



SALT Alert! 2023–03: Significant State and Local Tax Changes Affecting the 2022 Filing and Payments Obligations of Entities in the Asset Management Industry

Changes to state and local laws, as well as court decisions and state administrative actions, can have a significant impact on an entity's filing and payment obligations. The tables below set forth significant state and local tax developments that may affect return and/or payment obligations of companies engaged in the asset management industry for tax years beginning in 2022. Note that this is not an exhaustive list of all state and local developments, but includes items most likely to affect these taxpayers. The last table provides a list of states that have enacted a passthrough entity tax as a workaround for the federal SALT cap on taxes that may be deducted as an itemized deduction. For information on how these and other developments may impact your specific tax situation, please contact your KPMG State and Local Tax specialist.

Allocation and apportionment

CA California Franchise Tax Board (FTB) issued a new ruling that provides guidance on how to use the “cascading rules” of regulation 25136-2(c). The ruling retroactively revoked Chief Counsel Ruling (CCR) 2015-03 and CCR 2017-01, which used the “direct” customer/purchaser approach to sourcing nonmarketing services.

[Legal ruling 2022-01](#)

CA California Court of Appeal concluded that nonresident trust shareholders must apportion gain from an S corporation's sale of goodwill. The S corporation, Pabst Corporate Holdings, Inc., sold its interest in a wholly owned subsidiary, reporting the gain as apportionable business income. The trusts initially apportioned their pro-rata share of the gain to California using Pabst's apportionment factors. Later, the trusts filed for a refund, claiming the gain was from the sale of an intangible (goodwill) and is not apportionable income unless the property sold has a business situs in California. The court noted that IRC section 1366(b) provides that the character of any item of income is determined at the S corporation level. Therefore, court concluded that the income from the sale of the stock was corporation income derived from corporate activities and passed through to the shareholders.

[Metropoulos Family Trusts v. FTB](#)

- FL Florida Department of Revenue (DOR) issued guidance regarding sourcing of sales from asset management services globally to pension funds, large institutions, and individuals. The DOR found that the activities of the taxpayer corporation are those of a financial organization and thus, the corporation should source its income from asset management services to the location of the customer. [Florida TAA 21C1-010](#)
- ID Idaho legislation adopted market-based sourcing for sales other than sales of tangible personal property, sourcing sales of services to the location where the service is delivered. Previously, the statute used the greater cost of performance approach. The change is effective January 1, 2022. [Idaho House Bill 563](#)
- IL Illinois DOR permitted an LLC to apportion income received from the sale of the rights to future contingent payments using an alternative apportionment method. Taxpayer sold all the rights for biopharmaceutical products, equipment, and machinery to manufacture the product to a third party for cash plus contingent payments based on the buyer's net sales and certain milestones. Taxpayer first sold the rights to the contingent payments, and received permission to use alternative apportionment for that sale. In a later year, taxpayer sold the rights to the contingent payments that were based on milestones. Taxpayer requested to use the same alternative apportionment method as permitted in the previous request. In the year at issue, Taxpayer's only income was from portfolio interest and the sale of the future contingent payments. As a result, the only amounts included in the apportionment formula would be the Taxpayer's portfolio interest income, which would result in 100 percent of all income sourced to Illinois. Taxpayer argued this sourcing would not fairly represent income attributable to the sale of the milestone payments. The DOR agreed and allowed the taxpayer to use the terms of the 2019 PLR to apportion income. [Illinois PLR IT-22-003](#)
- MA Massachusetts Supreme Judicial Court concluded that the Commonwealth's tax statutes did not authorize taxation of the capital gain from the sale of an interest in another business when the in-state business and the out-of-state owner are not in a unitary relationship. Nevertheless, the court noted that such taxation would be permitted under the Constitution. [VAS Holdings & Investments LLC v. Commissioner of Revenue](#)
- MT Montana Tax Appeal Board (Board) determined an S corporation can apportion unitary business income from its Montana subsidiary. The Board determined that the unitary business principle applies to businesses other than C corporations under Montana law and thus, the S corporation was entitled to apportion its multistate unitary business income from its subsidiaries. [Pioneer News Group v. Montana](#)

- NY New York appellate court affirmed that the broker-dealer sourcing rules do not extend to receipts of the disregarded SMLLC's parent. Accordingly, the corporate owner's receipts could not be sourced using the broker-dealer rules because the corporate legal entity was not itself a registered securities broker-dealer. [Matter of BTG Pactual NY Corp.](#)
- OH Ohio legislation revised "business income" to include gain from the sale of a business ownership interest if the sale is treated as a sale of assets or the seller materially participates in the business activities. The statute indicates this is intended as a "remedial measure intended to clarify existing law." As such, the change applies to any transactions that occur or have occurred in any year not closed by the statute of limitations. [Ohio House Bill 515](#)
- TX Texas Court of Appeals concluded that net proceeds, not gross receipts, from the sale of non-inventory securities are included in a corporation's apportionment denominator. Conagra Brands Inc. (Conagra), a packaged food company, bought and sold commodity futures contracts and options on commodity futures contracts to mitigate price fluctuation for raw materials. Conagra argued that gross receipts, rather than net proceeds, from the sales of its hedging contracts should be included in the sales factor. Conagra asserted that, under the Corn Products doctrine, its securities "are, in substance, inventory" because the commodity hedges were used to maintain costs of the raw materials that were used to manufacture final products. The court disagreed and pointed to the undisputed findings that the securities were not "merchandise, stock in trade, raw materials, works in process, finished products, or supplies that are physically a part of the food products Conagra sold to its customers." [Conagra Brands Inc. v. Comptroller of The State of Texas](#)

Composite returns

- CT Connecticut House Bill 5473 provides an election for an affected business entity (ABE) to file a composite income tax return on behalf nonresident individual members. If the nonresident individual member's only Connecticut source income is from one or more ABEs that each elect to file a composite income tax return, then the member's state filing and payment obligations are satisfied. The law became effective May 27, 2022. [Connecticut House Bill 5473](#)

- IA Iowa allows composite returns for 2022 tax years. The state released guidance on the new law including: definitions for “pass-through entity” and “nonresident member,” requirements and exemptions, electing out of the composite requirement, and credits for Iowa tax paid by the PTE. The new law is effective for tax years beginning on or after January 1, 2022. [Iowa Composite Returns for Tax Year 2022](#)
- NM New Mexico allows a pass-through entity to file a composite return on behalf of electing nonresident members for 2022 tax years. The law became effective January 1, 2022. [New Mexico Senate Bill 410](#)

Nexus

- CO Colorado advised that the corporation nexus standards also apply to partnerships. The sales factor threshold for a partnership rendering management, distribution, or administration services to a registered investment company is \$500,000 or 25% of total sales sourced to Colorado. [Colorado GIL-21-004.pdf \(colorado.gov\)](#)
- MI Michigan Tax Tribunal determined that a non-resident holding company lacked nexus with Detroit and was not subject to city income tax. As a holding company, the taxpayer had no activities in Detroit (or elsewhere), although the annual report filed with Delaware listed the taxpayer’s primary address as being in Detroit and a shareholder accepted mail on the taxpayer’s behalf at that address. Because the City regulation exempts the agent’s activities from the definition of “doing business,” the Tribunal determined that the activities of the taxpayer’s shareholder are not taken into account in determining if the taxpayer has nexus in Detroit. The Tribunal rejected the state’s argument that the taxpayer’s “commercial domicile” was in Detroit, noting that the term “commercial domicile” was not used in the City Income Tax Act. [Apex Laboratories International, Inc. v. City of Detroit](#)
- NY New York adjusted the state’s factor presence nexus thresholds to \$1,138,000 for tax years beginning or after January 1, 2022, and before January 1, 2023. These thresholds apply to the state Article 9-A franchise tax and MTA surcharge. See NYS TSB-M-21(3)C for more details. [New York TSB-M-21\(3\)C](#)

Tax Base and Modifications

- AZ Arizona House Bill 2204 creates individual income tax subtractions from Arizona gross income for the value of virtual currency and non-fungible tokens (NFTs) received in airdrops. “Airdrop” means the receipt of virtual currency through a distribution of virtual currency to the distributed ledger addresses of multiple taxpayers. In addition, if a taxpayer includes a gain or loss on the sale of virtual currency or a NFT in Arizona gross income, the taxpayer may deduct any gas fees paid on the purchase of the virtual currency or an NFT. A gas fee is defined as a fee paid to the operator of a virtual network for the use of the network to facilitate the purchase, sale, or exchange of virtual currency or NFTs. The new law is effective on and after December 31, 2022. [Arizona House Bill 2204](#)
- CA California Office of Tax Appeals (OTA) upheld acceleration of contingent installment sale gain and exclusion of gross receipts from the sales factor. The FTB asserted that gain attributable to the future installment payments should have been accelerated and included in taxable income in the year of the sale. The OTA agreed, concluding that the amount to be included was equal to the fair market value of the contingent fees contract less the basis of the installment obligation and that the taxpayer had the burden of proving that the fair market value was less than the face amount of the obligation. [Matter of Appeal of Amarr](#)
- CA California OTA determined that a taxpayer should have reported capital loss related to the liquidation of an LLC in the year the LLC was terminated, not the year its assets were sold. An LLC sold all its assets in 2012 and entered into a settlement agreement in 2013 to distribute funds from the sale to the taxpayer and other members and to wind up and dissolve the entity as soon as possible. The OTA dismissed the taxpayer’s argument that the LLC’s sale of the property triggered a “constructive final liquidating distribution” under IRC § 708(b)(1)(A) (in effect during the tax year at issue). The OTA determined that controlling case law states a partnership continues to exist until wound up in accordance with the partnership agreement and that holding money in a bank account is sufficient nominal activity to prevent termination. [Matter of the Appeal of Rios](#)
- MI Michigan Department of Treasury advised that transactions involving digital currencies that are treated like transactions involving property or financial assets for federal purposes are treated similarly for Michigan purposes. [Mich. Treasury Update August 2022](#)

- NJ New Jersey Taxation Division affirmed the applicability of the federal “at-risk” limitation rules to a noncorporate partner, reversing a Tax Court decision that had denied a taxpayer’s loss from a partnership that was not claimed in the prior year due to the IRC § 465 “at-risk” limitation rules. The Division subsequently acquiesced to the determination that the federal “at-risk” rules apply to taxpayers who are partners in partnerships or sole proprietorships but stated that they do not apply to S corporation shareholders because there is specific statutory language in the New Jersey statute that limits shareholders’ losses. [Shechtel v. Director, Division of Taxation \(32 N.J. Tax 180 2020\) \(nj.gov\)](#)
- NJ New Jersey issued guidance addressing the state’s income and sales tax treatment of transactions involving convertible virtual currency. For Corporation Business Tax and Gross Income Tax purposes, New Jersey fully conforms to the federal tax treatment of virtual currency. Companies that sell virtual currency to customers in New Jersey are not protected by Public Law 86-272 because virtual currency is intangible property. [N.J. TAM 2015-1\(R\)](#)
- PA Pennsylvania court affirmed that gains from like-kind exchanges are taxed when property is exchanged rather than when acquired property is sold. In three recent cases, taxpayers asserted that the Pennsylvania rules allow them to use the Federal Income Tax (FIT) method of accounting, which permits deferral of gains from like-kind exchanges under IRC § 1031. However, the court refused to adopt this position, noting that the PIT regulations clearly state that “gain on the disposition of property is recognized in the taxable year in which the amount realized from the conversion of property into cash or other property exceeds the adjusted basis of property.” [Pealstein v. Commonwealth](#)
- WI Wisconsin updated its guidance on the deferral and exclusion of long-term capital gain for investments in qualified Wisconsin businesses. Both the deferral and exclusion are available only to individuals, including individual partners or members of a partnership, limited liability company, or limited liability partnership, and shareholders of a tax-option corporation. [Wisconsin Fact Sheet 1102-2](#)

Tax Rates

- CO Colorado approved a reduction in state income tax rates for individuals and corporations. Specifically, Proposition 121 reduced the state’s current 4.55 percent corporate and personal income tax rate to 4.40 percent. The change is effective tax years beginning on or after January 1, 2022. [Proposition 121](#)

MA Massachusetts voters approved the millionaire tax, which increases the state's flat individual income tax rate from 5 percent to 9 percent on income above \$1 million. The tax rate increase is effective for taxable years beginning on or after January 1, 2023.

[Question 1](#)

MO Missouri Governor approved Senate Bills Nos. 3 & 5 that reduce the state's personal income tax rates. For tax years beginning on or after January 1, 2023, the top tax rate is reduced to 4.95 percent (previously 5.2 percent). Additional rate reductions may occur in later year if certain collection thresholds are met.

[Missouri Senate Bills Nos. 3 & 5](#)

WA Washington DOR issued guidance explaining the qualifications for the preferential B&O tax rate applicable to an international investment management services (IIMS) provider. A person is engaged in providing qualified IIMS if the following conditions are met:

[Washington Excise Tax Advisory 3183.2022](#)

1. The person is engaged primarily in the business of providing international investment management services;
2. At least 10% of the person's gross income is derived from providing international investment management services to a qualifying collective investment fund (CIF);
3. More than 25% of the person's employees are in Washington; and
4. The taxpayer is a member of an affiliated group that collectively has at least ten offices in eight foreign countries and 500 full-time employees worldwide; > \$400 million worldwide gross revenue; and > \$200 billion average assets under management.

Withholding/Estimated Payments

NY The New York Department of Taxation and Finance advised KPMG that nonresident partners must file an individual personal income tax return in order to claim the PTET credit. An individual can be included in a group filing or they may file an individual income tax return, but they cannot file both for the same tax year. If any nonresident partners choose to be removed from a group return and file individual personal income tax returns, the entity must submit a written request to transfer the payment or payments to the individuals' estimated personal income tax accounts as explained in the Estimated income tax payments section of Form IT-203-GR-I.

N/A

- VA Virginia issued a ruling stating that withholding may be required on an interest held by a nonresident's IRA if the income was UBTI. The PTE in this ruling had Virginia source income from the sale of rental real estate. If the capital gains realized were from the sale of real estate financed by debt, the IRA also may have unrelated debt financed income subject to withholding. [Virginia Tax Commissioner Ruling 22-118](#)
- WI Wisconsin Tax Appeals Commission determined that withholding is required if a passthrough owner has at least \$1000 in passthrough "income," not "taxable income" and that Wisconsin returns must be filed to establish net business loss carryforwards. The Commission rejected the PTE's argument that it was not required to withhold any tax because each of the partners could apply losses from prior years to net Wisconsin taxable income to zero. [RADS Partnership](#)
- WI Wisconsin Tax Appeals Commission affirmed that a nonresident S corporation licensing software and providing maintenance for the software to Wisconsin customers was subject to withholding tax. The taxpayer argued that it was protected by Public Law 86-272 and that withholding was essentially an income tax. However, the Commission concluded that the issue of whether the withholding was essentially an income tax was "not ripe for appeal." [MacKinney Systems](#)

Other

- CA FTB will require partnerships and LLCs to report its partners' or members' capital accounts on the Schedule K-1 (565/568) using the tax basis method under California law, beginning with tax year 2023 (previously tax year 2022, based on superseded FTB Notice 2022-01). [FTB Notice 2023-01 \(ca.gov\)](#)
- CA California FTB advised KPMG that the \$800 annual tax applicable to limited partnerships and limited liability companies taxed as partnerships is not deductible for California tax purposes per CRTS § 17220(c). N/A
- CA California appellate court affirmed the definition of "realty sold" under San Francisco Transfer Tax Ordinance includes interests indirectly owned and that termination of a partnership triggered the transfer tax. Court declined to adopt the taxpayer's position that the Ordinance's definition of "realty sold" limited the imposition of transfer taxes to real property directly owned by the entity whose ownership interests were transferred. [CIM Urban REIT 211 Main Street \(SF\) LP v. City and County of San Francisco](#)

Passthrough Entity Taxes

| State | Effective | State | Effective |
|-------|-----------|-------|-----------|
|-------|-----------|-------|-----------|

| | tax year | | | tax year |
|----------------------------|----------|--|----------------|---------------------------------|
| Alabama | 2021 | | Missouri | 2022 |
| Arkansas | 2022 | | Mississippi | 2022 |
| Arizona | 2022 | | North Carolina | 2022 |
| California | 2021 | | New Jersey | 2020 |
| Colorado | 2018 | | New Mexico | 2022 |
| Connecticut (Mandatory) | 2018 | | New York State | 2021 |
| Georgia | 2022 | | New York City | 2022 |
| Idaho | 2021 | | Ohio | 2022 |
| Illinois | 2021 | | Oklahoma | 2019 |
| Kansas | 2022 | | Oregon | 2022 |
| Louisiana | 2019 | | Rhode Island | 2019 |
| Massachusetts | 2021 | | South Carolina | 2021 |
| Maryland | 2020 | | Utah | 2022 |
| Michigan | 2021 | | Virginia | 2021 |
| Minnesota | 2021 | | Wisconsin | 2018 (S corp), 2019 (P'ship) |

Contacts

Chris Bajec

Ft. Worth

T: 817-335-2655

[E: cbajec@kpmg.com](mailto:cbajec@kpmg.com)

George Burns

Boston

T: 617-988-6759

[E: gburns@kpmg.com](mailto:gburns@kpmg.com)

Abner Chong

Los Angeles

T: 213-593-6618

[E: ajchong@kpmg.com](mailto:ajchong@kpmg.com)

Mike Deal

Chicago

T: 312-665-1798

[E: mdeal@kpmg.com](mailto:mdeal@kpmg.com)

Julia Flanagan

New York

T: 212-954-8139

[E: juliaflanagan@kpmg.com](mailto:juliaflanagan@kpmg.com)

Chris Hoge

San Francisco

T: 415-963-8241

[E: whoge@kpmg.com](mailto:whoge@kpmg.com)

Nick Pamos

Dallas

T: 214-840-4076

[E: npamos@kpmg.com](mailto:npamos@kpmg.com)

Jennifer Petersen

San Francisco

T: 415-963-8241

[E: japetersen@kpmg.com](mailto:japetersen@kpmg.com)

Scott Salmon

Washington National Tax

T: 202-533-4202

[E: ssalmon@kpmg.com](mailto:ssalmon@kpmg.com)

John Skei

New York

T: 212-872-3610

[E: jskei@kpmg.com](mailto:jskei@kpmg.com)

© 2023 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. NDP392139-3E

© 2023 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. NDP333483-1H

The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organization.