AUGUST 2026

THE BR STATE + LOCAL TAX SPOTLIGHT

BLANKROME

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Notes from the Editors

By Joshua M. Sivin and Melanie L. Lee

Welcome to the August 2026 edition of *The BR State + Local Tax Spotlight*. We know the importance of remaining up-to-date on State + Local Tax developments, which appear often and across numerous jurisdictions. Staying informed of significant developments and decisions helps tax departments function more efficiently, along with improving strategy as well as planning. That is where *The BR State + Local Tax Spotlight* can help. In each edition, we will highlight important State + Local Tax developments that could impact your business. In this issue, we will be covering:

- Indiana Department Rules Cloud-Based Services Not Subject to Sales Tax
- Nebraska District Court Holds That the State Must Devise an Equitable Apportionment Formula for Apple's One-Time TCJA Transition Tax Income
- Stopping the P.L. 86-272 Evasion
- Processing Power: Maryland's Highest Court Rules Utility Equipment Qualifies for Sales Tax Exemption

We invite you to share *The BR State + Local Tax Spotlight* with your colleagues and visit Blank Rome's State + Local Tax webpage for more information about our team. Click here to add State + Local Tax to your subscription preferences.

Updates from previous editions. The July 2025 edition of *The BR State + Local Tax Spotlight* includes an article titled "Streaming into Taxable Territory: Colorado Court Rules Netflix Subscriptions Are Tangible Personal Property" that discusses the Colorado Court of Appeals decision in *Netflix, Inc. v. Colo. Dep't of Revenue*. Netflix appealed the Court's decision to the Colorado Supreme Court. On July 22, 2026, the State Supreme Court dismissed the case with prejudice after the parties entered a joint stipulation that affirmed the department of revenue's position that streaming services are subject to sales tax.

In the July 2026 edition of *The BR State + Local Tax Spotlight*, Irwin M. Slomka authored an article titled "New York Appellate Court Upholds Application of "Convenience of Employer" Rule Against Connecticut Law Professor," in which he discussed the New York Appellate Division's decision in *Matter of Zelinsky v. Tax Appeals Tribunal*. On July 20, 2026, Professor Zelinsky appealed the Appellate Division's decision to the New York Court of Appeals.

Co-Editors, *The BR State + Local Tax Spotlight*

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CRAIG B. FIELDS

PARTNER

Indiana Department Rules Cloud-Based Services Not Subject to Sales Tax

By Craig B. Fields

The Indiana Department of Revenue determined that a company's charges for accessing its cloud-based educational services through a web-based platform with optional downloaded software are not subject to sales tax. Ind. Rev. Rul. # 2026-04-RST (June 26, 2026). This ruling should assist other companies that provide similar services.

The Facts: The company provides educational and training services that offer customers an opportunity to test and develop their trading and risk management skills. The company's primary product is designed to teach users how to become successful traders in a simulated environment. The services are provided through a secure digital platform that offers various statistical and analytical capabilities, a simulated trading environment, and educational content accessible via any web browser.

Users primarily access the platform through the company's website. However, the company also provides users with the option to download a simulation-only application component (trading platform) for use in place of the web-based application. The downloaded trading platform is developed by an unrelated third-party and offered as a freeware application.

The Sales Tax: Sales tax is imposed on sales of tangible personal property, specifically enumerated services, and specified digital goods. Prewritten computer software is included in the definition of tangible personal property. IC 6-2.5-1-27. However, charges for accessing prewritten computer software electronically via the internet where no permanent ownership interest, control, or possession in the software is acquired are not subject to sales tax. IC 6-2.5-4-16.7.

Specified digital products are defined as electronically transferred digital audio works, digital audiovisual works, or digital books. IC 6-2.5-1-26.5. A person is considered to be engaged in making a retail transaction with respect to specified digital products only when the person (1) electronically transfers specified digital products to an end user and (2) grants the end user the right of permanent use of specified digital products that is not conditioned upon continued payment by the purchaser. IC 6-2.5-4-16.4(b).

The Ruling: The Department determined that the company's product does not meet the definition of a specified digital product as it does not meet the definition of a digital book, digital audio work, or digital audiovisual work, and customers do not obtain the right of permanent use of the product. Instead, the company's product allows customers to gain access to software that is accessed over the internet.

The option to download the third-party software also does not make the company's product downloadable software. As the Department found, "[t]he optional software that can be downloaded is not necessary to utilize the company's product and does not add additional functionality, which is the object of the transaction to purchase the product."

The Department concluded that the company is providing financial trading educational services. The company uses software in the performance of its services, which is electronically accessed by its customers who have no permanent ownership of the software and, as such, the accessed software is not subject to sales tax.

> **This ruling should help other companies since, as the ruling provides, "other taxpayers with substantially identical factual situations may rely on this ruling for informational purposes in preparing returns and making tax decisions."**

JOSHUA M. SIVIN
OF COUNSEL

Nebraska District Court Holds That the State Must Devise an Equitable Apportionment Formula for Apple's One-Time TCJA Transition Tax Income

By Joshua M. Sivin

In *Apple Inc. and U.S. Subsidiaries v. Nebraska Department of Revenue*, Case No. CI 24-4186 (Lancaster Cnty. Dist. Ct., July 13, 2026), a Nebraska district court reversed the Tax Commissioner's order, finding that the Department's apportionment formula did not fairly represent the Nebraska taxable income of the taxpayer, Apple Inc. ("Apple"), and remanded the case with instructions for the Commissioner to develop an equitable alternative. This is a significant victory for Apple and a reminder that a well-supported challenge to an inequitable apportionment methodology can succeed.

The Facts: By way of background, the 2017 Tax Cuts and Jobs Act ("TCJA") imposed a one-time "transition tax" under Section 965 of the Internal Revenue Code. The transition tax required U.S. shareholders of controlled foreign corporations ("CFCs") to include in income their share of the CFCs' accumulated post-1986 deferred foreign earnings. In effect, this was a deemed repatriation of up to 13 years of previously untaxed offshore profits, all recognized at once in a single tax year.

Apple, headquartered in California with subsidiaries in over 50 countries, earns more revenue abroad than domestically and maintains a small business presence in Nebraska (one retail store with few employees). On its 2017 Nebraska return, Apple reported a sales factor of 0.1269% and did not include Section 965 income. The Nebraska Department of Revenue ("NDOR") adjusted the return, disallowing approximately $281.7 billion in dividends-received deductions, roughly tripling Apple's Nebraska tax liability from about $1.5 million to over $5.3 million. Apple protested and, after an unsuccessful administrative hearing, sought judicial review.

The Law: Nebraska uses a single-sales-factor apportionment formula. Adjusted federal taxable income is multiplied by a fraction whose numerator is Nebraska sales and whose denominator is total sales everywhere, measured during the tax period. Neb. Rev. Stat. §§ 77-2734.05(1), 77-2734.14(1). CFC gross receipts are excluded from this fraction under Nebraska's standard apportionment statutes.

Nebraska also includes an alternative apportionment statute that can override the standard formula in certain circumstances. If the standard formula "does not fairly represent the taxable income that is reasonably attributable to the business operations conducted within this state," the Commissioner or the taxpayer may use "any other method to effectuate an equitable apportionment." The statute is meant for "unique and nonrecurring factual situations" that would otherwise produce "incongruous results."

The Decision: The Court agreed that the TCJA's one-time transition tax was the exact sort of "unique and nonrecurring" situation that triggers alternative apportionment. Once Section 965 income entered Apple's tax base, the standard, single-year sales factor could no longer fairly represent the income attributable to Apple's Nebraska operations.

The Court found that both parties' proposed alternative formulas shared a basic flaw, which the Court called a "temporal mismatch." Each formula paired a numerator and denominator confined to a single tax year, 2017, with a foreign addition reflecting 13 years of accumulated CFC activity, from 2005 through 2017. In the Court's words, "[a]ny method that introduces multi-period amounts into only one component of the fraction, while confining every other component to a single year, does not compare like with like."

NDOR's formula had additional problems. While acknowledging that the standard apportionment statutes do not use income in computing an apportionment factor,

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Nebraska District Court Holds That the State Must Devise an Equitable Apportionment Formula for Apple's One-Time TCJA Transition Tax Income

NDOR added an income figure, the $281.7 billion Section 965(a) inclusion, into a denominator built entirely on gross receipts, mixing apples and oranges. The Court also found a calibration defect. The denominator reflected the full $281.7 billion Section 965(a) inclusion amount, while the income that actually entered Apple's tax base was a smaller net figure of $163.5 billion, after the Section 965(c) deduction.

According to the Court, Apple's proposed formula had a temporal mismatch of its own, pairing 13 years of CFC gross receipts against a single year of Nebraska sales, a structure the Court described as presenting the mismatch "in its most pronounced form." It also had its own calibration problem. Apple's proposed denominator included the full $884.2 billion in CFC gross receipts tied to the $281.7 billion Section 965(a) inclusion amount, even though roughly $118.1 billion of that amount was later removed from Apple's tax base through the Section 965(c) deduction. In other words, receipts tied to income that never actually entered Apple's Nebraska tax base were still being used to shrink Apple's apportionment factor.

The Court reversed the Commissioner's order and remanded with specific parameters for a new formula. On remand, the formula must use gross receipts rather than an income proxy, must calibrate the denominator to the income actually entering the tax base, and must reconcile the mismatched time periods on a principled basis. The Court emphasized that the goal is "an equitable approximation, not perfection." Apple's constitutional arguments, including its Commerce Clause, Foreign Commerce Clause, and Due Process claims, were expressly preserved should Apple disagree with the result on remand.

The Takeaway: This decision is a reminder that taxpayers can, and do, prevail when challenging a state's apportionment methodology. Apple succeeded by demonstrating that the Commissioner's formula did not fairly represent its Nebraska income. The key was identifying specific structural mismatches. Apple pointed to the disconnect between a single-year factor and multi-year income, the use of an income proxy in a gross-receipts-based formula, and the failure to calibrate the denominator to the tax base actually being apportioned.

> **For multistate taxpayers facing similar issues, particularly those still working through the state-level ramifications of the TCJA's transition tax, this case offers a roadmap.**

Identify the structural defects, support them with the facts, and hold the taxing authority to the standard that alternative apportionment must be equitable in both directions.

NICOLE L. JOHNSON

PARTNER

Stopping the P.L. 86-272 Evasion

By Nicole L. Johnson

It is no secret that States abhor the protections afforded companies by P.L. 86-272—the federal provision that prevents States from imposing an income tax in certain circumstances. While many States have interpreted P.L. 86-272 as narrowly as possible, some have used other methods to attempt to sidestep the federal protections. One such method is the use of *Finnegan* rules for sourcing receipts for apportionment purposes in combined reporting States. Generally, under *Finnegan*, if one member of the combined group is taxable, then the sales of all members, even tax-exempt members, are included in the apportionment formula. However, the Massachusetts Appellate Tax Board (the "Board") put the kibosh on that.

The recent decision in *Smithfield Packaged Meats Corporation and Combined Affiliates v. Commissioner of Revenue* involves the Commissioner's "Reallocation Rule," which uses a *Finnegan* approach to sourcing. Dkt. No. C344811 (Mass. App. Tax Bd. July 22, 2026). Under the Reallocation Rule, if one member of a unitary group is taxable in Massachusetts, but another member is not, the sales of the nontaxable member may be assigned to the taxable group members. In *Smithfield*, one of the unitary group members was protected from taxation by P.L. 86-272. On audit, the Commissioner reassigned the Massachusetts sales of the nontaxable member to two taxable members.

On review, the Board analyzed whether the Reallocation Rule violated the Supremacy Clause of the U.S. Constitution. The Board determined that the Rule has the effect of taxing income proportionate to the amount of Massachusetts income earned by the nontaxable member. To determine if P.L. 86-272 prevented such taxation, the Board examined two questions. First, whether P.L. 86-272 only prevented a state from directly taxing the out-of-state entity. Second, whether the federal provision afforded its protections separately to each member of a unitary group.

With respect to the first issue, the Board determined that P.L. 86-272 exempts income earned by a protected entity from taxation. Here, by assigning the sales of the nontaxable member to other members, more income was taxable in Massachusetts. The Board found that the increase in taxable income was prohibited by the federal law.

For the second issue, the Board held that because a unitary group is not soliciting orders, a requirement to obtain P.L. 86-272 protection, but instead, the individual members are conducting the solicitation, the protections extend to each individual group member. Therefore, even if one member of the group is not protected by P.L. 86-272, other members may still be tax exempt.

While the Commissioner cited to many cases wherein the *Finnegan* approach to sourcing was upheld, the Board stated that those courts take positions that are not consistent with the federal law or incorrectly frame the issue. In the end, the Board did not permit the Commissioner to do indirectly what federal law prohibited it from doing directly—*i.e.*, subject the income of the nontaxable member to tax in Massachusetts.

> **In an onslaught of attempts to narrow P.L. 86-272, the case stands as a beacon that the federal provision's protections are holding steady.**

CHRISTOPHER M. LASH

ASSOCIATE

Processing Power: Maryland's Highest Court Rules Utility Equipment Qualifies for Sales Tax Exemption

By Christopher M. Lash

Electricity may be invisible, but the sales tax bill for the equipment that moves it is not. The Supreme Court of Maryland handed a significant victory to Potomac Edison, holding that the utility's conductor, substation, and transformer equipment is used "directly and predominantly in a production activity" and qualifies for Maryland's sales and use tax exemption. *Comptroller of Md. v. The Potomac Edison Co.*, No. 12, Sept. Term, 2025 (Md. July 17, 2026). The Court also clarified the applicable statute of limitations and entitlement to interest on refunds, two procedural questions that matter to any Maryland taxpayer who has ever written the Comptroller a check and later regretted it.

Background: Maryland exempts from sales and use tax "tangible personal property . . . used directly and predominantly in a production activity." Md. Code Ann., Tax-Gen. § 11-210(b)(1). Under the applicable regulation, "directly and predominantly" means "more than 50 percent of the time directly in production activities." COMAR 03.06.01.32-2B(2)(b). "Production activity" includes "processing . . . tangible personal property for resale," and "tangible personal property" is defined to include electricity. Tax-Gen. §§ 11-101(f)(1)(i), (k)(2)(iii).

Potomac Edison does not generate electricity, a detail the Comptroller thought dispositive and the Court did not. It receives high-voltage electricity from out-of-state power plants and delivers it to Maryland customers through a transmission and distribution system. Along the way, the voltage is "stepped up" to as high as 765,000 volts for efficient long-distance transmission, then "stepped down" through a series of substations and transformers until it reaches the 120 or 240 volts suitable for end-use consumption.

In 2006, Potomac Edison informed the Comptroller that its transmission and distribution equipment qualified for the production activity exemption. The Comptroller disagreed and audited. Due to an accounting irregularity, Potomac Edison paid sales tax on some equipment purchases during the audit period (August 2003 through July 2007) but not others. In April 2011, Potomac Edison filed for a refund of those payments. One week later, the Comptroller issued a notice of assessment for the taxes Potomac Edison had *not* paid, totaling over $1.7 million in tax, plus over $1.3 million in interest and penalties. The company persevered through the Maryland Tax Court, the Circuit Court, and two trips to the Appellate Court before finally reaching Maryland's highest court.

The Decision: Writing for a 6-1 majority over a sharply worded dissent, Justice Gould resolved all three issues in the taxpayer's favor. On the exemption, the Court held that "stepping up" and "stepping down" voltage constitutes "processing" under the plain meaning of the statute: the equipment "subjects the electricity to a series of actions designed for the specific objective of delivering, over long distances, electricity generated out of State to Maryland customers at a voltage suitable for their use." *Potomac Edison*, slip op. at 15. The Comptroller argued that the General Assembly meant to limit electricity-related exemptions to generation, not transmission. The Court disagreed, finding that generation and processing serve different statutory functions—one converts raw material into electricity, the other transforms it into a usable product.

On the statute of limitations, the Court held that the general four-year period under Tax-Gen § 13-1104(g) governs voluntary refund claims, not the narrow 30-day window under § 13-508(a), which applies only to refunds of payments made in response to a notice of assessment. The practical effect being that the refund was timely only as to payments made between April 1, 2007, and July 31, 2007, though the Court remanded for the Appellate Court to consider Potomac Edison's arguments on extension

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agreements and equitable estoppel. On interest, the Court held Potomac Edison was entitled to interest on its refund because the overpayment was "attributable to the State." "[W]hen the State takes the position that a tax is owed, the party sitting on the money bears the risk of being wrong." *Id.* at 28-29.

The Takeaway:

> **Three holdings, three wins, and each one matters independently.**

The production activity ruling opens the door to the exemption for utilities and other processors whose equipment transforms a product between the point of manufacture and the point of sale. The Court's willingness to apply the ordinary dictionary definition of "processing" without importing a "substantial transformation" test should encourage other industries to take a fresh look at whether their equipment qualifies. The limitations holding is equally important. Maryland taxpayers filing voluntary refund claims have four years, not 30 days, to act. And the interest holding puts the Comptroller on notice that when the State is wrong about whether a tax is owed, it pays for the privilege of holding the taxpayer's money.

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What's Shaking: Blank Rome State + Local Tax Roundup

Blank Rome's nationally prominent State + Local Tax attorneys are thought leaders in the community as frequent guest speakers at various local and national conferences throughout the year. Our State + Local Tax attorneys believe it is necessary to educate and inform their clients and contacts about topics that will impact their businesses. We invite you to attend, listen, and learn as our State + Local Tax attorneys interpret and discuss key legal issues companies are facing and how you can put together a plan of action to mitigate risk and advance your business in accordance with state and local tax laws.

COST Annual Meeting

- Blank Rome State + Local Tax partners Mitchell A. Newmark, Nicole L. Johnson and Eugene J. Gibilaro will be speaking at the COST Annual meeting in San Antonio, Texas on September 23 and 24, 2026. Mitchell's speech on the 23rd is titled "2026 In Review: Key Developments and the Road Ahead." Nicole's speech on the 23rd is titled "Hands Off Our Tax Base: When Federal Overreach Crosses the Line." Eugene's speech on the 24th is titled "Economic Substance and Business Purpose Doctrines in State Taxation." To learn more, please click here.

California All-Tax Conference

- Blank Rome State + Local Tax partner Nicole L. Johnson will be speaking at the California All-Tax Conference in San Diego, California on October 1, 2026. Nicole's speech is titled "SALT Litigation Update." To learn more, please click here.

Tax Executives Institute Annual Meeting

- Blank Rome State + Local Tax partner Eugene J. Gibilaro will be speaking at the Tax Executives Institute Annual Meeting in Nashville, Tennessee on October 20, 2026. Eugene's speech is titled "Alternative Apportionment Strategies: Challenging Distortion in a Single Sales Factor Environment." To learn more, please click here.

Paul J. Hartman SALT Forum

- Blank Rome State + Local Tax partners Nicole L. Johnson and Eugene J. Gibilaro will be speaking at the Paul J. Hartman SALT Forum in Nashville, Tennessee on October 27 and 28, 2026. Nicole's speech on the 27th is titled "That's Just Stupid," and Eugene's speech on the 28th is titled "Intergovernmental Disputes." To learn more, please click here.

Bank & Capital Markets Institute Conference

- Blank Rome State + Local Tax partner Mitchell A. Newmark will be speaking at the Bank & Capital Markets Institute Conference in Orlando, Florida on November 2, 2026. Mitchell's speech is titled "SALT Update." To learn more, please click here.

NYSSCPA New York and Tri-State Taxation Conference

- Blank Rome State + Local Tax associate Melanie L. Lee will be speaking at the NYSSCPA New York and Tri-State Taxation conference in New York, New York on November 10, 2026. Melanie's speech is titled "Top Nationwide SALT Issues." To learn more, please click here.

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New England State and Local Tax Forum

- Blank Rome State + Local Tax partner Nicole L. Johnson will be speaking at the New England State and Local Tax Forum in Boston, Massachusetts on November 18, 2026. Nicole's speech is titled "Hot Topics in Apportionment." To learn more, please click here.

NYU SALT Institute

- Blank Rome State + Local Tax partners Mitchell A. Newmark and Eugene J. Gibilaro will be speaking at the NYU SALT Institute conference in New York, New York on December 14, 2026. Mitchell's speech is titled "Smithfield: A Case Study" and Eugene's speech is titled "Apportionment – Focus on the Numerator and the Denominator." To learn more, please click here.