



AUGUST 2022

# THE BR STATE + LOCAL TAX SPOTLIGHT **BLANKROME**



CONTENTS

1. Note from the Editor
2. Protecting Their Own: Limiting Out-Of-State Taxation
3. Interest Payment Not Required to Be Added Back as Alabama's Subject-To-Tax Exception Applied
4. Alaska Supreme Court Saves Poorly Worded Tax Statute
5. What's Shaking: Blank Rome State + Local Tax Roundup

**STATE + LOCAL TAX TEAM:**

Craig B. Fields | [craig.fields@blankrome.com](mailto:craig.fields@blankrome.com)

Nicole L. Johnson | [nicole.johnson@blankrome.com](mailto:nicole.johnson@blankrome.com)

Mitchell A. Newmark | [mitchell.newmark@blankrome.com](mailto:mitchell.newmark@blankrome.com)

Irwin M. Slomka | [irwin.slomka@blankrome.com](mailto:irwin.slomka@blankrome.com)

Eugene J. Gibilaro | [eugene.gibilaro@blankrome.com](mailto:eugene.gibilaro@blankrome.com)

Kara M. Kraman | [kara.kraman@blankrome.com](mailto:kara.kraman@blankrome.com)

Philip M. Tatarowicz | [phil.tatarowicz@blankrome.com](mailto:phil.tatarowicz@blankrome.com)

Madison A. Ball | [madison.ball@blankrome.com](mailto:madison.ball@blankrome.com)

## Note from the Editor

By Eugene J. Gibilaro

---

**Welcome to the August 2022 edition of *The BR State + Local Tax Spotlight*.** We understand the unique demands of staying on top of important State + Local Tax developments, which happen frequently and across numerous jurisdictions. Staying updated on significant legislative developments and judicial decisions helps tax departments function more efficiently and improves strategy and planning. That is where *The BR State + Local Tax Spotlight* can help. In each edition, we will highlight for you important State + Local Tax developments that could impact your business. In this issue, we will be covering:

- New Hampshire legislation aimed at limiting other states' ability to tax its residents' income;
- The Alabama Tax Tribunal's decision that a corporation was not required to add back interest paid to a related entity as the recipient was subject to tax on that income in Ireland; and
- The Alaska Supreme Court's decision overruling a lower court that had struck down as unconstitutionally vague a tax statute affecting corporations.

**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.**

---

*Editor, **The BR State + Local Tax Spotlight***



**EUGENE J. GIBILARO**

Of Counsel

212.885.5118

[eugene.gibilaro@blankrome.com](mailto:eugene.gibilaro@blankrome.com)

---



NICOLE L. JOHNSON

PARTNER

## Protecting Their Own: Limiting Out-Of-State Taxation

By Nicole L. Johnson

In June, New Hampshire enacted legislation in an attempt to limit other states from taxing its residents' income. Specifically, H.B. 1097 provides that "compensation earned or received by residents of the state of New Hampshire for services entirely performed within the state of New Hampshire shall not be subject to personal income taxation *in any other state.*" H.B. 1097, Ch. 185, 2022 Sess., Reg.Sess. (N.H. June 17, 2022) (emphasis added).

This legislation is a not-so-subtle attack on Massachusetts' attempts, by regulation, to tax income earned by non-Massachusetts residents during the pandemic. Previously, New Hampshire sought to challenge the offending Massachusetts regulation at the U.S. Supreme Court but was unsuccessful. Motion for leave to file a bill of complaint DENIED, *New Hampshire v. Massachusetts*, No. 220154 (U.S. June 2021). Many hoped the Court would allow the case to proceed to deal with the constitutionality of the dreaded convenience of the employer rules adopted by some states. States with such "convenience" rules in place have been using those rules to tax the income of nonresidents that was earned outside of the taxing state for years—in fact, New York is one of the biggest offenders. Unfortunately, the challenge to the "convenience" rules will have to wait for another day.

Not to be discouraged, just over a year after its failed attempt to challenge the Massachusetts regulations, New Hampshire launched its second assault on other states taxing its residents' income. And there is an innate sense of fairness underlying the recent legislation. Why should another state be allowed to tax income for services that were performed wholly

within New Hampshire? Nevertheless, the legislation raises a number of issues.

First, does one state have the ability to limit the taxing jurisdiction of another state? It is easy to understand why a state would seek to protect its citizens, but there are limits to how far that protection can extend. The New Hampshire law is telling other states what they cannot do to New Hampshirites—or at least what they cannot do to their income. While such laws are certainly appealing, especially in the area of taxation, should one state have that power over others?

**States with such "convenience" rules in place have been using those rules to tax the income of nonresidents that was earned outside of the taxing state for years—in fact, New York is one of the biggest offenders.**

Second, if a state can dictate whether another state can tax its residents' income, should that power also extend to corporations? For example, should a state be able to prevent other states from taxing a domiciliary corporation?

Although New Hampshire's legislation is laudable in many respects, it will be telling to see the challenges against it. □



CRAIG B. FIELDS

PARTNER

## Interest Payment Not Required to Be Added Back as Alabama’s Subject-To-Tax Exception Applied

By Craig B. Fields

On July 28, 2022, the Alabama Tax Tribunal held that a corporation is not required to add back interest paid to a related entity as the recipient was subject to tax on that income in Ireland. This was so even though the related entity made significant interest payments to other affiliates and ultimately paid tax to Ireland on only \$10,000 of net income. *Pfizer, Inc. v. Alabama Dep’t of Revenue*, Docket No: BIT. 18-236-JP (Ala. Tax Trib. July 28, 2022). This ruling should help other taxpayers fighting the applicability of addback statutes.

**One of the exceptions to the add back is where the corresponding item of income was “subject to” a tax based on the related member’s net income by a foreign nation which has in force an income tax treaty with the United States.**

**Facts:** Pfizer paid \$658 million in interest to Pfizer Transactions Ireland (“PTI”) and did not add back that payment in calculating its Alabama corporate income tax. Pfizer took the position that the payment was not required to be added back as the interest was “subject to tax” in Ireland and, therefore, one of the exceptions to the add back applied.

The Department of Revenue (“Department”) challenged the applicability of the exception because, while PTI did include the \$658 million as income on its Irish tax return, it also deducted large amounts of interest payments to affiliates based in Luxembourg and, after deducting its

administrative expenses, had a trading profit (to which the tax rate is applied) of \$10,000.

Alabama’s add back statute generally requires the add back of interest and intangible expenses paid to an affiliate (called a “related member”). One of the exceptions to the add back is where the corresponding item of income was “subject to” a tax based on the related member’s net income by a foreign nation which has in force an income tax treaty with the United States.

In 2008, the statute was clarified to provide: “That portion of an item of income which is attributed to a taxing jurisdiction having a tax on net income shall be considered subject to a tax even if no actual taxes are paid on such item of income in the taxing jurisdiction by reason of deductions or otherwise.” Ala. Code § 40-18-35(b).

**The Decision:** The Tax Tribunal held that the clear wording of the statutory exception applied and found that by including the interest income from Pfizer in PTI’s Irish tax returns, the company was subject to tax on that income. That PTI deducted an almost equal amount of interest that it paid to its Luxembourg affiliates did not change this fact. The Tribunal rejected the Department’s attempt to limit the 2008 clarifying statutory change. “The facts presented in this appeal fit squarely within the subject-to-tax exception to Alabama’s add-back statute, as amended.” □



EUGENE J. GIBILARO

OF COUNSEL

# Alaska Supreme Court Saves Poorly Worded Tax Statute

By Eugene J. Gibilaro

When is a tax statute so poorly worded that it violates due process by being unconstitutionally vague and failing to give taxpayers fair notice of their compliance obligations? On August 5, 2022, the Alaska Supreme Court overruled a lower court decision that had struck down as unconstitutionally vague a tax statute requiring that corporations incorporated in or doing business in a so-called “low-tax jurisdiction” be included in an Alaska combined return. The Court here found instead that the statute could “be given meaning in the adjudication process” and, therefore, could be constitutionally applied to the taxpayer. *State v. Nabors Int’l Fin., Inc. & Subsidiaries*, No. 7609 (Alaska Aug. 5, 2022). This case is a reminder to taxpayers that in addition

to the most discussed requirements for a state tax to pass constitutional muster (*i.e.*, substantial nexus, fair apportionment, non-discrimination, fair relation to the services provide by the state), a state tax may also be struck down on other constitutional grounds, such as if the tax is unconstitutionally vague.

**The Facts:** Within an international conglomerate of corporations, Nabors International Finance, Inc. (“Nabors”) was the parent company of the U.S. group and provided oil field services throughout the world, including in Alaska. Nabors was audited by the Alaska Department of Revenue for the tax years 2007 through 2010. The Department included in Nabors’ Alaska combined return the income of its affiliated corporations that were incorporated or doing business in so-called “low-tax jurisdictions.”

The statute in question stated that a corporation incorporated or doing business in a so-called “low-tax jurisdiction” must be included in the combined return if “(A) 50 percent or more of the sales, purchases, or

payments of income or expenses, exclusive of payments for intangible property, of the corporation are made directly or indirectly to one or more members of a group of corporations filing under the water’s edge combined reporting method; (B) the corporation does not conduct significant economic activity.” Alaska Stat. § 43.20.145(a) (5). The lower court ruled that the missing conjunction in the statute (*i.e.*, either “and” or “or”) between (A) and (B) rendered the statute unconstitutionally void for

vagueness. That is, the lower court reasoned, the statute was invalid because it failed to indicate whether **either** (A) or (B) or **both** (A) and (B) were required for the company to be included in the combined return.

**The Court here found instead that the statute could “be given meaning in the adjudication process” and, therefore, could be constitutionally applied to the taxpayer.**

**The Decision:** The Alaska Supreme Court overruled the lower court and found that “a reviewing court could consider the statute’s language, legislative history, and purpose to determine the proper interpretation.” Analyzing those factors here, the Court concluded that the statute at issue had a “reasonably clear meaning” and that was that (A) and (B) should be read disjunctively, that is a company should be included in the combined return if it satisfied either (A) or (B). Nabors further argued that the requirement in (B) that the company “does not conduct significant economic activity” was itself unconstitutionally vague because the statute did not define “significant economic activity.” The Court also rejected this argument finding that the Alaska Administrative Code defines “does not conduct significant economic activity” and “[i]f a taxpayer is unsure which affiliates to include, it can request guidance from the Department.” Finally, the Court rejected Nabors’ alternative arguments that the statute discriminated against foreign commerce in violation of the Foreign Commerce Clause and that the statute was irrational and violated Nabors’ substantive due process rights. □

## What's Shaking: Blank Rome's 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.

### **29th Annual Paul J. Hartman State and Local Tax Forum**

- ▶ [Craig B. Fields](#) and [Nicole L. Johnson](#) will speak at Vanderbilt University Law School's 29th Annual Paul J. Hartman State and Local Tax Forum, being held October 19 through 21, 2022, in Nashville, Tennessee. There will also be a virtual option available for all program sessions. Craig will speak on the "Leading Practices in Audits, Assessments, and Alternative Dispute Resolutions" panel, taking place Wednesday, October 19. Nicole's session, "Allocable Income," will take place the next day, Thursday October 20. To learn more, please click [here](#). □

### **Council On State Taxation's North Atlantic Regional State Tax Seminar**

- ▶ [Craig B. Fields](#), [Eugene J. Gibilaro](#), [Nicole L. Johnson](#), and [Mitchell A. Newmark](#) will speak at the Council On State Taxation's North Atlantic Regional State Tax Seminar being held on September 20, 2022, from 8:30 a.m. to 3:30 p.m. EDT, in Blank Rome LLP's New York office. The seminar will provide updates on significant state tax issues for the North-Atlantic States: Connecticut, Maine, Massachusetts, New Hampshire, New Jersey, New York, Rhode Island, and Vermont. To learn more, please click [here](#). □

### **New Jersey State and Local Tax Day**

- ▶ [Eugene J. Gibilaro](#) and [Mitchell A. Newmark](#) will speak at the New Jersey State Bar Association's New Jersey State and Local Tax Day being held September 15, 2022, via webinar. Mitchell and Eugene's topic is "State of the States Litigation." To learn more, please click [here](#). □