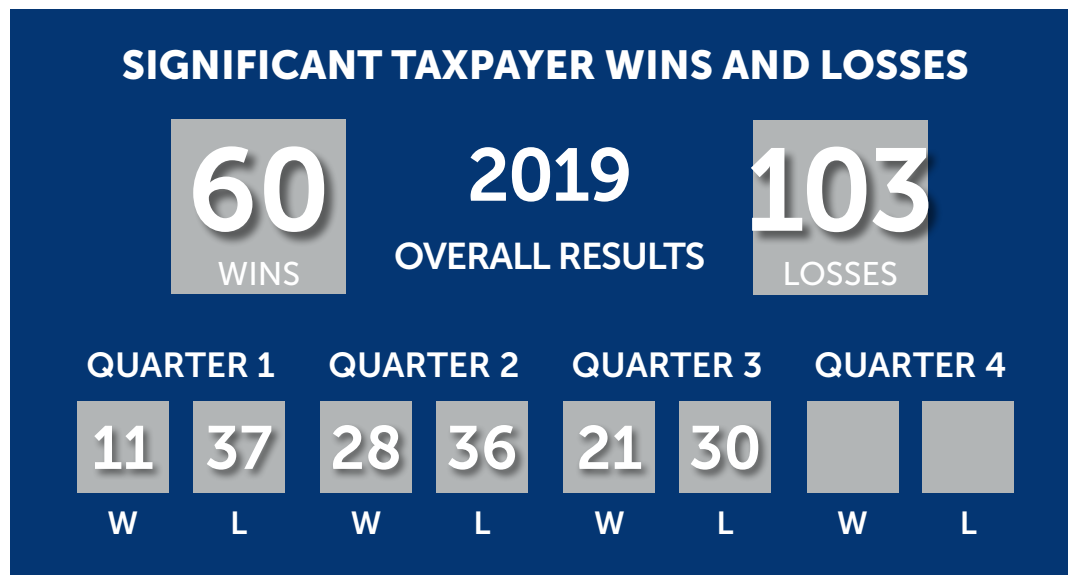


This is the third edition of the Eversheds Sutherland SALT Scoreboard for 2019. Since 2016, we have tallied the results of what we deem to be significant taxpayer wins and losses and analyzed those results. This edition of the SALT Scoreboard includes a discussion of the Illinois Appellate Court's recent decision in *Labell v. City of Chicago*, insights regarding Maryland's net operating loss deduction, and, to celebrate the opening of our new San Diego office, a spotlight on California tax cases.

3rd quarter 2019

In the third quarter of 2019, taxpayers prevailed in 41.2% (21 out of 51) of the significant cases.* Taxpayers won 50.0% (7 out of 14) of the significant corporate income tax cases and 40.9% (9 out of 22) of the significant sales and use tax cases in the third quarter. These results show continued improvement for taxpayers from the first quarter of 2019. Taxpayers have now prevailed in 36.8% of total significant cases, 32.6% of corporate income tax cases, and 38.7% of significant sales and use tax cases.



*Some items may have been decided in a prior quarter but included in the quarter in which we summarized them.

Year-to-date

Taxpayers prevailed in **14** out of **43** significant corporate income tax cases across the country

Taxpayers prevailed in **29** out of **75** significant sales and use tax cases across the country

SIGNIFICANT MULTISTATE DEVELOPMENTS

Dividends

CASE: *Exxon Mobil Corp. v. Montana Department of Revenue*, 444 P.3d 407 (Mont. 2019).

SUMMARY: The Montana Supreme Court held that the Montana Department of Revenue erred in determining that the taxpayer was entitled to only an 80% exclusion for dividends received from domestic corporations not included in the taxpayer's water's-edge combined return. Instead, the court held that all of the actual dividends it received from such entities should be excluded from income. In filing its return, the taxpayer excluded from its combined return domestic subsidiaries that had less than 20% domestic payroll and property factors (i.e., 80/20 corporations) and also excluded 100% of the dividends received from such corporations. The court stated that, unlike certain types of deemed distribution income, Montana law did not address the treatment of dividends actually received from 80/20 corporations and does not expressly prohibit the full dividend received deduction. [View](#) more information.

Streaming Services

CASE: *Labell v. City of Chicago*, 2019 IL App (1st) 181379.

SUMMARY: The Illinois Appellate Court upheld the City of Chicago's controversial imposition of its amusement tax on streaming video, streaming audio and online gaming services. The court determined that the tax did not: (1) exceed Chicago's home rule authority by effectively taxing activities occurring outside of Chicago; (2) violate the Uniformity Clause of the Illinois Constitution by applying the tax differently to: (a) Chicago residents and nonresidents; or (b) streaming services and automatic amusement devices or live cultural performances, or (3) violate the federal Internet Tax Freedom Act by treating streaming services differently from automatic amusement machines or live cultural performances. [View](#) more information.

Net Operating Losses

CASE: *Sunbelt Rentals, Inc. v. Comptroller of Maryland*, No. 18-IN-00-0241 (Md. Tax Ct. Sept. 9, 2019).

SUMMARY: The Maryland Tax Court reversed the Comptroller's disallowance of NOL deductions and essentially struck down a regulation that limited the usage of pre-nexus NOLs. Relying on a regulation enacted in 2007, the Comptroller disallowed the taxpayer's use of NOLs accumulated by entities with no nexus in Maryland that subsequently merged into a Maryland taxpayer. The Tax Court ruled that no statutory authority existed for this regulation, and the only permissible subtractions or additions to federal taxable income are those expressly set forth in Maryland statutes. In this case, the Tax Court approved the taxpayer's NOLs because they were allowed for federal income tax purposes, and no Maryland statute contemplated the Comptroller's modification. [View](#) more information.

Cost of Goods Sold

CASE: *Metropolitan Telecommunications Holding Co. v. Hegar*, No. 06-19-00016-CV (Tex. App. Aug. 21, 2019).

SUMMARY: The Texas Court of Appeals held that the sale of telecommunication signals constitutes the sale of a service for purposes of the franchise tax. The taxpayer sold electrical, light and radio signals to customers through lines leased from other telecommunications companies. The taxpayer argued it sold tangible personal property because the signals were perceptible to the senses. As a result, the taxpayer argued it was entitled to a deduction for the cost of goods sold. However, the court noted the taxpayer marketed itself as a telecommunications service provider. Applying Texas precedent, the court held that the "provision of telecommunications products constitutes the provision of services, not goods." The taxpayer also argued that although it sold signals, it did not provide a telecommunications service because it did not have the infrastructure to deliver, transmit or convey the signals. But the court concluded that leasing "the means by which it made its signals available to customers did not transform its business" to anything other than transmitting, conveying or routing its signals to customers. Consequently, the court held the taxpayer was not entitled to a cost of goods sold deduction. [View](#) more information.



Spotlight on California tax cases

CASE: *In re Jali, LLC*, Case No. 18073414 (Cal. Off. Tax App. July 8, 2019) (pending precedential).

SUMMARY: For purposes of the annual \$800 LLC tax, the California Office of Tax Appeals determined that an out-of-state LLC did not have taxable nexus with California, solely because it held an ownership interest (ranging from 1.12% to 4.75%) in an in-state LLC. The court rejected the Franchise Tax Board's 0.2% ownership threshold (derived from the California Court of Appeal decision in *Swart*) as a bright-line legal standard for distinguishing between an active or a passive ownership interest in an LLC classified as a partnership. The OTA concluded that the out-of-state LLC did not have any ability or authority to influence or participate in the management or operation of the in-state LLC because: (1) the in-state LLC was manager-managed by another member; (2) the out-of-state LLC had no power to manage the in-state LLC or bind or act on its behalf in any way, and (3) the out-of-state LLC had no interest in any specific property in the in-state LLC. Accordingly, the OTA held the out-of-state LLC did not have taxable nexus with California. [View](#) more information.

CASE: *In re Millennium Dental Technologies, Inc.*, Case No. 18063362 (Cal. Off. Tax App. May 31, 2019).

SUMMARY: The OTA upheld the FTB's denial of a taxpayer's refund claim for the 2008 tax year, ruling that the claim was barred by res judicata. The FTB had previously proposed adjustments to the taxpayer's 2008 corporate income tax return. The taxpayer appealed the FTB's notice of action to the State Board of Equalization, which sustained the assessment on the merits and denied a petition for rehearing. The taxpayer then paid the additional tax and filed a refund claim, reasserting largely the same arguments it had made before the SBE. The FTB denied the refund claim, stating that the SBE had already affirmed the 2008 notice. The OTA affirmed the FTB's decision, concluding that all four elements of res judicata were satisfied.

CASE: *In re Depot Repair Services, LLC*, Case No. 18012004 (Cal. Ct. App. Jul. 12, 2019).

SUMMARY: The OTA held that an out-of-state LLC did not have standing to prosecute an appeal of a California Department of Tax and Fee Administration decision. The California Secretary of State had forfeited the LLC's status in California, which can occur, for example, if an LLC fails to file tax returns or make required payments. The court held that foreign LLCs that have been forfeited have lost the privilege of exercising the powers, rights and privileges of a foreign LLC in the state, including prosecuting an appeal before the OTA. As a result, the OTA dismissed the taxpayer's appeal.

CASE: *Howard Jarvis Taxpayers Association v. County of Yuba*, No. CV PT 18-00002127 (Cal. Super. Ct. Sept. 9, 2019); *City of Fresno vs. Fresno Building Healthy Communities*, No. 19CECGOO422 (Cal. Super. Ct. Sept. 5, 2019); *Howard Jarvis Taxpayers Association v. City and County of San Francisco*, No. CHC-18-568657 (Cal. Super. Ct. July 5, 2019).

SUMMARY: On July 5, a San Francisco judge ruled that voters can approve special taxes placed on the ballot via signature-gathering without the two-thirds majority vote previously thought to have been required. The judge held that the California Constitution (specifically, the requirement that special taxes pass with a two-thirds majority) limits the San Francisco Board of Supervisors' authority to impose new taxes, but does not apply to the voters' initiative power. On the other hand, on September 5, the Fresno County Superior Court held that special local taxes require two-thirds approval by voters, regardless of whether they were put on the ballot by a local government body or by a voter initiative. Subsequently, on September 9, the Yuba County Superior Court struck down a sales tax increase that was presented to voters as a majority-vote measure, but in fact was a special tax requiring a two-thirds vote for passage. Despite the diverging opinions, each opinion cited the California Supreme Court's ruling in *California Cannabis Coalition v. City of Upland*, 401 P.3d 49 (Cal. 2017). The application of the two-thirds voting requirement will likely be resolved by the California Supreme Court. [View](#) more information.

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