This Week in State Tax (TWIST)

August 3, 2026

Massachusetts: Appellate board holds that Finnigan apportionment rule runs afoul of P.L. 86-272

The Massachusetts Appellate Tax Board recently addressed whether a taxpayer and certain affiliates were properly classified as manufacturing corporations for corporate excise tax purposes as well as the manner in which the Massachusetts *Finnigan*-style reallocation rule interacts with P.L. 86-272. The taxpayer's operating structure included manufacturing affiliates that produced and processed pork products, and sales companies responsible for customer-facing activities related to selling those products. For Massachusetts apportionment purposes, the taxpayer treated the entities processing the meat products as qualified manufacturers, while treating the affiliated sales companies as non-manufacturing corporations. One of the sales corporations included in the Massachusetts combined group was an entity protected under the provisions of P.L. 86-272. On audit, the Commissioner of Revenue aggregated the activities of the sales companies with those of the manufacturing entity, reclassifying the sales companies as manufacturers per relevant regulations. Moreover, the Commissioner used the "reallocation rule" to reassign portions of the Massachusetts receipts generated by the P.L. 86-272-protected sales corporation to the sales factor numerators of other combined group members that were taxable in Massachusetts. The taxpayer challenged these assessments, and the matter was taken to the Board.

During the tax years at issue, Massachusetts required qualifying manufacturing corporations to use single-sales-factor apportionment, while non-manufacturers used a three-factor formula. [Note: The general Massachusetts apportionment for all entities is now single sales factor.] The taxpayer challenged the Commissioner's application of the state's "combination rule," which treats the manufacturing and selling activities of related combined group members together when property manufactured by one member is sold by another to third parties. The Board upheld the regulation and its application to the taxpayer, concluding that the regulation reasonably coordinated Massachusetts' combined reporting rules with the statutory apportionment provisions for manufacturers. The Board found it reasonable to attribute the manufacturers' apportionment characteristics to the selling entities when those entities later sold the manufactured products to third parties because intercompany sales by the manufacturing members were eliminated from the apportionment factor. The Board further emphasized that each entity was still required to independently satisfy the manufacturing substantiality tests; the regulation merely attributed certain manufacturing-related sales and apportionment characteristics to the selling entities for purposes of determining whether the single factor manufacturer apportionment rule applied.

The Massachusetts reallocation rule, to which the Board next turned, is a *Finnigan*-style apportionment provision under which each taxable member of a unitary group is required to increase the numerator of its sales factor by its proportionate share of the aggregate Massachusetts sales of nontaxable members of the group, which in this

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case was the P.L. 86-272-protected entity. The Board framed the central question as whether Massachusetts could, consistent with P.L. 86-272 and the Supremacy Clause, include the protected entity's Massachusetts sales in the numerator of the sales factor of other group members when the protected entity itself could not be taxed on its net income. The Board held that the "person" protected by P.L. 86-272 is the specific corporation whose activities are being evaluated and P.L. 86-272 protects that corporation's net income (not just the entity itself) from state income taxation when the in-state activities of the entity do not exceed protected solicitation. In the Board's view, Massachusetts could not accomplish indirectly that which is prohibited by P.L. 86-272 by reallocating the protected entity's Massachusetts sales to other taxable group members and including those receipts in their sales factor numerators. Doing so would have the effect of taxing the protected entity's income in contravention of federal law. In its analysis, the Board reviewed cases from several other states and found them not persuasive as to the matter before them or not relevant as not involving a P.L. 86-272-protected entity.

Please contact James Carregal and Jenny Ek with questions about *Smithfield Packaged Meats Corp. v. Commissioner of Revenue*, No. C344811.