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# THE BR STATE + LOCAL TAX SPOTLIGHT

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# Note from the Editors

By Joshua M. Sivin and Melanie L. Lee

**Welcome to the December 2023 edition of *The BR State + Local Tax Spotlight.*** We know the importance of remaining up-to-date on State + Local Tax developments, which appear often and across numerous jurisdictions. Staying informed on significant legislative developments and judicial decisions helps tax departments function more efficiently, along with improving strategy as well as planning. That is where *The BR State + Local Tax Spotlight* can help. In each edition, we will highlight important State + Local Tax developments that could impact your business. In this issue, we will be covering:

- New Jersey Agency Required to Honor its Deal and Allow $26 Million in Tax Credits
- State Tax vs. Local Tax – Is there a Difference?
- New York ALJ Holds That Convenience of Employer Rule Applies Despite Covid Lockdowns
- A Lack of Transparency: Minnesota Edition

**A Holiday Note**: As we reflect upon the year, we are filled with gratitude for our readership and for the collaborative efforts of our team and the Blank Rome staff who make every issue of *The BR State + Local Tax Spotlight* a far-reaching success. We wish you and yours a joyous holiday season and endless health and happiness for the new year.

**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.**

## Co-Editors, *The BR State + Local Tax Spotlight*


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CRAIG B. FIELDS
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# New Jersey Agency Required to Honor its Deal and Allow $26 Million in Tax Credits

By Craig B. Fields

The Superior Court of New Jersey, Appellate Division, required the New Jersey Economic Development Authority ("EDA") to "turn square corners" and certify $26 million in tax credits pursuant to its contract with a company despite some issues with the company's application for the credits. *Holtec International v. New Jersey Economic Development Authority*, Docket No. A 1477-21 (Nov. 30, 2023).

**Facts**: In 2014, the EDA awarded Holtec International $260 million in tax credits over a ten-year period to induce the company to build a new technology campus in Camden. Holtec built the facility, and the EDA initially certified the tax credits on which Holtec had relied in building the facility.

In 2019, the Office of the State Comptroller issued a report asserting that Holtec misrepresented facts in its application and criticized the EDA for its lack of diligence in enforcing the tax incentive program. The EDA then refused to certify $26 million in tax credits for the 2018 tax year, asserting that Holtec had not disclosed on its application a ten-day debarment by the Tennessee Valley Authority and had misrepresented an incentive proposal from South Carolina to locate there.

**Decision**: The Court found that Holtec's failure to disclose the debarment was not grounds to void the contract. First, prior to Holtec's application, the EDA was on notice by several other applicants of problems with the contract application form. Moreover, it was shown that applications were granted to companies with histories of far more serious transgressions. One EDA employee acknowledged during a public hearing "that based on the twenty-five memoranda he drafted, nothing 'short of death' would 'constitute [] an outlier for the purpose of EDA disqualifications for tax incentives.'" Finally, the Tennessee debarment was publicly reported and available on the Internet.

> **Given the application form deficiencies and the manner in which the EDA oversaw the application process, Holtec's omission on its initial application did not constitute a material misrepresentation that would warrant rescinding the award of the tax credits.**

The Court then held that the information provided about South Carolina offering Holtec free land to locate there was not grounds to void the contract. Holtec had explicitly referred to land costs as assumptions and the EDA did not request any additional documentation regarding the land costs. Indeed, EDA's own employees testified that they did not press applicants for written offers from other states as the EDA did not want to encourage applicants to engage in further dialogue with other states.

The Court concluded that recission of the contract was not an appropriate remedy as Holtec had relied on the tax credits in deciding to make a very significant investment in New Jersey: "rescinding tax credits to a company that dutifully fulfilled its agreement to make substantial investments in Camden—an economically disadvantaged city—would hardly be equitable considering all relevant circumstances."

**EUGENE J. GIBILARO**
PARTNER

# State Tax vs. Local Tax – Is there a Difference?

By Eugene J. Gibilaro

Must a state tax and a local tax be considered together when determining whether either of them pass constitutional muster? In a recent decision, the Pennsylvania Supreme Court said "no" and determined that the City of Philadelphia was only required to provide income tax credits to Philadelphia residents for similar income taxes that they paid to other localities, but was not required to provide income tax credits to Philadelphia residents for income taxes paid to other states. *Zilka v. Tax Review Board City of Philadelphia*, Nos. 20 EAP 2022 & 21 EAP 2022 (Nov. 22, 2023).

**Facts**: The case involved a Philadelphia resident, Diane Zilka, who worked exclusively in Wilmington, Delaware. Zilka was subject to four income taxes: (1) Delaware state income tax; (2) Wilmington local income tax; (3) Pennsylvania state income tax; and (4) Philadelphia local income tax. When Zilka filed her Pennsylvania state income tax return, she claimed a credit for the income tax that she had paid to Delaware, though Zilka was not able to utilize as a credit the entire amount of income tax that she paid to Delaware, as Delaware had a higher tax rate. When Zilka filed her Philadelphia local income tax return, she claimed a credit for the income tax that she paid to Wilmington, though Zilka owed additional Philadelphia income tax even after utilizing the entire amount of the credit for income tax paid to Wilmington, as Philadelphia had a higher tax rate. Zilka argued that Philadelphia was constitutionally required to provide her with an additional credit to the extent of the amount of the remaining Delaware state income tax credit that Zilka was not able to utilize on her Pennsylvania state income tax return.

**Decision**: While Zilka asserted that a taxpayer's state and local tax burdens must be aggregated in determining whether either tax violates the dormant Commerce Clause of the U.S. Constitution, the Court disagreed, finding that state and local taxes need only be aggregated when a court determines that a purported local tax is actually "a state tax masquerading as a local tax," and is not "truly a local tax."

> **The Court then concluded that the Philadelphia local income tax was "truly a local tax" because it "was enacted by Philadelphia's City Council and is collected by the City's Department of Revenue solely for the benefit of the City and its citizenry.**

Considering the burden of the Philadelphia local income tax on a standalone basis, the Court had little trouble finding that the tax was both internally and externally consistent. The tax was internally consistent because if every local jurisdiction imposed the same taxing scheme, residents and nonresidents working in each locality would pay the same amount of local income tax (i.e., with nonresidents working in different localities receiving a credit from their locality of residence). The tax was externally consistent because Philadelphia had not taxed more than its fair share by providing Zilka with a 100% credit for the taxes she paid to Wilmington. Finally, the Court observed that the additional tax burden for Zilka was the result of Delaware having a higher tax rate than Pennsylvania and "'tax schemes that create disparate incentives to engage in interstate commerce (and some-times result in double taxation) only as a result of the interaction of two different but nondiscriminatory and internally consistent schemes' are not unconstitutional."

JOSHUA M. SIVIN
OF COUNSEL

# New York ALJ Holds That Convenience of Employer Rule Applies Despite Covid Lockdowns

By Joshua M. Sivin

In the latest but likely not final chapter of Professor Zelinsky's ongoing challenge to New York's convenience of the employer rule, a New York Administrative Law Judge (ALJ) upheld application of the rule, counting days the Professor worked at his home in Connecticut for his New York employer as New York workdays, even during the over nine-month period when the employer's New York campus was closed as a result of Covid restrictions. *In the Matter of Petition of Zelinsky*, DTA Nos. 830517 and 830681 (November 30, 2023).

**Facts**: Professor Edward Zelinsky, a tax professor at Cardozo School of Law, located in New York, sought refunds of taxes paid to New York for days he worked from his home in Connecticut for tax years 2019 and 2020, including for days when the law school was closed due to Covid restrictions. New York's Governor issued an order in March 2020 requiring that businesses use remote work to the maximum extent possible. In compliance with the order, Cardozo closed its doors to all in-person activity, and Professor Zelinsky exclusively worked from his home in Connecticut from March 16, 2020 through the remainder of the year. In denying Professor Zelinsky's refund claim, the Division of Taxation relied on the so-called convenience of the employer rule, which states that "any allowance claimed for days worked outside New York State must be based upon the performance of services which of necessity, as distinguished from convenience, obligate the employee to out-of-state duties in the service of his Employer." Professor Zelinsky had previously challenged the convenience of the employer rule on constitutional grounds decades earlier, and New York's highest court upheld application of the rule. *Zelinsky v Tax Appeals Trib.*, 1 NY3d 85 (2003), *cert denied* 541 US 1009 (2004).

**Decision**: For 2019, because the parties stipulated that Professor Zelinsky's work situation was the same as it was for his prior challenge, the ALJ found that the Court of Appeals decision from 2003 was determinative. For 2020, the ALJ acknowledged that "[a]s the facts and effects of the COVID-19 pandemic are unprecedented," the issue of whether the convenience of the employer rule applied was one of first impression. Nonetheless, the ALJ determined that the rule applied to Professor Zelinsky and was not unconstitutional. The ALJ found that the fact that Cardozo "did not provide accommodations but instead allowed petitioner to work out-of-state at home does not constitute necessity or requirement by Cardozo… [and] Professor Zelinsky failed to meet his burden that he worked out-of-state due to his employer's necessity." The ALJ further found that accepting Professor Zelinsky's arguments would "result in special tax benefits to those who do not live in New York, but nonetheless work for, and benefit from, a New York employer."

> **The ALJ concluded that Professor Zelinsky's virtual presence in New York was sufficient under the Constitution to allow New York to tax him for days he worked in Connecticut, citing the *Wayfair* decision.**

*(continued on page 4)*

**Take Aways**: The ALJ appeared to focus on the wrong question—*i.e.*, whether Cardozo required Professor Zelinsky to work from Connecticut—rather than on whether Professor Zelinsky was permitted to work at his office in New York. If viewed from the latter standpoint, it becomes clear that because Professor Zelinsky was prohibited from working from his office in New York, the days he worked from home in Connecticut should not be sourced to New York. Furthermore, the ALJ's reliance on *Wayfair* was questionable as *Wayfair* was not an income tax case and merely held that in the sales tax context, physical presence is not required in order to require a remote seller to withhold sales tax. Professor Zelinsky has already indicated that he intends to appeal the determination, so there will likely be more to this story.

**NICOLE L. JOHNSON**
PARTNER

# A Lack of Transparency: Minnesota Edition

By Nicole L. Johnson

Taxpayers and practitioners are often stymied by the lack of clarity or other information provided by state departments of revenue on tax issues. While the limited information can be understandable when a department does not want to be shoehorned into a position, it does not lessen the frustration. That same frustration was highlighted by the Minnesota Supreme Court in a recent decision.

In *Cities Management, Inc. v. Commissioner of Revenue*, the taxpayer was challenging the Commissioner's treatment of goodwill as apportionable income. Docket No. A23-0222 (Minn. Nov. 22, 2023). The taxpayer relied on a prior Minnesota Tax Court decision that held the sale of goodwill is nonbusiness income. *See Nadler v. Comm'r of Revenue*, No. 7736 R (Minn. Tax Ct. 2006). The Commissioner did not appeal the *Nadler* decision. Nevertheless, the Commissioner's internal policy was to not follow the *Nadler* decision. However, the Commissioner did not make that internal policy decision public until 2017—over 10 years after the decision in *Nadler.*

Egregiously, penalties were imposed on the taxpayer during the audit for following the *Nadler* decision. The Commissioner reversed those penalties on administrative appeal finding that there was reasonable cause for the taxpayer's position.

One of the issues in the *Cities* case was whether the Commissioner was bound by prior Tax Court decisions that were not appealed. The Minnesota Supreme Court noted that it was "troubled by the Commissioner's conduct" and that the Commissioner's actions "do little to inspire the trust and confidence of taxpayers in Minnesota's tax system." Nevertheless, the Court declined in the *Cities* case to determine whether the Commissioner was bound by unappealed decisions.

While the majority did not rule on the issue, the dissent in *Cities* provided a very reasonable resolution. Specifically, the dissent proposed a rule that the Commissioner be "bound by tax court decisions that are not appealed unless the Department of Revenue provides public notice of its disagreement with the tax court opinion." Such a level-headed approach would prevent taxpayers from being blindsided by hidden determinations of the Department.

Unfortunately for taxpayers, the majority's admonishment of the Commissioner's actions—while satisfying to read—does little to encourage the Department to be more forthright with their positions. Taxpayers should not be left to guess what the Department's position is on an issue for which there is a court decision.

> **Although this remains an open issue in Minnesota, hopefully other departments—or legislatures—will see the logic of the dissent's proposed rule and implement it.**

# 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.

### The 2024 National Multistate Tax Symposium

- Blank Rome State + Local Tax partner Craig B. Fields will serve as a speaker for the 2024 National Multistate Tax Symposium in a session titled "Alternative Apportionment and Forced Combination – Dishing on the Latest," being held February 9, 2024, in Orlando, Florida.





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