. New York Tax Appeals Tribunal*, New York Court of Appeals DTA NO. 828304 & *International Business Machines Corp. v. New York Tax Appeals Tribunal*, New Your Court of Appeals DTA NOS. 827825, 827997 AND 827998, Petition for Certiorari denied January 21, 2025.

IBM and Disney received royalty payments from foreign affiliates. The foreign affiliates were not New York taxpayers. Prior to 2014 under N.Y. Tax Law § 208(9)(o)(3) taxpayers could deduct royalty income received from related parties who were subject to New York corporate income tax

The taxpayers argued that the deduction limitation violated the internal consistency test and constituted facial discrimination against interstate and foreign commerce, violating the dormant Commerce Clause.

The New York Court of Appeals upheld the lower court's the ruling and held that a related member must be subject to New York's addback requirement for royalty income to be excluded from the taxpayer's net income. Since their foreign affiliates weren't New York taxpayers, their deductions were denied.

If It Smells Like a Duck, It May Be a Turkey

Precision Castparts Corp. v. Nebraska Dep't of Rev., 317 Neb. 481 (2024). The Nebraska Supreme Court held the amounts included under IRC § 965 are neither dividends nor deemed dividends. The Court relied on reasoning in *Moore*, which concluded that IRC § 965 does not operate by deeming shareholders to have received a distribution of retained earnings from CFCs.

Taxpayer included amounts under IRC § 965 in its Nebraska gross income. Taxpayer argued that the inclusion amounts were "dividends received or deemed to be received from corporations which are not subject to the Internal Revenue Code" and were therefore eligible for Nebraska's dividends received deduction (DRD).

Instead, the Court found that "Section 965 treats the inclusion as pass-through income and attributes the retained earnings of a CFC to its shareholders."

Accordingly, the Court concluded the income under IRC § 965 cannot be considered as a dividend or deemed dividend that qualifies as deductible under the state DRD.

Non-Business Income and Expense Lives!

The Arkansas Supreme Court affirmed that Murphy Oil is entitled to a $4 million tax refund in holding that income from atypical activity qualifies as nonbusiness income and is fully allocable to the state of domicile.

Murphy, an Arkansas-based retail fuel operator, incurred $650 million in interest expenses during a 2013 corporate spin-off. Though initially apportioned across states, Murphy later amended its 2014–2015 returns to allocate all interest to Arkansas, citing the nonrecurring nature of the transaction.

The Court agreed, finding the spin-off was not part of Murphy's regular business activities, and therefore the interest expense was nonbusiness income under UDITPA, properly allocable entirely to Arkansas.

See also U.S. Beef Corp. v. Arkansas.

APPORTIONMENT ISSUES

Just Not the Same: Income and Apportionment

In re S. Minn. Beet Sugar Coop., No. 19034447 (Cal. OTA 2023). The California Office of Tax Appeals (OTA) rejected in the Franchise Tax Board's (FTB's) longstanding position that denied apportionment factor representation for business activities that generate deductible income and ruled a beet sugar manufacturer can include deductible income in its California apportionment formula.

SMBSC is an agricultural cooperative headquartered in Minnesota. In 2005, SMBSC acquired a California-based company that is not a cooperative and filed combined reports with SMBSC as a unitary business. As a cooperative business, SMBSC was allowed a deduction under California R&TC Section 24404 for income "resulting from or arising out of (its) business activities for or with (its) members."

The OTA concluded that the removing the deductible income from the apportionment formula would result in excluding unitary business activities that contribute to the production of apportionable business income from the apportionment formula without support in the UDITPA and without showing distortion.

And We Mean IT!

In re Microsoft Corp. and Subsidiaries, Case No. 2103736 (Cal. OTA 2024). The OTA ruled in that Microsoft's could include 100% of its foreign dividends in its sales factor denominator. Quoting its previous decision in *In re Southern Minnesota Beet Sugar*, the OTA stated [t]here is no language . . . to support FTB's position that unitary business activities are excluded from the apportionment formula if they relate to deductible income."

Microsoft repatriated $108 billion in dividends for the 2017 tax year in connection with the IRC Section 965 inclusion rules. Microsoft included those dividends, which did not come from entities included in the water's-edge group, in its income tax base. It deducted 75 percent of the dividends based on CA's dividends received deduction.

The FTB disagreed with Microsoft's position, saying: FTB Legal Ruling 2006-01 requires that only net dividends be included in the denominator of the sales factor. Further arguing, gross receipts from qualifying dividends should be excluded under Cal. Code Reg. §25137(c)(1)(A) as a substantial and occasional sale and RTC section 25137 warrants the use of an alternative apportionment method.

The OTA rejected all three of the FTB's arguments.

California – Senate Bill 167...That's Cheating!

As a result of the *Microsoft* and *Southern Minnesota Beet Sugar Co-op* decisions , the California Legislature amended SB 167 to include Section 25128.9, which was then quickly passed and signed into law. Section 25128.9 amended the statute to prevent the retroactive application of those decisions. The Legislature stated Section 25128.9 was enacted to "clarify" existing law. Thus, applying apply retroactively to California's adoption of UDITPA in 1966.

Two matters are pending in Sacrament Superior Court challenging the legislation:

- National Taxpayers Union v. California Franchise Tax Board, *et. al.* Case No. 24CV016118
- California Taxpayers Association v. California Franchise Tax Board, *et. l.*, Case No. 24CV016118

TXCPA DALLAS

Even Oregon Gets It...

Microsoft Corp. v. Department of Revenue, OR. Tax Ct. No. TC 5413 (8/29/24). The Oregon Tax Court held Microsoft is permitted to include Sec. 965 income in its apportionment sales factor

Oregon allows taxpayers an 80% deduction for its Sec. 965 repatriated dividends.

The Department disallowed the taxpayer's inclusion of the 20% Sec. 965 income that was included in its tax base.

The Oregon Tax Court found that, as a matter of statutory construction, the deemed included amounts were included in the definition of "sales" because they derived from the primary business activity of the taxpayer.

Alternative Apportionment to What?

E.I. DuPont de Nemours v. Minn. Comm'r of Revenue, No. 9485-R (Minn. Tax Ct. 2024), Appeal pending MN Supreme Court.

- The Minnesota Tax Court (the "Court") held that the Minnesota Department of Revenue correctly applied an alternative apportionment scheme to DuPont (the "Taxpayer"). The Department argued, and the Court agreed, that alternative apportionment better represented the Taxpayer's economic activities and taxable income within Minnesota than the traditional apportionment scheme used initially by the Taxpayer.
- The Department argued that the Taxpayer's net income resulting from "forward exchange contract transactions" should be included in the Taxpayer's apportionment factor, instead of the gross receipts from such contracts.
- The Taxpayer argued that using gross receipts was the most accurate method because they best represent their business activity in the state.
- The Court determined that the Department had demonstrated that these transactions differed from the Taxpayer's usual business transactions and granted the Department's alternative apportionment request.

Does Your Dog Bite?...That's Not My Dog!

Mastercard International Inc. v. Department of Revenue, No.20-ALJ-17-0008-CC (SC Admin Ct. June 2024), Appeal pending S.C. Appellate Court.

The South Carolina Administrative Law Court (ALC) utilized a "look through" concept finding the receipts from Mastercard's services should be sourced to the locations where individual cardmembers and merchants consummated credit card transactions using Mastercard-branded credit cards, rather than the locations of the banks that were Mastercard's direct customers.

South Carolina requires receipts from services to be sourced to the location where the taxpayer performs its "income-producing activity." Based on the evidence introduced at trial, the ALC found that Mastercard's income-producing activity consisted of "providing Network access to Cardholders, Merchants, and banks," and that activity occurred in South Carolina when the cardholder and merchant concluded transactions in the state.

Mastercard argued that its income-producing activity occurred solely at the data center locations used to communicate with its direct customers, that is, the issuing and acquiring banks that issue credit cards to cardmembers and contract with individual merchants.

SALES AND USE TAX

Wait, You Want It All?

Ellingson Drainage, Inc. v. Dep't of Revenue, South Dakota, No. 30280 (February 7, 2024), Petition for Certiorari denied (October 7, 2024).

The South Dakota Supreme Court ruled an infrastructure management company was liable for unpaid use taxes and interest. The company, Ellingson Drainage, Inc., didn't pay sales tax when purchasing the equipment out of state. As a result, South Dakota imposed a use tax on the property when it entered the state.

The company claimed that the tax imposed an unequal burden compared to its activity in the state, especially considering that some equipment was used for only one day. However, the court disagreed, stating that the company benefited from operating in South Dakota, just like any other business. The ruling emphasized that the company was free to bring its equipment back for future projects in South Dakota without facing additional use tax.

The South Dakota Supreme Court applied a *Complete Auto* four-part standard to support their position that the imposition of the use tax was not a burden on interstate commerce.

I Have to Do What? Exemption Certificates

Toolpushers Supply Co. v. Miss. Dep't of Revenue, No. 2021-CT-01186-SCT (Miss. 2023). The Mississippi Supreme Court upheld in the Mississippi Department of Revenue's assessment of sales tax.

The Taxpayer is a Wyoming-based company that sells supplies to energy (primarily oil and gas) companies from a retail location in Mississippi. Under Mississippi law, the wholesale purchaser must present the seller with a certificate signaling their tax-exempt wholesaler status. In this case, purchasers presented this certificate, but the Taxpayer took no further steps to confirm the purchaser was a retailer that re-sold the purchased products.

The Taxpayer argued that the transactions at issue were wholesale and thereby exempted sales tax collection and remittance, but the Court held the Taxpayer's action of simply confirming the purchaser had the required documentation failed to satisfy the separate and additional requirement that the wholesale be made in good faith.

Bundled Transactions. Look at the Paperwork.

Bekkerman et al., v. California Department of Tax and Fee Administration, CA App. Ct. Case Number C093763 (2/27/2024). The California Court of Appeals upheld the determination that Regulation 1585 requires California cell phone retailers who are also wireless providers to collect sales tax on the full retail price of a phone rather than the discounted price customers receive when they bundle a phone with ongoing telecommunication services through a provider.

The plaintiffs' argued Regulation 1585 contravened three basic rules of sales tax in California: 1) services are nontaxable, 2) discounts should be excluded from gross sales price, and 3) tax should be charged on the agreed upon price. The Appeals Court agreed regarding the services and discount exclusion but disagreed on what was the agreed upon price. The agreed upon price, according to the Court of Appeals and Regulation 1585, was the initial payment for the phone plus subsequent monthly payments and the retailers were not offering a true discount. Rather, retailers can recoup the discount through the customers' monthly payments.

The Court went on to detail that under the California Revenue and Tax Code, "gross receipts" is the total sale price represented in money, whether actual payment was received in money or through some other form of payment. Since the carrier-retailers can allocate monthly payments from customers to the cell phone cost, CDTFA can also levy sales tax on the full cost. A bundled transaction is created because the discount on the phone is not offered unless customers also agree to the service.

The Court rejected plaintiffs' arguments regarding the technical issues with Regulation 1585. Plaintiffs claimed the Regulation was adopted without evidence as to adverse effect on economic impact for businesses or consumers and without public notice and hearings which are required under the California Administrative Procedures Act (APA). The Court first declared that CDTFA could reasonably determine there would be no adverse impact on businesses. Finally, the Court addressed the argument related to public notice and hearings, where they also rejected the plaintiffs' contentions. There was a public hearing where participants objected to the original text, thus creating both the hearing and notice.

Services Smervices…Who Knows?

Dynamic Logic Inc. v. Tax Appeals Tribunal of N.Y., No. 535445 (N.Y. Div. Tax. App. 2024). The New York State Supreme Court upheld the Tax Appeals decision that Dynamic Logic (Taxpayer) sells taxable information services when performing a service to measure the effectiveness of advertisements.

The Taxpayer collects advertising information for its clients and measures advertisements' performance against baseline metrics established by another Taxpayer database. The Taxpayer claimed that the "primary reason" for report purchases is this narrative content. The Taxpayer also argued that, even if they were deemed a taxable information service by the Court, such service is exempt from tax because the information provided is not incorporated in reports furnished to other persons.

New York law requires those who sell "information services" to collect and remit sales and use tax. However, no tax is owed if the furnishing of such information is "personal or individual" in nature and is "not or may not be substantially incorporated in reports furnished to other persons."

The Court found that the Taxpayer had not presented sufficient evidence demonstrating that its interpretation of the statute was the only reasonable interpretation, as required by New York law.

Big Brother is Everywhere!

Assurance Wireless USA, LP f/k/a Virgin Mobile USA, LP v. Wash. Dep't of Revenue, No. 101873-8 (WA S.Ct. March 7, 2024). The Washington Supreme Court held that Assurance Wireless USA's (Assurance) transactions were taxable, but that imposition of the tax was unconstitutional based on the Supremacy Clause of the United States Constitution and the intergovernmental immunity doctrine.

Assurance provides free wireless phones and service contracts to eligible low-income individuals through a "Lifeline" program. Universal Service Administrative Co. ("USAC") is a non-profit subsidiary of the National Exchange Carrier Association ("NECA"). NECA is a for-profit association created by the FCC to administer the fees that long-distance companies pay to access local telephone networks in the US. By contrast, USAC is tasked with the collection of funds from telecommunications carriers to support low-income programs such as Assurance's Lifeline and disburse a subsidy to the company. USAC's board members are appointed or approved by the FCC, all funding must be FCC-approved, and Congress has sanctioned the FCC's reliance on USAC to administer these programs.

The Court held that the transactions would normally be taxable because they were retail sales when telecommunications services were exchanged for Lifeline support funds. The Court held that USAC, not the FCC, was the buyer legally obligated to pay for Assurance for these services, thereby placing sales tax obligations on USAC. The Court found that the USAC was an instrumentality of the government and immune from state taxation.

Do You Feel Me?

Netflix Inc. v. Dep't of Revenue of Colo., No. 2023CV30184, (Denver Dist. Ct. 2024). The Denver District Court held Colorado's sales tax did not apply to the sale of Netflix's subscription service because such products were not "corporeal" and could not be perceived by sight or touch, therefore falling outside the definition of tangible personal property ("TPP").

The Colorado Department of Revenue (the "Department") argued the tax applied to all goods that could be perceived by any bodily senses, and thus, the video streaming service offered by Netflix constituted a taxable piece of TPP.

The Colorado Legislature defined TPP as "corporeal" and "tangible" in its original 1935 version of the act. Accordingly, the Court held that the original legislature intended to limit the scope of the tax. The Department argued that lawmakers at the time of adoption would have viewed streaming subscriptions as TPP, citing a 1943 Arizona case in which the court found that a song played on a jukebox was TPP because the playing of music was perceptible.

D.H. Holmes Revisited?

AAA Life Ins. Co. v. Mich. Dep't of Treasury, No. 365613 (Mich. Ct. App. 2024). The Michigan Court of Appeals affirmed a lower court ruling holding that AAA Life Insurance Co. owes use tax on advertising materials it mailed via an out-of-state contractor.

The Taxpayer is a life insurance provider that contracted with a Missouri-based marketing company to process, print, and mail advertisements each year, some of which were addressed to Michigan residents.

The Taxpayer argued that it lacked "sufficient control" over the contractor's work and the mailing to be subject to the Michigan use tax. According to the Taxpayer contract, the contractor owned all the mailers and their copyrights and performed all the publishing and mailing of these advertisements. The Court disagreed, affirming the lower court's finding that "only some level of control is needed" to constitute a taxable use under Michigan law and that the Taxpayer had exerted sufficient control to justify tax imposition. Here, the Taxpayer provided approval for final proofs, maintained authority for changes, reviewed materials for legal compliance, and had final approval on all advertisements

Chicken or the Egg?

Lowe's Home Centers, LLC v. S.C. Dep't of Revenue, No. 6062 (S.C. Ct. App. 2024). The South Carolina Court of Appeals affirmed that Lowe's Home Centers, LLC must collect and remit sales tax on the retail, as opposed to the wholesale, price of materials sold to customers with associated installation services.

Taxpayer's customers can purchase materials from its hardware stores and can purchase installation services via third-party contractors. When purchased together, the Taxpayer would not charge the customer's sales tax on such materials and instead personally remitted tax based on the wholesale price. Following the Department's assessment, the Taxpayer protested, arguing that it acted as a contractor for those sales and that the proper fair market value of the materials was the wholesale price.

The Court held that the Taxpayer acted as a retailer when the materials for an installation contract were purchased and thereafter as a contractor overseeing installation. This retail sale thereby established the fair market value of the materials and should be the basis for the application of sales tax. The fact that the retail sale and installation were listed as separate items within the contracts further supports this notion that the Taxpayer knew a retail sale occurred.

Another Way to Look at the Chicken or the Egg…

Illinois Court of Appeals has allowed in *People ex rel. Lindblom v. Best Buy Stores LP* (No. 1-24-0379) a False Claims Act (FCA) suit to proceed against Best Buy and held that the trial court erred in dismissing the suit. The issue was whether Best Buy knowingly failed to collect and remit sales tax on appliances purchased with installation services after an Illinois Department of Revenue compliance alert is a genuine issue of material fact.

The court set out that Best Buy collected and remitted sales tax on dishwashers and microwaves sold without installation services between 2002 and November 2020 but paid use tax on the cost of the goods if the appliances were sold with installation services.

Best Buy had been audited by the DOR for the sales tax periods between 2005–2007 and 2011–2013, but the DOR did not assess any liability against the company for improperly collecting tax at the conclusion of the audits.

The DOR issued a compliance alert in June 2015, explaining that most retailers were not acting as construction contractors and a separate agreement to install tangible personal property did not convert a retail sale of the tangible personal property to a construction contract. Giving the example of a dishwasher sold by an appliance store, the alert added that the seller would pay sales tax on the receipts from the sale of the property.

The court found that Best Buy’s actions after receiving the compliance alert raised a genuine issue of material fact regarding whether it is liable under the FCA, saying that Best Buy's receipt of the compliance alert should have made it examine or alter its tax practices.

This One Was a Gimmie!

Orthofix Inc. v. S.C. Dep't of Revenue, No. 2023-000318 (S.C. 2024). The South Carolina Supreme Court held that a state sales tax exemption for durable medical equipment (DME) was facially unconstitutional because it discriminated against out-of-state sellers and thus was in violation of the Dormant Commerce Clause.

The Court struck down the entire exemption, finding that the geographic restrictions were inseparable from the remainder of the exemption. The statute, enacted in 2007, provided an exemption for DME paid directly by Medicaid or Medicare funds only if the seller's principal place of business was located in South Carolina.

The Court struck the exemption down in its entirety, stating that the exemption was facially unconstitutional, and the geographic provision was non-severable. The statute was facially unconstitutional because a foreign DME seller was required to remit sales tax, while local ones were not. The Court rejected the Department's argument that the purpose of the exemption was non-discriminatory, holding that the dormant commerce clause prohibits a state from taxing interstate transactions to favor local businesses over out-of-state ones. Furthermore, the Court noted that the geographic provision was not independent and severable, invalidating the entire statute.

Increase the Base by Taxing What....?

Maryland enacted the first-in-the-nation gross receipts tax imposed on digital advertising.

Taxpayers challenged the tax under the: Internet Tax Freedom Act, Commerce Clause, Due Process Clause, and First Amendment

- Defenses include novel theories like Anti-Commandeering and no private right of action.

Four cases pending at the Maryland Tax Court (Peacock, Apple, Google, Meta).

Several other states have considered imposing similar taxes so the outcome of the Maryland litigation will have consequences in other states.

But We Don’t Sell That!

The Louisiana Court of Appeal, First Circuit, in *Robinson et al. v. Priceline.com Inc. et al.*, 389 So. 3d 168 affirmed that online travel companies' (OTCs) facilitation fees are not subject to Louisiana sales tax on hotel rooms.

The Court clarified that sales tax applies only to the discounted net rate paid by the OTC to the hotel, not the higher retail rate charged to consumers. Because OTCs are neither "hotels" providing taxable services nor "dealers" obligated to collect or remit sales taxes under state law.

It Is What We Say It Is!

The Wisconsin Tax Appeals Commission ruled in *CMFG Life Insurance Co. v. Dep't of Rev.*, Docket No. 20-S-078 that CMFG Group's aircraft and software agreements with PNC Finance constituted taxable sale-leaseback arrangements, despite contractual language suggesting otherwise.

The TAC rejected CMFG's claim that these arrangements were refinancing agreements, concluding that contractual statements about intent "for tax purposes" do not bind the Department of Revenue. Thus, the agreements were subject to Wisconsin sales tax.

Don’t Try To Change Me.

The Pennsylvania Supreme Court ruled in Garcia v. Am. Eagle Outfitters, Inc., No. 27 WAP 2023, 2025 WL 540049 (PA. Feb. 19, 2025) that a merchant’s collection of sales tax does not constitute "conduct of any trade or commerce" under the Unfair Trade Practices and Consumer Protection Law (UTPCPL).

The Court concluded that sales tax collection is a statutory obligation distinct from commercial activities, and even if collected incorrectly, it cannot form the basis of a UTPCPL claim. Merchants collecting sales tax act as government agents, not commercial entities subject to UTPCPL liability.

Texas – Local Tax Standoff

City of Coppell, City of Round Rock, et al. v. Hegar, Case No. D-1-GN-21-003198 (December 3, 2024), Appeal pending. The Travis County Court held the Comptroller was attempting to establish destination sourcing for online orders without legislative authorization. The decision included a permanent injunction.

Previously, cities, including Round Rock, and online retailers would enter into agreements wherein the retailer would locate an office or fulfillment center in the city in return for a rebate as an incentive. The city also benefited because it was then treated as the retailer's in-state place of business, resulting in local sales taxes on those sales being sourced to that locality.

The Comptroller promulgated amendments to Rule 3.334 which would result in sales being sourced to the location of the buyer instead of where the retailer's office or fulfillment centers are based. Round Rock and several other cities sued, and the court determined the rule's adoption violated the state's Administrative Procedure Act process.

UNCLAIMED PROPERTY AND OTHER FUN STUFF

Chevron Overturned, Any State Impact?

In a 6-3 decision, the Supreme Court in *Loper Bright Enterprises et al. v. Raimondo*, 144 S. CT 2244 (2024) overruled *Chevron*, which directed courts to give deference to regulatory interpretations of ambiguous statutes (provided the interpretations were reasonable).

The Court stated that *Chevron* was "misguided because agencies have no special competence in resolving statutory ambiguities. Courts do."

Congress may still vest interpretation powers in agencies when it enacts a statute.

While this case involved federal regulations, it may also impact how courts interpret state regulations.

Legislative Updates-Actual Good News

Delaware adopted S.B. 267, which made technical changes to its unclaimed property law, and S.B. 266, dealing with whistleblowers.

The latter law removes the ability of whistleblowers to directly bring claims of noncompliance with unclaimed property law, but the state attorney general may still do so and may provide whistleblowers with incentives for coming forward. The state also sent out several notices to holders this fall concerning compliance.

Important Take on Time Limits

The Walt Disney Co. v. Rachael Eubanks, Michigan Supreme Court and *Dine Brands Global Inc. v. Rachael Eubanks*, Michigan Supreme Court, Docket Nos. 165391 and 165392. March 24, 2025.

The Michigan Dept. of Treasury has argued that an audit is considered a "proceeding" under the statute that triggers a halt to the statute of limitations clock, whereas Disney and Dine Brands have said that an audit is not a judicial "action or proceeding" that would pause that clock. The Michigan Supreme Court held the start of an audit does not toll the statute of limitations.

However, the court remanded the cases back to the Appeals Court to determine if the issuance of a notice at the completion of the audit starts the running of a new statute of limitations.

You Get Nothing And Like It.

Michigan's Court of Appeals held in Kemerer v. State, No. 362055, 2024 WL 4609911 (Mich. Ct. App. Oct. 29, 2024) that interest is not recoverable on abandoned property returned by the state.

Reversing a lower court decision, the appellate court found the Uniform Unclaimed Property Act (UUPA) explicitly covers property returns and interest provisions, rendering common-law doctrines inapplicable. The court concluded that the claimant was not entitled to interest accrued while the state held the abandoned assets.

Now Children, You Need To Play Nice.

Delaware reached a settlement with a coalition of 30 states in an unclaimed property dispute involving MoneyGram official checks. The dispute centered on whether $190 million in unclaimed checks belonged to Delaware, MoneyGram's state of incorporation, or to the states where the checks were sold. The U.S. Supreme Court previously ruled unanimously that these checks are governed by the Federal Disposition Act and should be remitted to states of purchase. Under the settlement, Delaware will distribute $102 million previously received and $89 million held in escrow, plus interest, among the states according to where checks were purchased.

Questions?

Thank you!

Presenter

Jordan Goodman
KILPATRICK TOWNSEND & STOCKTON LLP
jgoodman@ktslaw.com