PwC's Law Firm Services News Alert

Missouri and Tennessee Adopt Market-based Sourcing; Connecticut Adds a Higher Personal Income Tax Bracket while Texas lowers the Franchise Tax Rate; a Georgia Tax Tribunal Permits Resident to Adjust Taxable Income for Taxes paid other States on Passthrough Income; Puerto Rico enacts a Value Added Tax Scheme

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July 22, 2015

Several states - Connecticut, Georgia, Missouri, Tennessee & Texas - and Puerto Rico have recently made changes to their local tax systems which have the potential to affect US law firms.

Connecticut

Retroactively effective to January 1st of this year, the personal income tax rate for high earners resident in Connecticut has been increased. Effective for taxable years beginning on or after January 1, 2015, the 6.7% personal marginal tax rate is increased to 6.9%. A seventh, higher income tax bracket has been added and is subject to a 6.99% marginal tax rate. Individuals earning more than $250,000 and married couples making more than $500,000 are taxed at 6.9% on the excess over these dollar limits. Individuals earning more than $500,000 and couples making more than $1 million are taxed at 6.99% on such excess amounts. In addition, Connecticut has added mandatory unitary combined reporting and filing, it will continue the state's income tax surcharge, and will limit the use of NOLs and tax credits. For more detailed information, please see:

Connecticut Update

Original Connecticut SALT Alert

Georgia

The Georgia Tax Tribunal issued a final consent order adopting a November 25, 2014 decision, holding that a Georgia taxpayer was entitled to adjust his federal adjusted gross income under O.C.G.A 48-7-27(d)(1) for his distributive share of income that was subject to Texas franchise tax and District of Columbia franchise tax imposed at the partnership level. Rosenberg v. Riley, Georgia Tax Tribunal, File No. 1414626, July 13, 2015.

Georgia taxpayers that receive income from flow-through entities, such as a law firm partnership, that are also subject to the Texas franchise tax, DC franchise tax, or any other entity level tax measured by income should determine whether they properly calculated their Georgia taxable income, taking into account the taxes paid to these, and possibly other, jurisdictions. Other states that impose entity level taxes that may qualify include Tennessee, Illinois, and New Hampshire. For more detailed information, please see:

Georgia Update

Missouri

Receipts from the sale of services into Missouri are subject to market-based sourcing under the new single sales factor apportionment provisions enacted in July 2013, which all taxpayers are eligible to elect. However, the state has yet to resolve the question of when the election becomes available to sellers of other than tangible personal property.

Because market based sourcing is applicable only within the new single sales factor election, sellers of services and intangibles should engage in a determination of the most beneficial apportionment method annually, comparing: (1) the standard 3 factor method under §32.200 RSMo (a cost of performance approach), (2) the old single factor sales method under §143.451.2(2) (a partially within or wholly within/without approach), or (3) the new single factor method under §143.451.2(3) (a market based sourcing approach). For more detailed information, please see:

Missouri Update

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Tennessee

In the Revenue Modernization Act (RMA) Tennessee has made several major changes to its tax system, including expanding the State's nexus standard for it gross receipts-based business tax. Law firms having systematic and continuous business activity in Tennessee that produces gross receipts attributable to customers in the State will be subject to taxation in Tennessee. In addition, a bright-line threshold has been enacted as part of the RMA, creating a clear line of demarcation as to when a law firm will have a taxable presence in Tennessee -- receipts in excess of $500,000 in Tennessee will establish this bright-line nexus. These provisions are effective for tax years beginning on or after January 1, 2016. The State has also implemented market based sourcing for services and intangibles. In order to be subject to tax in Tennessee, a taxpayer must have substantial nexus and be engaged in certain activities in the state. The RMA expands the definition of activities 'engaged in this state' to include the sale of a service delivered to a Tennessee location. For more detailed information, please see:

Tennessee Update

Texas

Texas has permanently reduced its Franchise Tax (Margin Tax) rates by 25% to 0.75% of taxable margin applicable to the provision of legal services. The reduction is applicable to tax reports originally due on or after January 1, 2016.

Prior to this change, the 2016 report year tax rates were due to revert to their general rates of 0.5% for retail or wholesale trade businesses and 1% for all other taxpayers. For reports due in 2015, the rates were temporarily reduced to 0.475% for retailers or wholesalers and 0.95% for other taxpayers. For more detailed information, please see:

Texas Update

Puerto Rico

Effective July 1, 2015, the Puerto Rico sales and use tax (SUT) rate has increased from 7% to 11.5%. Moreover, starting October 1, 2015, the SUT will have a broader base since certain services to other businesses and designated professional services will be subject to a 4% SUT -- including legal services.

Effective April 1, 2016, the SUT will be replaced with a Value Added Tax (VAT) regime. VAT will apply to the rendering of services by a nonresident to a resident of Puerto Rico. The VAT rate will be 10.5%, and the Municipal SUT (1%) will continue to apply. Rendering services for export, i.e., a Puerto Rico firm rendering services for a nonresident client, will be exempt from VAT. For more detailed information, please see:

Puerto Rico Update

Contact PwC's Law Firm Services for further details

PwC can assist your firm in evaluating the potential impact of these changes in state and Puerto Rico tax law. Please give us a call to start the conversation.

Gary M. Pogharian at +1 (646) 471-7202 or gary.m.pogharian@us.pwc.com

Gregg Sincoff at +1 (646) 471-1335 or gregg.sincoff@us.pwc.com

Nancy Regan at +1 (973) 236-5771 or nancy.regan@us.pwc.com

or any member of your PwC Law Firm Services team