State Tax Matters
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The power of knowing
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State Tax Matters

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In this issue:

Multistate Tax Alert
California Legislature proposes repeal of water's-edge election

On February 10, 2026, California lawmakers introduced *Assembly Bill 1790 (A.B. 1790)*, which would – if enacted – modify California's water's-edge combined reporting regime and ultimately repeal the water's-edge election beginning with taxable years beginning on or after January 1, 2028. If enacted, A.B. 1790 would also impose interim changes for taxpayers that continue to file on a water's-edge basis for tax years beginning on or after January 1, 2026 and before January 1, 2028, including changes related to controlled foreign corporation ("CFC") income and the scope of entities included in the combined group.

A.B. 1790 is designated as a tax levy that would result in a taxpayer paying higher taxes within the meaning of the California Constitution and, as such, would require approval by a two-thirds vote of each house of the California Legislature.

This Multistate Tax Alert summarizes some of the relevant provisions of A.B. 1790.

URL: *https://www.deloitte.com/content/dam/assets-zone3/us/en/docs/services/tax/2026/california-legislature-proposes-repeal-of-waters-edge-election.pdf*

[Issued February 26, 2026]

Income/Franchise
Colorado – Ruling Addresses How Receipts from Partnership's Sale of Real Estate Impact Apportionment on Unitary Return

Private Letter Ruling - PLR 26-002, Colo. Dept. of Rev. (2/17/26). In a private letter ruling involving an S corporation that wholly owns or has majority interests in several partnerships and other entities and which files a "Colorado DR 0106 Partnership and S Corporation Tax Return" on a unitary basis with its related entities, the Colorado Department of Revenue's Office of Tax Policy held that certain gross receipts from one of its controlled partnership's sale of Colorado real estate are not included in receipts for purposes of calculating the apportionment factor that determines the S corporation's Colorado-source apportionable income under Colo. Rev. Stat. section 39-22-303.6. Under the submitted facts, the partnership will make the election under Colo. Rev. Stat. section 39-22-203(1)(a) to determine its Colorado-source income using the corporate apportionment and allocation rules. Additionally, the partnership will make the election provided under section Colo. Rev. Stat. section 39-22-303.6(8) to treat all of its income as apportionable income. The ruling explains that while the Colorado real estate at issue was related to the operation of the partnership's business, the sale of real estate was not a transaction or activity in the regular course of the partnership's business of operating assisted living facilities. As such, the ruling reasoned that the gross receipts from the sale of the Colorado real estate would not be included in the partnership's apportionment factor, and accordingly, no share of the gross receipts should be included in the calculation of the S corporation's apportionment factor under state law. Please contact us with any questions.

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District of Columbia – Attorney General Says Congressional Resolution Missed the 30-Day Deadline and Failed to Nullify Law that Decouples from Certain OBBBA Provisions

Impact of House Joint Resolution 142 on the District's Tax Laws, D.C. Office of the Attorney General (2/24/26). The Attorney General for the District of Columbia (D.C.) issued an opinion concluding that notwithstanding the recent enactment of H.J. Res. 142 [see *H.J.Res.142*, signed by President 2/18/26, and *State Tax Matters, Issue 2026-7*, for additional information on this Congressional joint resolution], the changes to the D.C. tax laws made by the "D.C. Income and Franchise Tax Conformity and Revision Emergency Amendment Act of 2025" [see *A26-0214 (D.C.B. 26-0457)*, enacted without mayor's signature 12/3/25 and *State Tax Matters, Issue 2025-46*, for more details on this emergency legislation] and the "D.C. Income and Franchise Tax Conformity and Revision Temporary Amendment Act of 2025" [see *A26-0217 (D.C.B. 26-0458)*, *enacted without mayor's signature 12/20/25* and *State Tax Matters, Issue 2026-1*, for more details on this temporary legislation that was subject to a 30-day congressional review period and scheduled to expire 225 days after taking effect] "continue to govern tax liabilities for taxpayers whose tax year ended December 31, 2025," and the temporary legislation "remains in effect and, absent further legislative action, will expire on September 25, 2026." In doing so, the D.C. Attorney General explains that because H.J. Res. 142 was not enacted into law by February 11, 2026, it did not, under section 602 of the Home Rule Act, prevent the temporary legislation from taking effect. As a result, the D.C. Attorney General determined that the temporary legislation at issue took effect on February 12, 2026.

This temporary legislation decouples from certain aspects of the federal One Big Beautiful Bill Act (commonly referenced as "OBBBA" and more formally as P.L. 119-21), including some of the OBBBA provisions pertaining to:

- the expensing of domestic research and experimental (R&D) expenditures in Internal Revenue Code (IRC) section 174A;
- IRC section 163(j)(8) on the definition of adjusted taxable income for the business interest limitation; and
- the special depreciation allowance for qualified production property under IRC section 168(n).

Please contact us with any related questions.

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Illinois – Appellate Court Affirms that Subsidiary Was Not an 80/20 Company and Affiliate Operated as a Shell

Case No. 4-25-012, Ill. App. Ct., 4th Dist. (2/25/26). In a case involving whether a parent company's subsidiary may be excluded from the Illinois corporate income tax combined return as an "80/20" company, an Illinois Appellate Court (Court) affirmed the trial court's 2025 ruling that the facts showed a certain affiliate of the subsidiary was operating as a "shell" company, and as a result, the subsidiary did not conduct 80% or more of its business outside the United States [see *Case No. 2022TX000155,* Ill. Cir. Ct. (1/9/25) and *State Tax Matters, Issue 2025-2*, for more details on the trial court's decision in this case]. In doing so, the Court agreed that certain "expatriate compensation charged" to the shell did not represent "substantive foreign business activities" conducted by the subsidiary through the shell under an "economic substance" analysis and thus should not be incorporated into the payroll portion of the "80/20" company calculation. The Court also agreed with the trial court that no reasonable cause exists to abate the underlying late payment penalty.

Note that another Illinois Appellate Court concluded similarly in 2025, in a case involving the same taxpayer but different tax years [see *Case No. 1-23-0913*, Ill. App. Ct., 1st Dist. (4/30/25) and *State Tax Matters, Issue 2025-21*, for details on this other Illinois Appellate Court decision]. Please contact us with any questions.

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Michigan – Department of Treasury Addresses Implications of Case Involving Insurance Affiliates and Combined Filing

Notice to Taxpayers Regarding Nationwide Agribusiness Insurance Co v Department of Treasury, Mich. Dept. of Treasury (2/19/26). A Michigan Department of Treasury (Department) notice addresses the Michigan Supreme Court's denied review of a 2024 Michigan Court of Appeals decision, which essentially held in the taxpayer's favor that i) a unitary business group (UBG) of insurance companies must file a combined return for calculation of Michigan premiums tax and related credits under Chapter 12 of the Michigan Income Tax Act ("Chapter 12"), and ii) because the retaliatory tax under the Michigan Insurance Code is incorporated into Chapter 12 of the Michigan corporate income tax (CIT), it also must be filed on a combined basis. Because the 2024 Michigan Court of Appeals holding stands, the notice explains that for purposes of unitary filing under Chapter 12, the definition of "taxpayer" includes a UBG of insurers. Furthermore, according to the notice, where a UBG of insurers exists, "the UBG must file a unitary return that calculates both the premiums tax and retaliatory tax liabilities at the UBG level." Consequently, "insurers may need to review their status as a member of a UBG."

The notice also explains that because this 2024 Michigan Court of Appeals decision is published, it applies to all open Michigan tax years. For tax year 2025, the notice suggests that because the deadline to file Michigan returns is "upcoming on March 1, 2026, insurers potentially impacted by the holding in this case are encouraged to file an application for an extension of time to file those returns." For tax years prior to 2025, the notice provides that amended returns are not required to be filed solely for compliance with the 2024 Michigan Court of Appeals decision, "but will be accepted from insurers who may benefit from doing so." Additionally, the notice explains that the Department is evaluating the decision and "reviewing the actions that must be taken by it and insurers to comply." To this end, "compliance instructions will be forthcoming" upon the Department's completed evaluation. The Department also states that any amended returns that have been filed based upon this 2024 Michigan Court of Appeals decision "will be processed upon the completion of this evaluation," and any further guidance "will be published on an ongoing basis as needed." Please contact us with any questions.

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Missouri – Consolidated Return Rule Amendments Reflect Apportionment Revisions and Treatment of Intercompany Transactions

Amended Rule 12 CSR 10-2.045, Missouri Consolidated Income Tax Returns, Mo. Dept. of Rev. (3/2/26). The Missouri Department of Revenue adopted changes to its rule on Missouri consolidated corporate income tax returns, including revisions reflecting legislation enacted in 2018 [see *previously issued Multistate Tax Alert* for more details on this legislation] that modified the Missouri consolidated return provisions such that transactions between members of the Missouri consolidated group are eliminated for apportionment purposes. The amendments also update references to Missouri's corporate income tax apportionment methods, which for tax years beginning on or after January 1, 2020, were replaced with an allocation and apportionment statute, Mo. Rev. Stat. § 143.455, that establishes concepts of "apportionable income" and "non-apportionable income," and requires that apportionable income for most taxpayers be apportioned to Missouri using a single receipts factor. Additional updates to the rule reflect appropriate timing for making the Missouri consolidated corporate income tax return election pursuant to subsequent caselaw, as well as several administrative and implementation items concerning changes to relevant Missouri forms and form instructions. The amended rule has been adopted as originally proposed in December 2025; no changes were made to the text of the proposed amendments [see *State Tax Matters, Issue 2025-47*, for details on the revised text]. Please contact us with any questions.

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Virginia – New Law Updates State Conformity to IRC, Couples with Some OBBBA Provisions and Decouples from Others

H.B. 29, signed by gov. 2/20/26; *Tax Bulletin 26-1 - Important Information Regarding 2025 Virginia Income Tax Returns: Virginia's Rolling Conformity to the Internal Revenue Code Replaced with a Fixed Date of December 31, 2025*, Vir. Dept. of Tax. (2/20/26). Following the enactment of legislation in 2025 providing that Virginia will not conform to certain federal law changes enacted on or after January 1, 2025, but before January 1, 2027, which impact its general fund revenues [see *H.B. 1600*, signed by gov. 5/2/25, and *State Tax Matters, Issue 2025-19*, for more details on this budget legislation], a recently signed 2026 budget bill now provides for a fixed Internal Revenue Code (IRC) conformity date of December 31, 2025, for Virginia corporate and individual income tax purposes, with some newly listed exceptions. A related Virginia Department of Taxation bulletin explains that under this enacted 2026 budget bill, Virginia generally will "continue to automatically conform to any federal tax law amendment that extends the expiration date of a federal tax provision to which Virginia conforms or has previously conformed." In this respect, the 2026 budget bill conforms with many aspects of the federal One Big Beautiful Bill Act (commonly referenced as "OBBBA" and more formally as P.L. 119-21), but specifically decouples from certain OBBBA provisions – including those pertaining to the:

- immediate expensing of qualified production property under IRC section 168(n);
- immediate expensing of domestic research and experimental (R&D) expenditures under IRC section 174A, "including retroactive and catchup provisions"; and
- increases to the expensing limits for certain depreciable business assets under IRC section 179.

The bulletin also explains that the OBBBA modifies the federal limitation on the deduction of business interest expenses under IRC section 163(j), "which affects the amount of business interest disallowed as a deduction on the federal return." Further, while "Virginia conforms to this federal change," for taxable years 2025 and thereafter, Virginia law now provides that "the Virginia subtraction for disallowed business interest is reduced from 50 percent to 20 percent of the amount of business interest disallowed on the federal return." The bulletin notes that Virginia will continue to decouple from many federal tax law provisions, including bonus depreciation allowed for certain assets.

The budget bill also updates terminology of the deduction under IRC section 951A from global intangible low-taxed income (GILTI) to net controlled foreign corporation tested income (NCTI), as well as extends Virginia's elective pass-through entity tax (PTET) indefinitely rather than have it sunset on December 31, 2026.

Similar to provisions included in state budget acts from previous years [see *State Tax Matters, Issue 2024-20*, for similar provisions from a previous year], applicable retroactively for taxable years beginning on and after January 1, 2004, the budget bill includes non-codified provisions that limit the "subject to tax" and unrelated party "safe harbor" statutory exceptions to Virginia's intercompany intangible expense addback statute. These various non-codified provisions are essentially being continued with this most recent budget legislation enactment. Please contact us with any questions.

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Gross Receipts

Ohio – Amended Rule on CAT's Agency Exclusion Updates Agency Definition to Reflect Caselaw

Amended Ohio Admin. Code 5703-29-13, Ohio Dept. of Tax. (2/17/26). The Ohio Department of Taxation amended its Ohio commercial activity tax (CAT) rule on the "agency exclusion" by revising the definition of "agency" to "incorporate changes due to recent case law." The amended rule provides that "in the case of a person who enters into a contract with a client where the person is reimbursed for its own expenses incurred in the performance of the contract, an agency relationship generally does not exist." Therefore, "the amounts received from the client to reimburse the person for its own expenses are considered gross receipts and cannot be deducted from the person's gross receipts." An illustrative example involving a food services provider is also included.

Note that in 2025, in a case involving a company providing managed services for its clients wherein it purchased food and supplies for them pursuant to certain management fee contracts, the Ohio Supreme Court affirmed the company failed to show it was acting as an agent of its clients and thus the reimbursements it received from these contracts could not be excluded from its Ohio CAT receipts [see *Case No. 2023-1540*, Ohio (6/18/25) and *State Tax Matters, Issue 2025-24*, for more details on this decision]. Please contact us with any questions.

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Sales/Use/Indirect

Federal – U.S. Supreme Court Says Federal Act at Issue Does Not Authorize the President to Impose Tariffs

Docket No. 24-1287, U.S. (2/20/26). The U.S. Supreme Court (Court) recently held that the federal International Emergency Economic Powers Act (IEEPA) does not authorize the President to impose tariffs. However, in doing so, the Court did not address a refund mechanism and instead remanded the case to address the issue.

Note that any subsequently instituted tariff refunds resulting from this case (if any) potentially may allow for sales tax refunds in some state and local taxing jurisdictions. Please contact us with any questions.

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Alabama – Focusing on Substance Over Form, Truck Purchased & Used for Freight Delivery Deemed Subject to Use Tax

Docket No. S. 24-0533-RC, Ala. Tax Trib. (2/19/26). In a case involving a trust, limited liability company (LLC), and individual who served as the trust's sole trustee and beneficiary and the LLC's sole owner, the Alabama Tax Tribunal (Tribunal) applied a "substance-over-form"-type analysis to hold that the individual effectively purchased a truck at retail from an out-of-state vendor and was liable for Alabama use tax when he subsequently brought it into the State for use in his freight delivery business. Under the facts, the trust had entered into a "Truck Lease/Operator Agreement" with the LLC providing that the trust's sole trustee (i.e., the individual) was the truck's "operator." Rejecting the trust's claim that it had purchased the truck exempt under statute at wholesale, rather than at retail, and was in the business of leasing trucks to others, the Tribunal concluded that "for tax purposes," neither the trust nor the LLC existed as they are "both one and the same taxpayer" (i.e., the individual). In this respect, the Tribunal held that the "purported lease agreement" between the trust and LLC was a "legal nullity," and the individual effectively acquired the truck himself and purported to lease it to himself – a "transaction that has no legal effect and cannot give rise to a lessor/lessee relationship, regardless of any agreement or any level of activity." In doing so, the Tribunal noted that the LLC and trust were both disregarded entities for federal income tax purposes for the relevant years at issue. Please contact us with any questions.

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Louisiana – Complimentary Hotel Rooms Deemed Nontaxable Marketing Tool Rather than Taxable Transactions for Consideration

Case Nos. L01710 and L01762, La. Bd. of Tax App. (2/5/26). In a "case of first impression" concerning whether local sales and occupancy taxes were due on complimentary hotel rooms furnished by two casinos to select patrons and guests, the Louisiana Board of Tax Appeals concluded that, based on the provided facts and taxpayer testimony, the casinos were not liable for either of the taxes as the rooms were considered a marketing tool and a promotional means to incentivize gaming, rather than exchanged for consideration or rents paid. Among the facts in the taxpayers' favor, submitted testimony showed that the patrons and guests were not required to gamble or otherwise do anything else to obtain a free hotel room "comp" from the casinos. Please contact us with any questions.

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Maryland – Adopted Rule Changes Reflect New 3% Sales Tax on Certain IT and Data Services

Amended COMAR 03.06.01.01, 03.06.01.03, 03.06.01.05, 03.06.01.07, 03.06.01.08, 03.06.01.11, 03.06.01.21, 03.06.01.25, 03.06.01.28, 03.06.03.02, and New COMAR 03.06.01.48, 03.06.01.49, 03.06.01.50, Md. Comptroller (eff. 3/2/26); *News Release*, Md. Comptroller (12/12/25). Pursuant to legislation enacted in 2025 imposing a new 3% sales tax on certain information technology (IT) and data services as of July 1, 2025 [see *H.B. 352*, ***signed by gov. 5/20/25***, and *previously issued Multistate Tax Alert* for more details on these law changes], the Maryland Comptroller (Comptroller) adopted amended and new administrative rules on the application and administration of the new taxable services. According to a related news release from the Comptroller, the adopted rules are "aligned with" previously issued guidance [see *Technical Bulletin 56 - Questions and Answers on New Taxable Services*, Md. Comptroller (rev. 6/30/25) and *State Tax Matters, Issue 2025-26*, for more details on this earlier guidance]. The amended rules have been adopted as originally proposed in December 2025; no changes were made to the text of the proposed amendments [see *State Tax Matters, Issue 2025-48*, for details on the revised text]. Please contact us with any questions.

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Other/Miscellaneous

Maryland – Amended DAGRT Rule Says that Taxable Digital Ad Services Must be Programmatic and Conveyed Visually

Amended COMAR 03.12.01.01, Digital Advertising Tax, Definitions, Md. Comptroller (eff. 3/2/26); *News Release*, Md. Comptroller (12/12/25). The Maryland Comptroller (Comptroller) adopted changes to an administrative rule on Maryland's novel tax on digital advertising services (*i.e.*, the "Digital Advertising Gross Revenues Tax" or "DAGRT") that reflect guidance issued in 2025 [see *Technical Bulletin No. 59: Digital Advertising Gross Revenues Tax*, Md. Comptroller (eff. 7/11/25) and *State Tax Matters, Issue 2025-27*, for more details on this 2025 guidance], requiring that digital advertising services be both programmatic and conveyed visually to be taxable under the DAGRT. According to a related news release from the Comptroller, "any taxpayer who may have previously reported tax on digital advertising services that are not both programmatic and conveyed visually has three years from the due date to file an amended return." The amended rule has been adopted as originally proposed in December 2025; no changes were made to the text of the proposed amendments [see *State Tax Matters, Issue 2025-48*, for details on the revised text]. Please contact us with any questions.

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