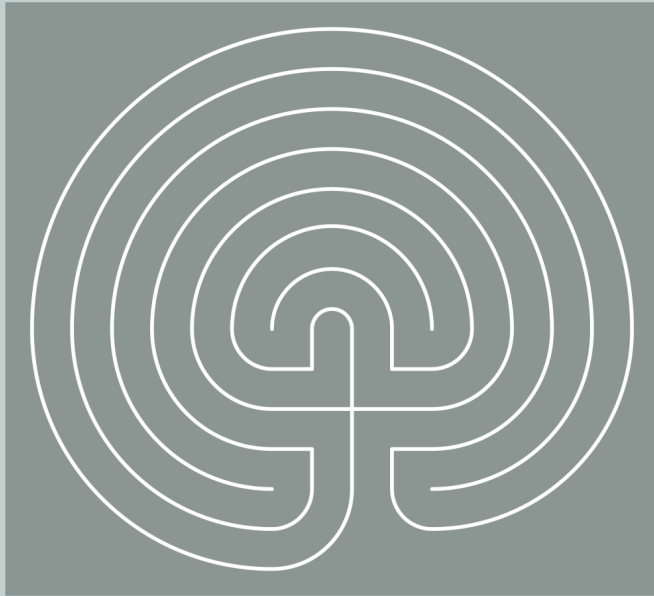


# Out of the Franchise Tax Labyrinth



*TTARA Annual Meeting 2011*

**Jennifer Patterson Rabb**  
**Winstead PC**

# Into the Labyrinth...



# Into the Labyrinth...

## Objectives of the margin tax

- More revenue
- Fair distribution of the tax burden
- End the Delaware sub

# Into the Labyrinth...

**Problem:** Bullock Amendment

# Into the Labyrinth...

## **Problem:** Bullock Amendment

"a tax on the net incomes of natural persons, including a person's share of partnership... income"

# Into the Labyrinth...

**Problem:** Bullock Amendment

"a tax on the net incomes of natural persons, including a person's share of partnership... income"

**Solution:** Invent a Business Tax

- Not an income tax
- Not on natural persons

# Into the Labyrinth...

**Problem:** Not very much time

# Into the Labyrinth...

**Problem:** Not very much time

**Solution:** Hurry



# Into the Labyrinth...

**Problem:** Not very much time

**Solution:** Hurry

**Problem:** Is it constitutional?

# Into the Labyrinth...

**Problem:** Not very much time

**Solution:** Hurry

**Problem:** Is it constitutional?

**Solution:** Original jurisdiction in the Supreme Court

*Ruling by the 120<sup>th</sup> day*

# Inside the Labyrinth...

- **Revenue shortfall**
- **Some unfair, unfixable outcomes**
- **Many questions, few answers**
- **Constitutional challenges**

# Constitutional Challenges

## ***In re Allcat Claims Service LP and John Weakly***

Filed: July 29, 2011

Oral argument: October 24, 2011

120<sup>th</sup> day: November 26, 2011

Issue: Bullock Amendment

## ***In re Nestle USA, Switchplace LLC, and NSBMA LP***

Filed: October 19, 2011

Oral argument: January 12, 2012

120<sup>th</sup> day: February 16, 2012

Issues: Equal & Uniform  
Taxation and issues under  
the U.S. Constitution

# Out of the Labyrinth...

# Out of the Labyrinth...

- Almost any decision that gives new information about constitutional limitations would be helpful

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  - Meaning of the Bullock Amendment
  - Requirements for Equal and Uniform Taxation

# Out of the Labyrinth...

- Almost any decision that gives new information about constitutional limitations would be helpful
  - Meaning of the Bullock Amendment
  - Requirements for Equal and Uniform Taxation
- But new information is not a certainty...



# A Surprise Constitutional Issue

# A Surprise Constitutional Issue

Does the Texas Supreme Court have jurisdiction to decide the constitutionality of the margin tax in an original proceeding?

*"The supreme court has exclusive and original jurisdiction over a challenge to the constitutionality of this Act and may issue injunctive or declaratory relief in connection with the challenge."*

*H.B. 3, SECTION 24 (79<sup>th</sup> Leg., 3<sup>rd</sup> C.S.)*

# Out of the Labyrinth...

What will we learn from *Allcat* and *Nestle*? What will be the ramifications?



# Out of the Labyrinth...



What will we learn from *Allcat* and *Nestle*? What will be the ramifications?

- **Jurisdiction**

- Bullock Amendment
- Equal & Uniform Taxation
- Relief

# Out of the Labyrinth...

Does the Supreme Court have original jurisdiction?



# Out of the Labyrinth...

Does the Supreme Court have original jurisdiction?

Yes: Decision on the merits soon.



# Out of the Labyrinth...

Does the Supreme Court have original jurisdiction?

Yes: Decision on the merits soon.

No: Plaintiffs must go to district court.



# Out of the Labyrinth...



What will we learn from *Allcat* and *Nestle*? What will be the ramifications?

- Jurisdiction
- Bullock Amendment**
- Equal & Uniform Taxation
- Relief



# Out of the Labyrinth...

Is the margin tax subject to the Bullock Amendment?  
And what do we learn?



# Out of the Labyrinth...



Is the margin tax subject to the Bullock Amendment?  
And what do we learn?

Yes: Tax is unconstitutional for margin attributed to natural-person partners.  
*Beyond that, it depends*

# Out of the Labyrinth...



Is the margin tax subject to the Bullock Amendment?  
And what do we learn?

Yes: Tax is unconstitutional for margin attributed to natural-person partners.  
*Beyond that, it depends*

No: *It depends.*

# What do we learn from a decision on the Bullock Amendment issue?

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A tax on net income: Not much.

# What do we learn from a decision on the Bullock Amendment issue?

"a tax on the net incomes of natural persons, including a person's share of partnership... income"

A tax on net income: Not much.

A tax on income *of natural persons*:

A tax on a partnership is or is not a tax on the partners.

*Not so fast!*



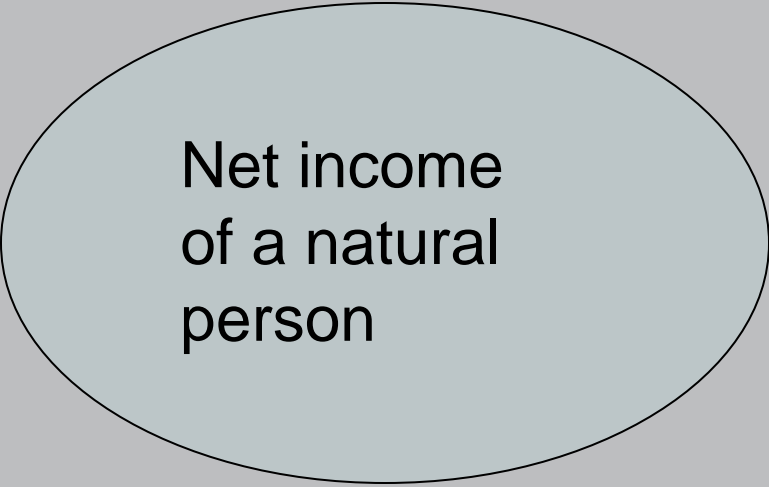
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# Consider the Rules of Construction

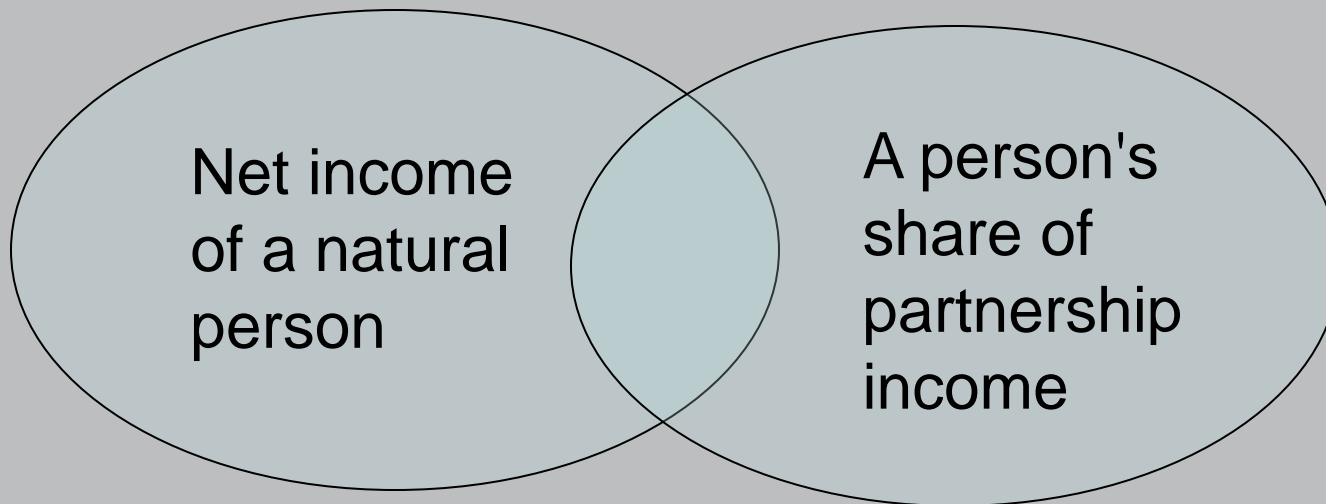
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Net income  
of a natural  
person

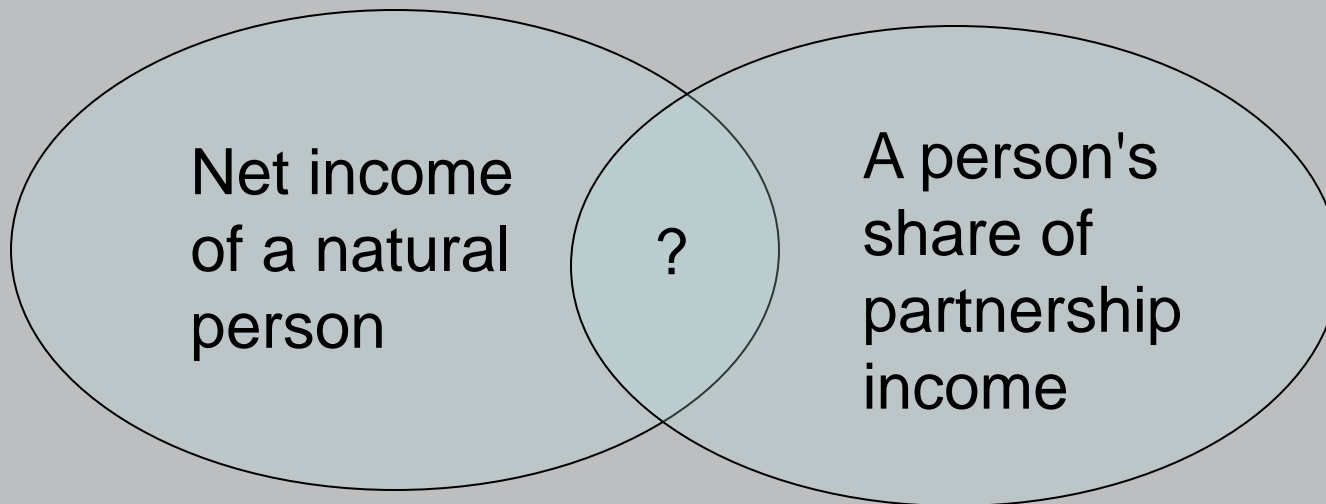
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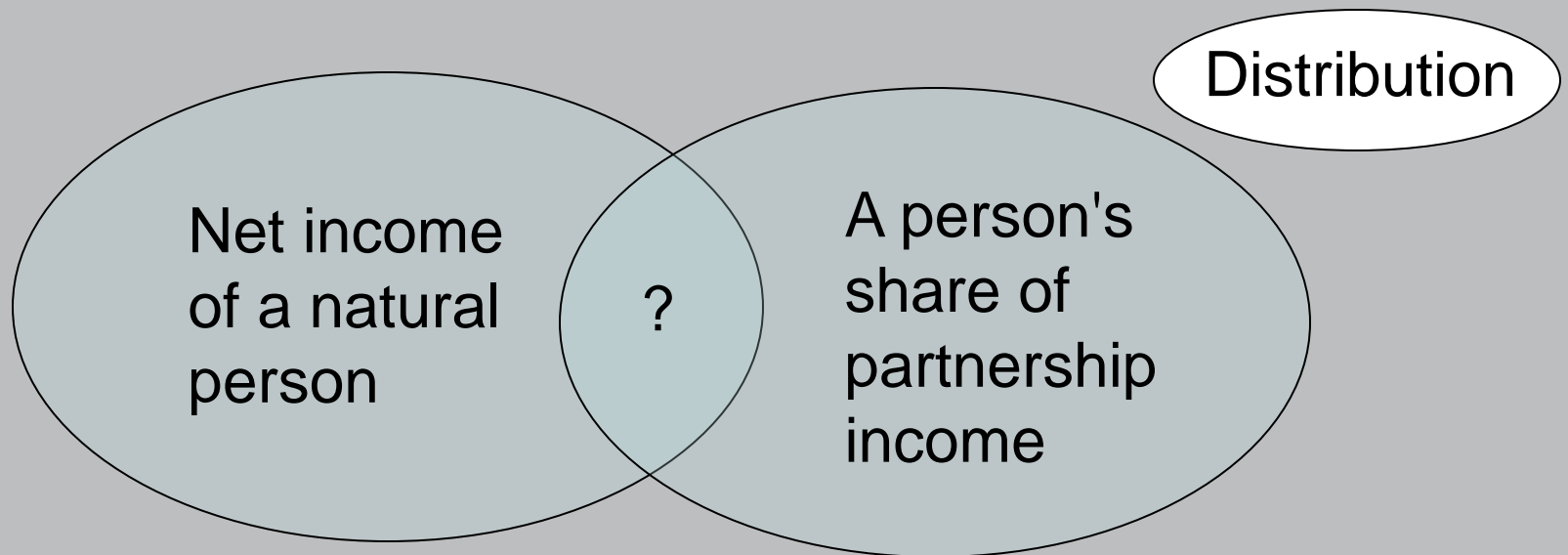
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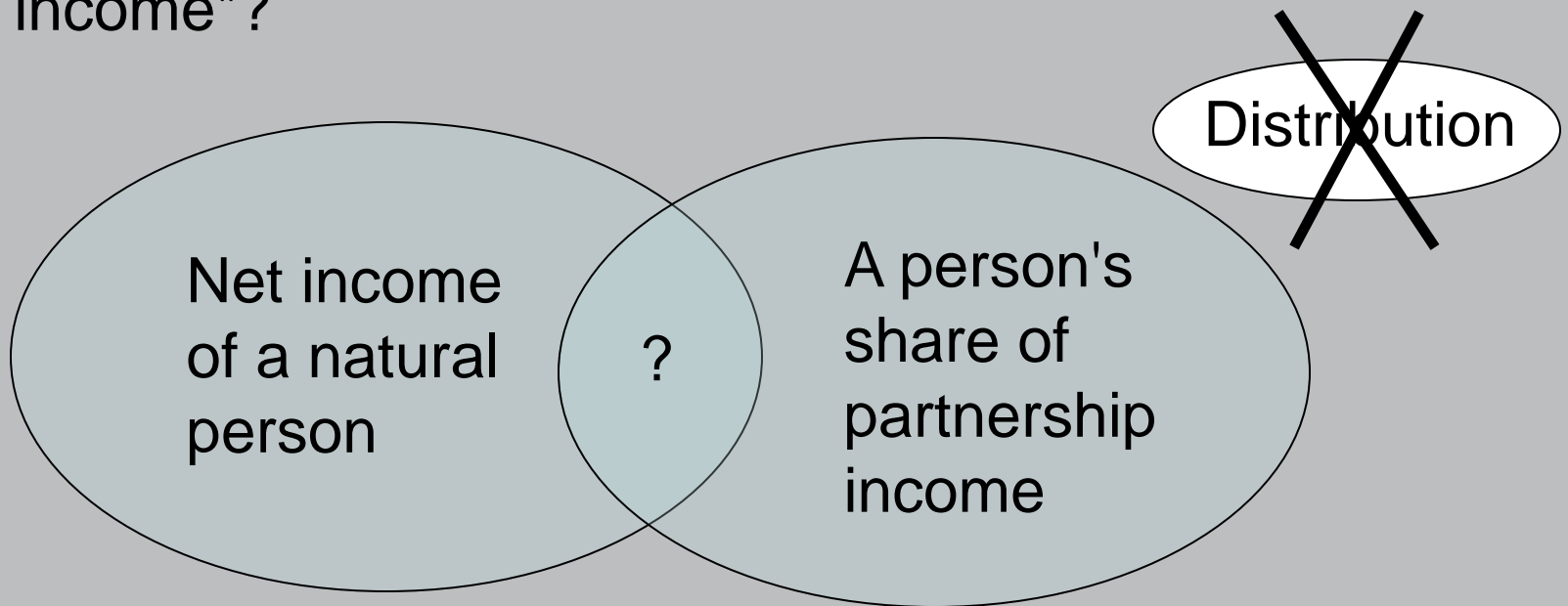
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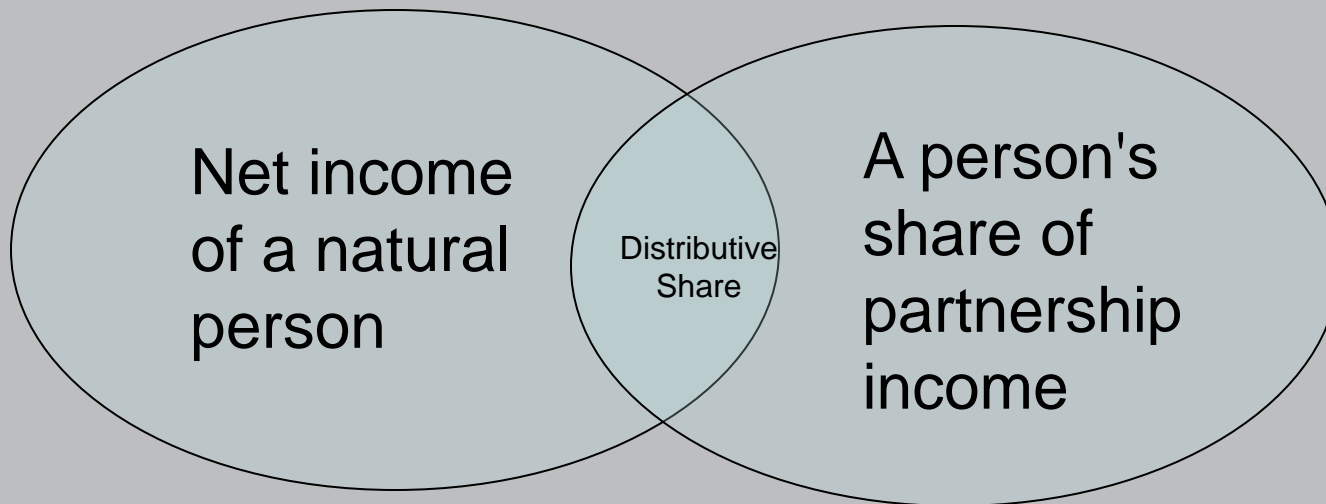
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# Consider the Rules of Construction

What is both "a tax on the net incomes of natural persons" and "a person's share of partnership income"?





# Out of the Labyrinth...

What do we learn from the Bullock Amendment issue?

If margin is not income:

Not much

If not on natural persons:

Tax on partnerships is safe.

If tax on partner's distributive share is tax on partner:

Tax on partnerships is subject to referendum.



# Out of the Labyrinth...



What will we learn from *Allcat* and *Nestle*? What will be the ramifications?

- Jurisdiction
- Bullock Amendment
- Equal & Uniform Taxation**
- Relief

# Out of the Labyrinth...

Does the Margin Tax satisfy the Equal & Uniform Clause?



# Out of the Labyrinth...

Does the Margin Tax satisfy the Equal & Uniform Clause?

- Franchise tax is imposed for the privilege of doing business.



# Out of the Labyrinth...



Does the Margin Tax satisfy the Equal & Uniform Clause?

- Franchise tax is imposed for the privilege of doing business.
- To be equal and uniform, the tax must be commensurate with the value of the privilege.

# Out of the Labyrinth...

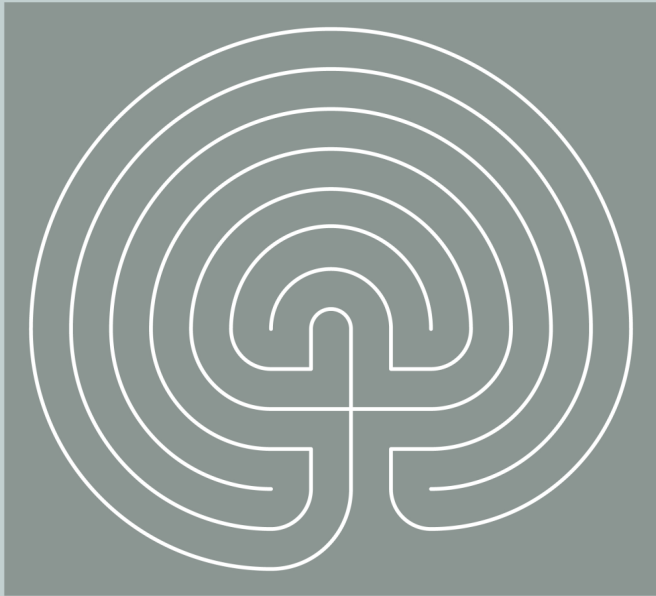
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# Out of the Labyrinth...

Does the Margin Tax satisfy  
the Equal & Uniform Clause?

Yes: \_\_\_\_\_



# Out of the Labyrinth...



Does the Margin Tax satisfy the Equal & Uniform Clause?

Yes: \_\_\_\_\_

No: Back to the drawing board. See decision in *Allcat*.



# Out of the Labyrinth...



What will we learn from *Allcat* and *Nestle*? What will be the ramifications?

- Jurisdiction
- Bullock Amendment
- Equal & Uniform Taxation
- Relief**

# Out of the Labyrinth...

If the Margin Tax is unconstitutional in any respect, what relief will the court grant?



# Out of the Labyrinth...



If the Margin Tax is unconstitutional in any respect, what relief will the court grant?

Retroactive

*or*

Prospective only

# Constitutional Challenges

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