LBMC

STATE & LOCAL TAX INSIGHTS

Stay ahead of shifting state and local tax developments with LBMC's SALT newsletter. Each edition delivers timely updates, legislative highlights and actionable insights to help businesses navigate evolving compliance requirements and uncover potential tax savings. Whether you operate in one state or across multiple jurisdictions, our state and local tax specialists keep you informed on the trends and policy changes that impact your business.

SALES TAX

Arkansas High Court Limits Resale Exemption for Shipping Pallets

The Arkansas Supreme Court held that the state's sale-for-resale exemption applies only to items that physically become a recognizable, integral part of the finished product. Equipment used to handle or move goods during manufacturing or shipping remains subject to sales tax under this standard even when it plays an essential role in getting the product out the door, because the equipment itself is never incorporated into what is sold to the customer.

Arizona Tax Court: Data Center Rentals Subject to TPT Going Forward

In a case involving an internet service provider's data center operation, the Arizona Tax Court held that colocation services and server rentals are subject to transaction privilege tax (TPT) as rentals of real and tangible personal property, respectively. The Court found that customers, not the provider, controlled the servers and space, and that related services were incidental, but limited the tax's application to prospective periods and ruled it did not violate the Internet Tax Freedom Act.

Colorado Expands Sales Tax to Downloaded Software and SaaS

Colorado enacted H.B. 26-1223, signed June 4, 2026, repealing the state's long-standing sales and use tax exemption for downloaded computer software effective January 1, 2027. Under the new law, software available for repeated sale or license, including remotely accessed software, SaaS, and mobile applications, is generally treated as taxable unless an exemption applies. A narrower exemption survives for software governed by a negotiated license agreement that is individually bargained and signed by both parties before or at the time of access, or software developed for a specific user. Standard click-through, browse-wrap, and other non-negotiated agreements do not qualify.

Colorado Ties MTC Resale Certificate Use to State Sales Tax License

The Colorado Department of Revenue reiterated that a wholesaler cannot claim a sales tax exemption using the resale certificate developed by the Multistate Tax Commission unless the wholesaler holds a Colorado sales tax license. However, sellers may accept Form 5002 from buyers without a Colorado sales tax license.

Illinois Budget Bill Adds Slate of New Digital Economy Taxes

Illinois enacted S.B. 3019 (Public Act 104-0468), signed June 16, 2026, as part of the state's fiscal year 2027 budget. Effective January 1, 2027, the law creates a Targeted Advertising Services Tax equal to 10% of gross receipts derived from targeted advertising delivered in Illinois, applying only to providers whose annual Illinois gross receipts from such services exceed $1 million. The same effective date brings a new Digital Asset Tax of 0.2% on the value of certain digital asset business activity received by Illinois customers, collected by digital asset brokers that meet the applicable Illinois presence or receipts thresholds, along with a Social Media Platform Fee assessed on platforms based on the number of Illinois users from whom they collect data. The law also expands the state's Sports Wagering Act to tax exchange wagers placed on prediction markets tied to sporting contests.

Missouri Finds SaaS Platform Isn't a Marketplace Facilitator

In a letter ruling, the Missouri Department of Revenue determined that a company providing software, SaaS solutions, and an online platform for customer auctions is not a "marketplace facilitator" because it does not collect or remit payments for sales made through its site. The Department emphasized that merely connecting users to third-party payment processors does not constitute payment processing, particularly where the company has no control over transactions, funds, or payment selection.

Tennessee Finds Online Auction Platform Falls Outside Marketplace Facilitator Rules

The Tennessee Department of Revenue ruled that a company providing a digital infrastructure platform for auctions of real and tangible personal property is not a marketplace facilitator required to collect and remit sales tax on sales made through its platform. The Department found that the company's role was limited to hosting listings and running the auction mechanics, without collecting payment from buyers or transmitting proceeds to sellers, so the statutory marketplace facilitator test was not met.

INCOME TAX

California Finds Taxpayer's Activities Exceed P.L. 86-272 Protection

The California Office of Tax Appeals denied an out-of-state S corporation's rehearing request, affirming that it owed both the $800 minimum franchise tax and California net income tax for 2012–2013. The OTA held that the company's in-state activities went beyond mere solicitation under P.L. 86-272, as employees gathered competitor samples, shared customer data, and performed product-matching functions to gain a competitive edge. It also found that "menu ideation" and market research conducted in California were ongoing, non-ancillary activities that created sufficient nexus for taxation.

Colorado Adds Income Tax Add-Backs and New Water's-Edge Election

Colorado enacted several income tax changes affecting both individuals and corporations. Beginning in 2026, individual taxpayers must add back overtime compensation excluded from federal income when calculating Colorado taxable income. Starting in 2027, taxpayers must also add back federally excluded gains from Qualified Opportunity Funds unless the investment is in a Colorado Qualified Opportunity Fund with at least 90% of its assets located in Colorado Opportunity Zones. For corporations, Colorado introduced a new elective water's-edge combined reporting method for unitary groups of C corporations effective in 2027. This election replaces the prior water's-edge option under worldwide combined reporting rules and will remain binding for 10 years.

Hawaii Adds Top Income Tax Bracket, Trims Several Credits

Beginning in 2027, Hawaii will add a new 13% personal income tax bracket for higher-income taxpayers, with thresholds starting at $1 million for joint filers and lower levels for other filing statuses. The law also tightens the renewable energy tax credit by adding income limits, new reporting requirements, a $40 million annual cap, and a 2029 sunset, while phasing out several other tax credits between 2027 and 2029.

Illinois Extends Cap on Corporate Net Operating Loss Deductions

Illinois extended the limitation on the corporate net operating loss carryover deduction to taxable years ending on or after December 31, 2027, a limitation that previously did not apply beyond that date. For those years, the carryover deduction is capped at the greater of $500,000 or a percentage of net income that starts at 15% for tax years ending in 2027 and 2028 and rises in steps to 80% for tax years ending on or after December 31, 2031. The legislation also permits an alternative computation method for Illinois's pass-through entity tax election for tax years ending on or after December 31, 2026.

Illinois Revenue Department Turns Down Bid for Alternative Apportionment

The Illinois Department of Revenue denied a corporate taxpayer's request to replace the standard single-sales factor apportionment with throwback sales or to exclude certain throwback sales, emphasizing that alternative methods cannot be used solely to achieve a different result. The Department concluded the taxpayer failed to prove that the statutory formula did not fairly represent its Illinois business activities or market presence.

South Carolina Appeals Court Upholds Forced Combined Reporting

The South Carolina Court of Appeals affirmed a decision requiring Tractor Supply Company to file its South Carolina corporate income tax returns on a combined unitary reporting basis rather than on a separate-entity basis. The Department of Revenue had determined that the company's transfer pricing arrangement with an affiliated procurement subsidiary understated its South Carolina income, and the court agreed that combined reporting was a reasonable alternative apportionment method under the state's statute. The decision reinforces that South Carolina's separate-entity filing requirement can give way to combined reporting when the Department shows that related-party pricing distorts the income properly attributable to the state.

Texas Updates Cost of Goods Sold Rule Under the Franchise Tax

The Texas Comptroller adopted amendments to 34 Tex. Admin. Code Section 3.588, the rule governing the cost of goods sold deduction under the franchise tax margin calculation. Beginning with the 2026 franchise tax report, taxable entities will determine depreciation and other cost of goods sold items using the federal tax law in effect for the relevant federal tax year, rather than the version of the Internal Revenue Code in effect on January 1, 2007, except where a Texas statute or rule specifically references the IRC. The amendments also allow a one-time net depreciation adjustment on the 2026 report to reconcile historical differences between federal and Texas depreciation for qualifying assets.

Learn More About LBMC's SALT Practice

Navigating the complex and evolving landscape of state and local taxation often leaves businesses overpaying taxes to state and local taxing authorities, driving a negative impact on operations and financial performance. Refund reviews and strategic appeals can unlock historical overpayments and help businesses proactively manage cash flow. LBMC's State and Local Tax (SALT) team can assist your business by providing a data-driven review of state and local tax payments, identifying overpayments, working with taxing authorities to recover value, and implementing an optimized tax strategy that ensures compliance while mitigating future overpayments and exposure.

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