

State Income Tax Update

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The Playing Field: The Rules of the Game Have Changed

Challenges Facing State Departments of Revenue

- Decline in Revenue Collections
- Increase in Refund Claims
- Tax Revenue Department Cuts / Hiring Freezes

New Strategies by The Home Team

- Increased Compliance Efforts
- Reducing, eliminating, or increasing tax credits
- Changes to NOL carryforward provisions
- Alternative Income Tax Revenue Generation Being Explored:
 - Amnesty Periods
 - Combined Reporting
 - Aggressive Nexus Positions
 - Alternative Minimum Taxes

The 2008-2009 Season Highlights

- I. Nexus**
- II. Combined Reporting**
- III. Apportionment**
- IV. Other Noteworthy Highlights**

I. Nexus

- A. The Pre-Game Show: Substantial Nexus
- B. Today's Game: The Shift to Economic Nexus
- C. Recent Home Team Wins: Economic Nexus Sufficient
- D. The Standings

The Pre-Game Show: Substantial Nexus

- Constitutional Limits on State's Jurisdiction to Tax:
 - Due Process Clause (14th Amendment)
 - Commerce Clause (Art. I, Sec. 8)
- Commerce Clause = most important line of defense for multistate taxpayers
 - Congress has power to regulate commerce with foreign Nations and among the several states. This affirmative grant of power does not expressly limit state action, but the U.S. Supreme Court has interpreted that the “dormant” Commerce Clause limits state authority to tax.
- Complete Auto Transit's 4-Prong Test
 - Prong #1 = Substantial Nexus
- Geoffrey, Inc. v. South Carolina Tax Commission, 437 S.E.2d 13 (1993): “physical presence” rejected / US denies cert

Today's Game: The Shift to Economic Nexus

- Current Debate: Dispute in State Courts, Statehouses, and Congress about States' authority to tax corporate income.
- Three Areas:
 - Economic Nexus
 - Attributional Nexus
 - Affiliate Nexus

Today's Game: The Shift to Economic Nexus

- Congressional Efforts
 - Business Activity Tax Simplification Act (BAT)
 - Reintroduced February 13, 2009 as H.R. 1083
 - Codified physical presence + allows de minimus (less than 15 days)
 - Mobile Workforce State Income Tax Fairness and Simplification Act of 2009
 - Introduced April 28, 2009 as H.R. 2110
 - Limits personal income taxation to resident state unless physically present in another state for more than 30 days
 - Resident vs. Source
 - Springstein, Michael Jordan not covered
 - Provides clarity and reduces burden on companies
 - Effect on N.Y. stumbling block to passage

Today's Game: The Shift to Economic Nexus

- Examples of State Codification of Economic Nexus
 - New Hampshire (N.H. RSA 77-A:1, XII)
 - Minnesota (Minn. Stat. 290.015)
 - Wisconsin (Wis. Stats., section 71.22(1r)), eff. 1/1/2009

Recent Home Team Wins

- West Virginia v. MBNA America Bank, 220 W. Va. 163, 640 SE2d 226 (2006) , *cert. denied*, 127 S. Ct. 2997 (2007).
 - Business Franchise and Corporate Income Tax Case (WV).
 - Court looked at substantial economic presence rather than physical presence standard.
 - Substantial economic presence test is satisfied because of Taxpayer's significant gross receipts in the State.
 - Taxpayer systematically and continuously engaged in direct mail and telephone solicitation and promotion in the State.
 - Court concluded that the Commerce Clause was not violated.

Recent Home Team Wins

- Lanco Inc. vs. Director, Division of Taxation, 879 A. 2d 1234 (N.J. App. Div. 2005) , *aff'd*, 908 A2d 176 (N.J. 2006) , *cert. denied*, 127 S.Ct. 2974 (2007).
 - Corporate Income Tax (NJ).
 - Lanco licensed its intangible personal property to Lane Bryant, Inc. for use in the latter’s retail operations in New Jersey and other states in return for royalty payments.
 - Lanco had no physical presence in New Jersey.
 - Court held that Lanco has substantial nexus in NJ and that imposition of corporate income tax did not violate Commerce Clause
 - The Court concluded that “[t]he recent, and in our view, the more persuasive authority leads us to join the jurisdictions that have followed *Geoffrey* and to uphold the tax” and that the physical presence requirement applicable to sales and use taxes is not applicable to income tax.

Recent Home Team Wins

- Capital One Bank v. Comm'r, 453 Mass. 1 (Mass. 2009)
 - Corporate Income-Based Excise Tax (MA).
 - Massachusetts statute subjected out-of-state financial institutions to income tax without regard to physical presence in the state if institution exceeded threshold of assets or receipts attributable to in-state borrowers.
 - Massachusetts Appellate Tax Board sustained application of statute to Capital One credit card bank, which had no presence in MA.
 - ATB held that Quill's physical presence requirement was not applicable to an income-based excise tax; applicable test is Complete Auto's substantial nexus prong.
 - ATB adopted a market approach.
 - Mass Supreme Court Affirms ATB and Rejects Taxpayer Appeal.
 - Petition for writ of certiorari pending before U.S. Supreme Court.

Recent Home Team Wins

- Geoffrey, Inc. v. Comm'r, 453 Mass. 17 (Mass. 2009)
 - Corporate Income-Based Excise Tax (MA).
 - Decided on the same day as Capital One.
 - Massachusetts Supreme Court finds that out of state holding company (Geoffrey) with no physical presence in the state had substantial nexus with Massachusetts through its trademark licensing activities.
 - Court relied on its decision in Capital One: Complete Auto's substantial nexus test applies, not Quill's physical presence test.
 - Court found that Geoffrey encouraged Massachusetts customers to shop at affiliated (Toys R Us) retailers.
 - Petition for writ of certiorari pending before U.S. Supreme Court.

Pending Game

- Overstock.com Inc. v. Levin, Franklin County, Ohio, Court of Common Pleas, No. 08CVH11-16412 (filing made Nov. 14, 2008)
 - Ohio Commercial Activity Tax (CAT)
 - Issue: the applicability of the CAT's economic nexus provision to Overstock.com
 - CAT: taxpayer subject to CAT if it has Ohio property or payroll of at least \$50,000; or gross receipts of at least \$500,000 from Ohio sources; or at least 25% of its total P,P,R are in Ohio; or its domicile is Ohio.
 - Will the CAT be treated as a transactional tax in analyzing the issue?
 - Status: motions to dismiss

Nexus: The Standings

- Stats are in: the home team is winning
- Season over (certiorari denials)
 - Lanco (2007)
 - MBNA (2007)
- Play-Off Potential
 - Capital One (MA)
 - Geoffrey (MA)

II. Combined Reporting

- A. Pre-Game Show: The National Shift to Combined Reporting
- B. New Players: The 6 New Combined Reporting States
- C. Recent Wins /Losses: Noteworthy Unitary Cases
- D. Team Strategy: Impact on Industry

The Pre-Game Show

- Fairly stable landscape for many years
- East Coast / West Coast
- For many years, only Illinois, New Hampshire, and Maine east of the Mississippi River
- 1990s: targeted measures (e.g., add-backs)
- Debate re: increase to state revenue

Combined Reporting States as of 2004

West of Mississippi

- Alaska
- Hawaii
- Oregon
- California
- Idaho
- Montana
- Utah
- Arizona
- Wyoming
- North Dakota
- Nebraska
- Kansas
- Minnesota

East of Mississippi

- Illinois
- New Hampshire
- Maine
- (Additional states had discretionary authority to require combined reporting under certain circumstances)

Combined Reporting States As of 2009

West of Mississippi

- Alaska
- Hawaii
- Oregon
- California
- Idaho
- Montana
- Utah
- Arizona
- Wyoming
- North Dakota
- Nebraska
- Kansas
- Minnesota
- TEXAS (2008)

East of Mississippi

- Illinois
- New Hampshire
- Maine
- * VERMONT (2006)
- * MICHIGAN (2007)
- * NEW YORK (2007)
- * MASSACHUSETTS (2009)
- * WEST VIRGINIA (2009)
- * WISCONSIN (2009)

The 6 New Players

State	Effective TYB	Enactment
Vermont	TYB on or after 1/1/06	P.A. 152, Laws 2004 (H. 784)
New York	TYB on or after 1/1/07	L. 2007, ch. 60 (A.B. 4310-C)
Michigan	TYB on or after 1/1/08	L. 2007, P.A. 36 (w/enactment of MBT)
West Virginia	TYB on or after 1/1/09	L. 2008, c. 215
Massachusetts	TYB on or after 1/1/09	Ch. 173, Laws 2008 (H.B. 4904)
Wisconsin	TYB on or after 1/1/09	Act 2, Sec. 9343 Laws 2009 (S.B. 62)

The Minor Leagues

State	Bill	Status
• Alabama	HB 865	Died/Adjourned
• Connecticut	SB 807	Died/Could Come Back
• Florida	SB 2270	Pending
• Iowa	SF 211	Died/Adjourned
• Louisiana	HB 754	Pending
• Maryland	HB1244/SB603	Died/Adjourned**
• Missouri	SB 241	Died/Adjourned
• New Mexico	SB 389	Died/Adjourned
• Rhode Island	SB 776	Pending
• Tennessee	SB 502/HB1350	Pending

*Maryland has informational combined reporting requirements

Key Combined Reporting Factors

1. Composition of the Group

- A. “Unitary Business” Definition
- B. Common Ownership
- C. Eligible Entities
- D. Water’s Edge Group
- E. Worldwide Elections
- F. Consolidated Elections
- G. Specialized Industries
- H. State-Specific FYI’s

A Four-State Comparison....

A. Definition of a “Unitary Business”

VT	<p>“one or more related business organizations engaged in business activity both within and without this state among which there exists a unity of ownership, operation and use; or an interdependence in their functions” 32 VSA Section 5811; Code of Vt. Rules Section 1.5862(d)-6.</p> <p>Regulations cite <u>Butler Brothers</u>, <u>Container Corp.</u>, <u>Mobil Oil</u>.</p>
MA	<p>“...activities of two or more corporations under common ownership that are sufficiently interdependent, integrated or interrelated through their activities so as to provide mutual benefit and produce a significant sharing or exchange of value among them or a significant flow of value between the separate parts” 830 CMR 63.32B.2(2)</p>
NY	<p>“substantial intercorporate transactions” which means substantial intercompany receipts, substantial intercompany expenditures, or substantial intercompany asset transfers. N.Y. Tax Law § 211.4 (a)</p>
WI	<p>“...a single economic enterprise that is made up either of separate parts of a single business entity, of multiple business entities that are related under section 267 or 1563 of the Internal Revenue Code, or of a commonly controlled group of business entities that are sufficiently interdependent, integrated, and interrelated through their activities so as to provide a synergy and mutual benefit that produces a sharing or exchange of value among them and a significant flow of value to the separate parts.” Wisc. Stat. § 71.255 (1)(n).</p>

B. Common Ownership

VT	<p>“. . .more than 50 percent of the voting stock of each member corporation is directly or indirectly owned by a common owner or owners, either corporate or non-corporate or by one or more of the member corporations.” Code of Vt. Rules Section 1.5862(d)-4. Regulations require certain family ownership attribution.</p>
MA	<p>“. . .more than 50 percent of voting control of each member of the group is directly or indirectly owned by a common owner or owners”; common owner can be corporate or non-corporate, and need not be member of the group.</p>
NY	<p>Ownership or control “either directly or indirectly substantially all the capital stock of one or more other corporations, or substantially all the capital stock of which is owned or controlled either directly or indirectly by one or more other corporations or by interests which own or control either directly or indirectly substantially all the capital stock of one or more other corporations” N.Y. Tax Law § 211.4 (a)</p>
WI	<p>Four ways a “commonly controlled group” is defined:</p> <ol style="list-style-type: none"> 1.“direct or indirect ownership” in “stock representing more than 50% of the voting power” or if the parent corporation or any of the connected corporations owns stock that cumulatively represents more than 50% of the voting power of each of the connected corporations” 2.2 or more corporations if the common owner directly or indirectly owns stock representing more than 50% of the voting power of the corporations or connected corporations. 3.Any 2 or more corporations if stock representing more than 50% of the voting power in each corporation are interests that cannot be separately transferred. 4.Any 2 or more corporations if the more than 50% ownership is through family attribution. <p>Wisc. Stat. § 71.255 (1)(n).</p>

C. Eligible Entities

	Conformity to Check the Box?	Entities Taxed Federally As C Corporations	S Corporations	Treatment of Partnership Income
VT	Yes	Yes	No	MTC
MA	Yes	Yes	Yes*	MTC*
NY	Yes*	Yes	Yes*	Includable, but varies from MTC
WI	Yes	Yes	No*	Similar to MTC

D. Water's Edge Group

VT	<p>Exclusion for “overseas business organizations” (“OBO’s”) Vermont OBO is defined as any “business organization that ordinarily has 80 percent or more of its payroll and property” outside the 50 states and D.C. 2 out of 3 years rule for 80 percent and 70 percent in current tax year</p>
MA	<p>Statute includes the following Water’s Edge Group members: (1) all members incorporated domestically; (2) any member (regardless of place of incorporation) if the average of its more payroll, property and sales in the U.S. is 20% or more; (3) any intangible property/service company that earns 20% or more of its income from intangible property or service-related activities, but only to the extent of the related income/factors;</p>
NY	<p>Alien corporations are excluded from the group, but no 80/20 type test</p>
WI	<p>If 80 percent or more of a corporation’s worldwide income is active foreign business income, as defined in IRC 861(c)(1)(B), the income and apportionment factors of the corporation shall not be included in the combined report, but the corporation shall compute and allocate or apportion its income from the unitary business separately.</p>

E. Consolidated Election

VT	<p>Confusing holdover—likely neutral effects</p> <p>Consolidated Election converted to consolidated member concept. Nexus-only, but subject to unitary requirements.</p> <p>Potential Defense to Non-Unitary Position</p>
MA*	<p>Apparent response to critics FIN 48 concerns.</p> <p>Affiliated group election available (on original return, binding for 10 years).</p> <p>Affiliated group defined with reference to IRC 1504 but subject to 50% common ownership test.</p> <p>Must include all commonly owned whether or not part of affiliated group</p> <p>Potential M&A issues to consider.</p> <p>One way to address lack of instant unity in combined filing.</p> <p>Objections as to inclusion waived.</p> <p>DOR directed to study revenue impact of affiliated group election and report to Legislature by March 15, 2013.</p>
NY	<p>No (except for corporate stockholders in tax-exempt DISC's)</p>
WI	<p>No</p>

* MA also has a worldwide election

F. Specialized Industries

	Included	Excluded
VT	Banks, insurance, telephone, railroad * Included in group but exempt from tax	Captive insurance companies Corporations not taxable under the IRC (remember importance of captives to VT)
MA	Financial, utilities, insurance companies not taxed as such for purposes of the IRC (e.g., captives), REITs, RICs	Securities corporations Insurance companies Corporations not taxable under the IRC
NY	Special apportionment industry entities not in group with entities with another apportionment method (but may be in their own combined report)	REIT's and RIC's, generally insurance companies and banking companies
WI	Domestic insurers, but alternative gross premiums method available	Corporations not taxable under the IRC Foreign insurers Life insurers

Other Key Combined Reporting Factors

1. Composition of the Group
2. Composition of the Tax Base
 - A. Computation of Unitary Income
 - B. Intercompany Eliminations
 - C. Taxation of Dividends Received from Non-Group Corporations
 - D. Net Operating Loss Treatment
 - E. Business / Nonbusiness Income Distinction?
 - F. Specialized Industries: Method of Inclusion of Income
 - G. Treatment of Partnership Income
3. Apportionment in the Unitary Group
 - A. Weighting of Factors
 - B. Sales Factor: Sales of TPP
 - C. Sales Factor: Throwback Rule
 - D. Sales Factor: Intangibles
 - E. Specialized Industries: Method of Apportionment
 - F. Treatment of Partnership Factors

Recent Wins/Losses: Noteworthy Unitary Cases

- Wal-Mart Stores East, Inc. v. Hinton, North Carolina Court of Appeals 08-450, May 19, 2009
 - Corporate Income Tax (NC) (separate company state)
 - Holding: Secretary of Revenue was authorized to combine the reports of Wal-Mart stores (Wal-Mart Stores) with that of Wal-Mart's REIT that owned the Wal-mart real property (Wal-Mart Real Estate and Wal-Mart Property Co.)
 - Tax benefits from structure:
 - Wal-Mart Store deducted rent paid to Wal-Mart Real Estate
 - Wal-Mart Store classified dividends from Property Co. as nonbusiness income
 - Wal-Mart Real Estate deducted dividends paid to Wal-Mart Property Co.

Recent Wins/Losses: Noteworthy Unitary Cases

- Wal-Mart Stores East, Inc. v. Hinton (*continued*)
 - Court concluded that forced combination statute was broad enough to allow secretary to require combined reporting if the corporation's returns do not disclose the true earnings of the corporation on its business in North Carolina.
 - Court found that combined reports properly revealed the true earnings of the taxpayer in North Carolina
 - Court rejected all federal and state constitutional arguments
 - Court rejected taxpayer's arguments that forced combination is not allowed if transactions are arm's length
 - Court held that no APA violation occurred
 - Significance:
 - Arm's length transactions not given deference
 - Published guidance on state interpretation not required

Recent Wins/Losses: Noteworthy Unitary Cases

- W.R. Grace & Co. v. Massachusetts Comm'r of Rev., Mass. Appellate Tax Board, No. C271787, April 6, 2009.
 - Corporate Income-Based Excise Tax (MA) (separate company state)
 - Parent (Grace)'s subsidiaries engaged in financing transaction to channel money to Grace to reduce its debt
 - Issue: whether dividend and interest income received by subsidiary (Ventures) as part of financing transaction was apportionable on Grace's MA combined return
 - Focus: whether Grace (parent chemical business) was engaged in a unitary business with subsidiaries (engaged in variety of businesses)
 - Grace: specialty chemical business
 - Cocoa Associates: cocoa manufacturing
 - Ventures: financing entity
 - NMC: home healthcare business

Recent Wins/Losses: Noteworthy Unitary Cases

- W.R. Grace & Co. (continued)
 - Non-Unitary Facts:
 - No meaningful intercompany activities
 - No regular intercompany services or shared functions
 - No joint officers / occasional oversight only
 - Holding: income not apportionable to MA
 - Income not derived from operational function (Allied-Signal, Mead)
 - Entities at issue not unitary (no functional integration, centralized management, or economies of scale)
 - Comm'r prohibited under Due Process Clause from assessing income because not rationally related to in-state activities of the recipient
 - Significance:
 - Intercompany financing transactions not necessarily apportionable
 - Distinguish mere stewardship function – not unitary

Combined Reporting: Impact on the ELFA Industry

- Assess the benefits in new combined reporting states
 - Bringing in NOLs
- Beware of the key factors
 - Composition of group, calculating base, and apportionment
- Examine the “same line of business” presumptions
 - MA and VT
 - Establishing unity more complex in ELFA industry
- Importance of documenting the unitary ties
- Increased compliance costs

III. Apportionment

A. Game Rules Changing?

NCCUSL Proposes Revision to UDITPA

B. A Shift in Strategy:

1. Intangible Income: shift to market-based sourcing
2. MeadWestvaco: Operational Income
3. In or Out?: The Status of the Throwout Rule
4. A New Player to Watch?: Polar Tankers

Game Rules Changing?: Proposed UDITPA Revision

- February 2008: National Conference of Commissioners on Uniform State Laws (NCCUSL) created drafting committee
- Impetus: Section 17 – receipts from sales of services and intangibles in the sale factor
 - Current: income-producing activity
 - MTC advocates destination based / market approach
- COST / Industry objections / participation
- May 2009: recommendation to extend group decision to revise UDITPA to January 2010

Intangible-Based Income: Shift to Market-Based Sourcing

- States move to market-based sourcing
 - Cost of performance debate
 - What is the “use” of an intangible?
 - Recent changes to market-based sourcing
- Case Update
 - AT&T vs. Illinois Department of Revenue, Illinois Circuit Court (pending)
 - Calculating COP for telecommunications services
 - Interface Group v. Comm’r of Revenue, Mass. ATB (Oct. 17, 2008)
 - All or nothing rule
 - Ameritech Publishing, Inc. v. Wisconsin Dept. of Revenue, Wisconsin Tax App. Comm. (2008)
 - IPA performed in WI based upon finding that the service of advertising was provided when the customers received the telephone directories

MeadWestvaco: Operational Income

- MeadWestvaco v. Illinois Department of Revenue, 128 S.Ct. 1498 (April 15, 2008), vacated and remanded to Appellate Court.
 - Corporate Income Tax (IL)
 - Holding: Illinois could not tax capital gain realized by Mead (Ohio corporation) from the sale of its LexisNexis business division.
 - Clarified limitations on state taxing authority under the commerce and due process clauses of the U.S. Constitution regarding the unitary business principle
 - Defined the role the operational function test plays under the unitary business principle
 - Unanswered questions: no state court has applied the test
- Gannett Satellite Information Network v. Montana, 348 Mont. 333 (Mont. Jan. 13, 2009)
 - Corporate License Tax (MT)
 - Holding: IRC 338(h)(10) gain apportionable business income
 - Statutory definition of business income includes both a transaction test and functional test
 - Court looked to UDITPA

In or Out?: The Status of the Throwout Rule

- NJ adopted the “throwout” rule in 2002
 - Receipts that are not “subject to a tax on or measured by profits or income or business presence or business activity” in another jurisdiction are excluded from the denominator of the NJ sales factor. (N.J. Stat. Ann. 54:10A-6; N.J. Admin Code tit., 18, 7-8.7)
 - Increases NJ factors
 - Potential double counting since same receipts can be thrown back in other states
- May 29, 2008: NJ Tax Court denied Pfizer and others claims that NJ throwout rule is facially unconstitutional
- Case continues, including appeals and “as applied” challenges
- December 19, 2008: NJ repealed throwout rule with Governor’s signature effective for tax years beginning after June 30, 2010
- Tax years 2002-2010 all subject to throwout

The New Player to Watch?: Polar Tankers

- Polar Tankers, Inc. v. City of Valdez, 182 P. 3d 614 (Alaska 2008), cert. granted, 129 S. Ct. 762 (Dec. 12, 2008)
 - City property tax on certain vessels (Valdez, Alaska)
 - Issue: whether the city property tax violates the U.S. Constitution's prohibition on duties of tonnage; and whether the tax's apportionment formula (which divides days at the Alaska port by days in all other ports) is unconstitutional because it improperly attributes a portion of days spent on the high seas to the city.
 - Alaska Supreme Court Holding: for the city
 - Status: oral arguments held on April 20, 2009

IV. Other Noteworthy Highlights

- A. Bonus Depreciation
- B. ELFA Cases
- C. Tax Attributes: NOLs
- D. Intangible Add-Back Provisions

Bonus Depreciation: Federal Overview

- Pre-2008 Act Depreciation Rules
 - Job Creation and Worker Assistance Act of 2002: allowed a 30% bonus depreciation deduction in the first year for qualifying property purchased after 9/10/01 and before 9/11/04 (IRC 168(k))
 - Jobs and Growth Tax Relief Reconciliation Act of 2003: increased the bonus depreciation deduction from 30% to 50% for assets purchased after 5/2/03 but placed in service before 1/1/05
 - American Jobs Creation Act of 2004: extended the placed in service date to 1/1/06 for certain property, and extended bonus depreciation to noncommercial aircraft, and shortened recovery periods for qualified leasehold improvements and restaurant property

Bonus Depreciation: Federal Overview

- Federal 2008 Economic Stimulus Act
 - H.R. 5140, P.L. 110-185, amending IRC 168(k)
 - Allows a qualifying taxpayer a 50% first-year bonus depreciation of the adjusted basis of qualifying property placed in service after 12/31/07 and before 1/1/09.
- American Recovery and Reinvestment Act of 2009
 - H.R. 1, P.L. 111-5, amending IRC 168(k)
 - Extends the temporary bonus depreciation provision of the 2008 Act to qualifying property purchased and placed into service before 1/1/10.
 - Signed into law February 17, 2009

Bonus Depreciation: State Conformity - Overview

- 2001 – 2004 Economic Downturn: Approximately 30 states disallowed all or part of the favorable bonus depreciation
 - Effect of Federal Acts on State Corporate Tax Revenues:
 - 2002 Act: \$14.7 B
 - 2003 Act: \$16 B (over 10 years)
 - 2004 Act: \$2.2-3.5 B
- (Univ. of Tenn, NTA, 2007)*
- Effect of 2009 Act on State Corporate Tax Revenues:
 - Kansas April 2009 estimates: \$45 MM loss in CIT receipts
 - Nebraska estimates (state general fund revenue loss): FY09 - \$2.02 million, FY10 -\$20.45 million, FY11 -\$33.24 million
 - Oklahoma estimates: \$46 MM decline in state revenues for FY10

Bonus Depreciation: State Conformity Chart

	State Conformity to 2008 Act	State Conformity to 2009 Act
Conforming States	AK,CO,DE,ID,KS,LA, MO,MT,NE,NM,ND, OH,OR,UT,WV	AK,CO,DE,FL,ID,IA, KS,LA,MO,MT,NE, NM, ND,OK,UT,WV
Non-Conforming States	AL,AZ,AR,CA,CT,DC, FL,GA,HA,IL,IN,IA,KY, ME,MD,MA,MI,MN, MS,NJ,NY,NC,OK,PA, RI,SC,TN,TX,VT,VA,W I	AL,AZ,AR,CA,CT,DC, GA,HA,IL,IN,KY,ME, MD,MA,MI,MN, MS,NJ,NY,NC,OH, OR,PA,RI,SC,TN,TX, VT,VA,WI

Bonus Depreciation: 2008 and 2009 Issues

- Disparity in federal conformity provisions comes into play
 - Conformity to 2009 Act still undecided
 - Strategic lobbying issues
- Non-Conforming states that provide partial subtraction modifications:
 - FL: 1/7 modification for 7 years
 - MN: modification over 5 years
 - NC: 20% of addition modification for 2008 for 5 years
 - OK: 25% of addition modification for 2008 for 4 years
- Non-Conforming states that have partial conformity:
 - MN: add back of 80% federal bonus depreciation
 - OK: add back of 80% of 2008 Act depreciation

Bonus Depreciation: 2009 State Watch

- AZ SB 1185 (enacted 4/9/09): conforms to IRC as of 1/1/09
- FL SB 1112 (signed into law 3/17/09): decouples from 2008 Act
- FL SB 2504 (passed Senate): would decouple from 2009 Act
- GA HB 74 (enacted 4/8/09): conforms to IRC as of 1/1/09 but not giving effect to IRC 168(k)
- MD HB 669 (introduced): allows bonus depreciation provided under IRC 168(k) eff. 7/1/09 and applies to property placed in service after 12/31/08
- MN HF 1298 (approved by leg): conforms to IRC as of 3/31/09, thereby adopting 2009 Act
- MO SB 241 (introduced): would reinstate decoupling
- OR HB 2157 (enacted Feb. 2009): decoupled from current IRC; ties into IRC as of 12/31/08
- Other States to Watch (KS, OK, IA): decoupling legislation expected or being discussed due to recent revenue estimates

State ELFA Cases

In the Matter of the Petition of BTMU Leasing & Finance, Inc., N.Y. Div. of Tax Appeals, DTA No. 821525 (Nov. 26, 2008)

- Corporate Franchise (Income) Tax (NY)
- Facts:
 - Finance company was headquartered in NY
 - Equipment was located outside of NY
 - Lessees took possession of equipment outside of NY
- Department: proceeds from sales should be allocated based upon where the work earning such receipts was performed, 100% to NY, under SINAA rules applicable to income from loans and financing leases
- Holding: BTMU's proceeds from end-of-lease sales of leased equipment located outside the state should be allocated to the situs of the property and not where the proceeds are earned

State ELF Cases

Christopher M. Watts, et al., v. Arizona State Department of Revenue, Superior Court of Arizona (Jan. 16, 2008)

- Income Tax (AZ)
- Issue: whether individual engaging in business of leasing construction equipment to reduce dust pollution was entitled to pollution control credit
- Held: taxpayer/lessor was not entitled to credit for assisting others to abate their pollution
 - Statutory construction basis

NOLs:

Recent Noteworthy Cases

- Golden West Financial Corp. et al., v. Dept. of Revenue, Florida Dist. Court of Appeal, No. 1D07-0135 (Feb. 19, 2008)
 - Corporate Income Tax (FL)
 - Facts: Golden West filed refund claims applying that NOLs sustained by FL affiliates should be applied to the group's consolidated returns
 - Holding: The state separate return limitation rule (SRYL) was invalid because it enlarged, modified or contravened the specific laws implemented by the rule
- Colgate-Palmolive Company v. Florida Department of Revenue, Florida District Court of Appeal, No. 1D07-1051 (June 2, 2008)
 - Corporate Income Tax (FL)
 - Holding: the state's limitation of NOL carryovers to federal net losses does not violate the Commerce Clause because corporations may subtract all foreign-source dividends from their income calculation and offset state taxes with foreign tax credits

NOLs: Legislative Developments

- California
 - Laws 2008, A.B. 1452: CA NOLs suspended for tax years beginning 1/1/08 through 12/31/09 (certain exceptions for small taxpayers)
- Vermont
 - 2006: computation of Line 30 NOL in 1st year of combined filing
 - 2007: conversion of federal NOL into state-level NOL
- Massachusetts
 - 2009: computation of NOLs coming into 1st year combined filing
- Georgia
 - Laws 2009, H.B. 74: updated IRC conformity to changes made after 2007 and before 1/1/09 with the exception of changes to IRC 168 and 172
- Maine
 - Laws 2009, L.D. 2289, L.D. 2305: limitations on recapture of disallowed federal carryback NOL deductions (effective 7/1/08) and other modifications (eff. 2008)

NOLs:

Legislative Developments (cont.)

- Utah
 - Laws 2009, S.B. 136: limitation on NOL deduction against separate income of entity acquired by a unitary group
- New Jersey
 - Laws 2009, S. 2130: extension of carryforward from 7 to 20 years (eff. for losses incurred after June 2009)

Intangible Expense Add-Backs

- V.F.J Ventures, Inc. v. Surtees, 2008 Ala LEXIS 197 (Ala. Sept. 19, 2008), cert. denied, Apr. 27, 2009.
 - Corporate Income Tax (AL)
 - AL DOR: imposed add-back statute to include royalty payments to affiliates in the tax base
 - VFJ: argued that royalty payments met the “unreasonable” and “subject to tax” exceptions and that imposition of statute violated the Commerce Clause
 - Alabama Supreme Court: upheld the DOR’s add-back because VFJ did not meet either exception:
 - VJF did not meet “unreasonable” exception: resulting tax was not out of proportion to instate activities
 - VJF did not meet “subject to tax” exception
 - No constitutional violation
 - U.S. Supreme Court denied certiorari
 - Add-back exceptions in the 20+ states remain open to interpretation

V. Post-Game Show

- I. The Economy
- II. The Impact of the Economy on Income Tax
 - A. Nexus
 - B. Combined Reporting
 - C. Apportionment
 - D. Other Noteworthy Highlights
- III. What to Expect Next Season