Current Tax Developments Across the States

TTARA Annual Meeting
Austin, TX
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www.cost.org

Agenda

- COST/STRI/EY FY 2018 State and Local Business Tax Burden Study
- Due Process & Nexus Case Developments
- Other U.S. Supreme Court Cases of Interest
- State Response to Federal Tax Reform
- Combined Unitary Reporting
- Sourcing of Receipts
- Other GRT and Corporate Income Tax Issues to Watch
- Sales and Use Tax Case Developments
- *Qui Tam* Actions
- Treasury Offset Program
- Property Tax Scorecard

FY 2018 State and Local Business Tax Burden Study

October 2019

How Much Do Businesses Pay?

- Businesses paid more than $781 Billion in U.S. state and local taxes in FY 18, an increase of 6.1% from FY 17
- State business taxes increased by 7.1% and local business taxes grew by 5.1%
- In FY18, business tax revenue accounted for approximately 43.5% of all state and local tax revenue.
- Remarkably, the business share of SALT nationally has been within approximately **1% of 45% since FY 2003**
- Moreover, C Corporations on average pay about three-fifths more in income tax than pass through businesses
- **Severance taxes increased from $8.9 billion in FY2017 to $12.7 billion in FY2018, an increase of nearly 42.2%**.

Sources:
Total State and Local Business Taxes: State-by-State Estimates for Fiscal Year 2018, study prepared by Ernst & Young LLP for the State Tax Research Institute and the Council On State Taxation (Release Pending)
COST/PWC Study, Corporate and Pass-Through Business State Income Tax Burdens, October 2017

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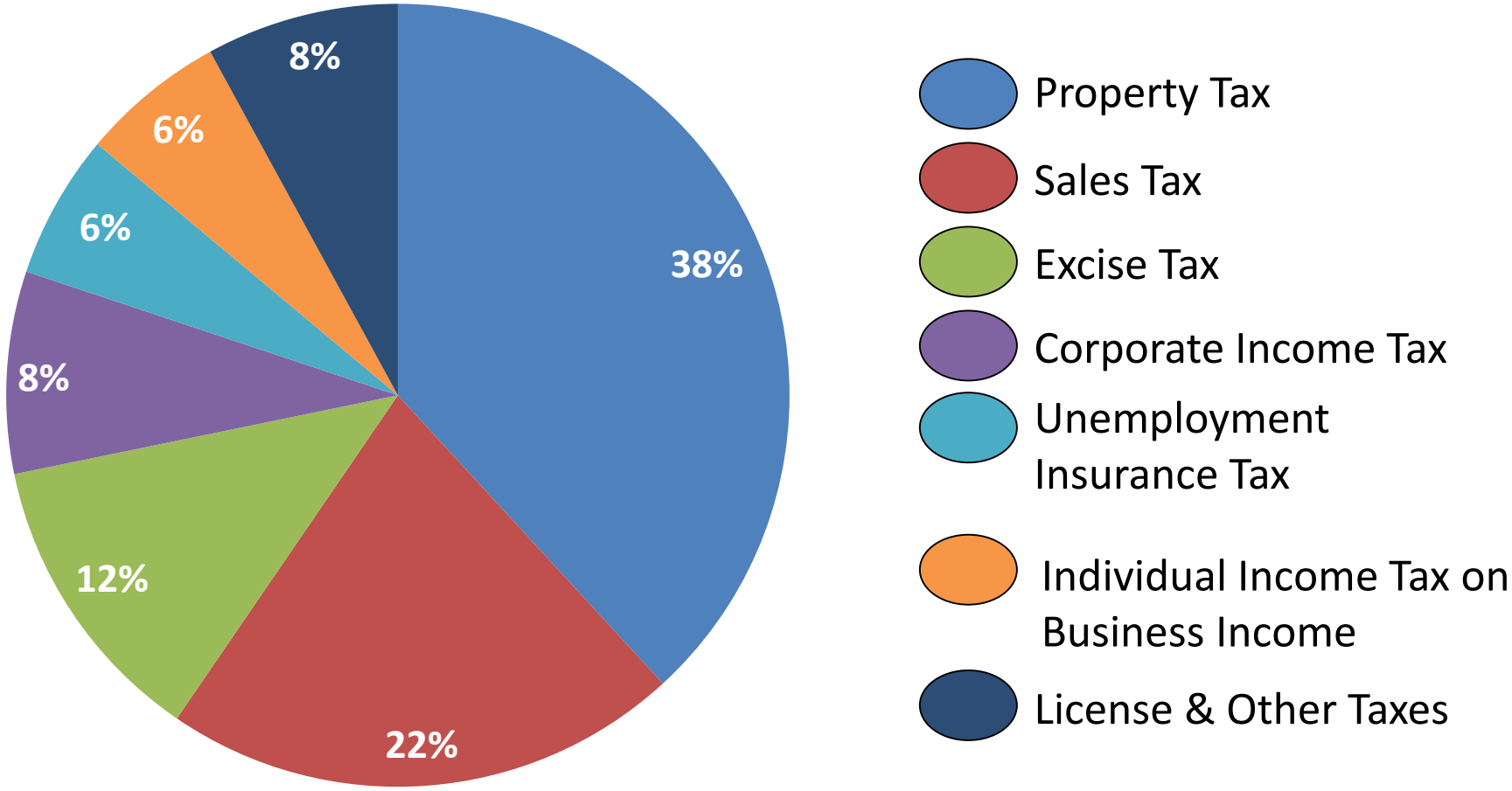
OVERALL STATE AND LOCAL TAX REVENUE



Source: Total State and Local Business Taxes: State-by-State Estimates for Fiscal Year 2018, study prepared by Ernst & Young LLP for the State Tax Research Institute and the Council On State Taxation (October 2019)

Due Process & Nexus Developments

Which of the following best describes the U.S. Supreme Court's holding in *Wayfair*?

A. The Court held that South Dakota's law was constitutional.

B. The Court overruled *Quill*'s physical presence rule, replacing it with an economic and virtual presence test.

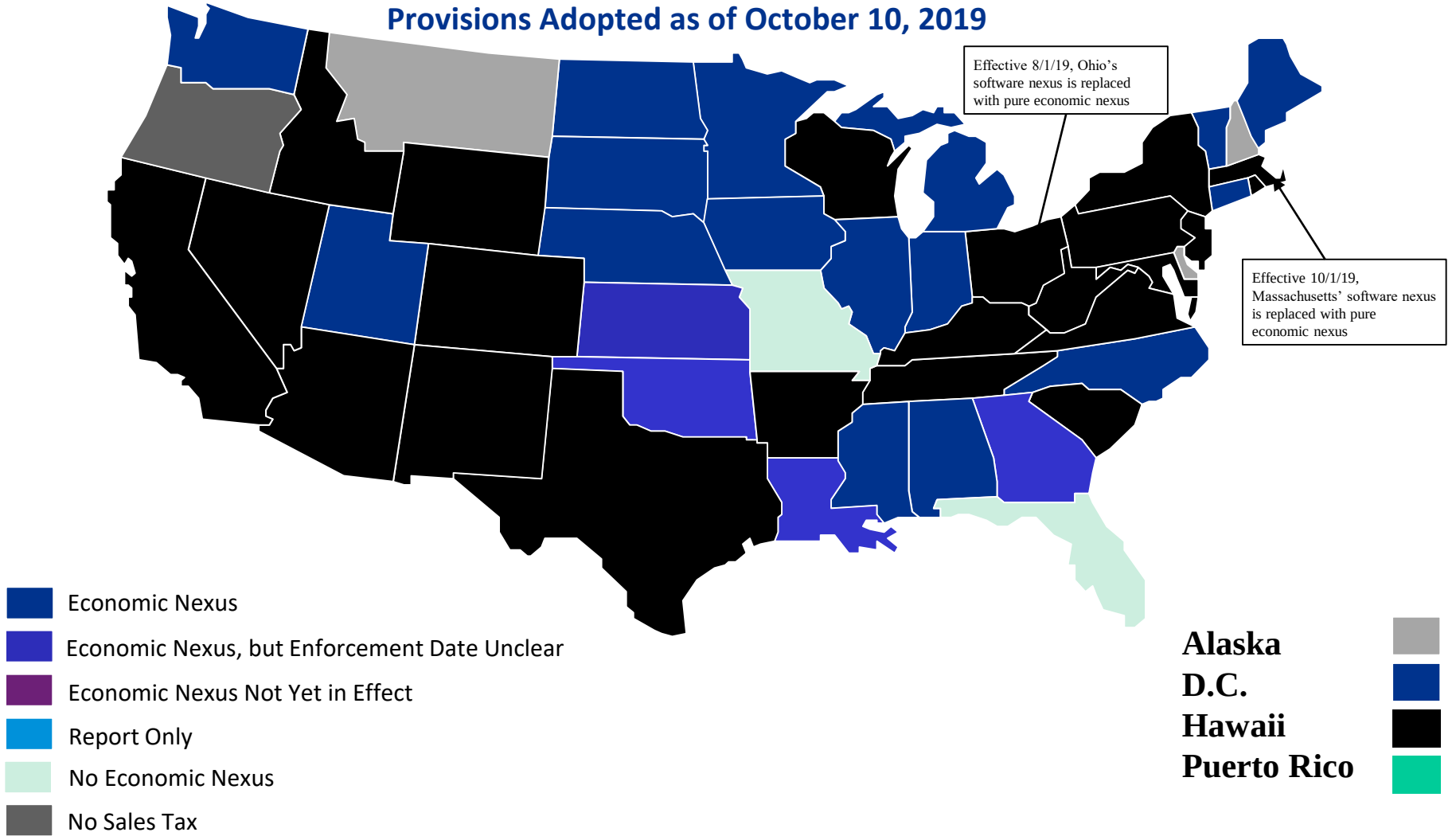
C. The Court ruled that remote sellers and marketplace facilitators must collect state sales taxes.

D. The Court ruled that, in order to collect sales tax, a state must enact an economic threshold, not make it retroactive, and enact *some* level of simplification.

The *Wayfair* Decision

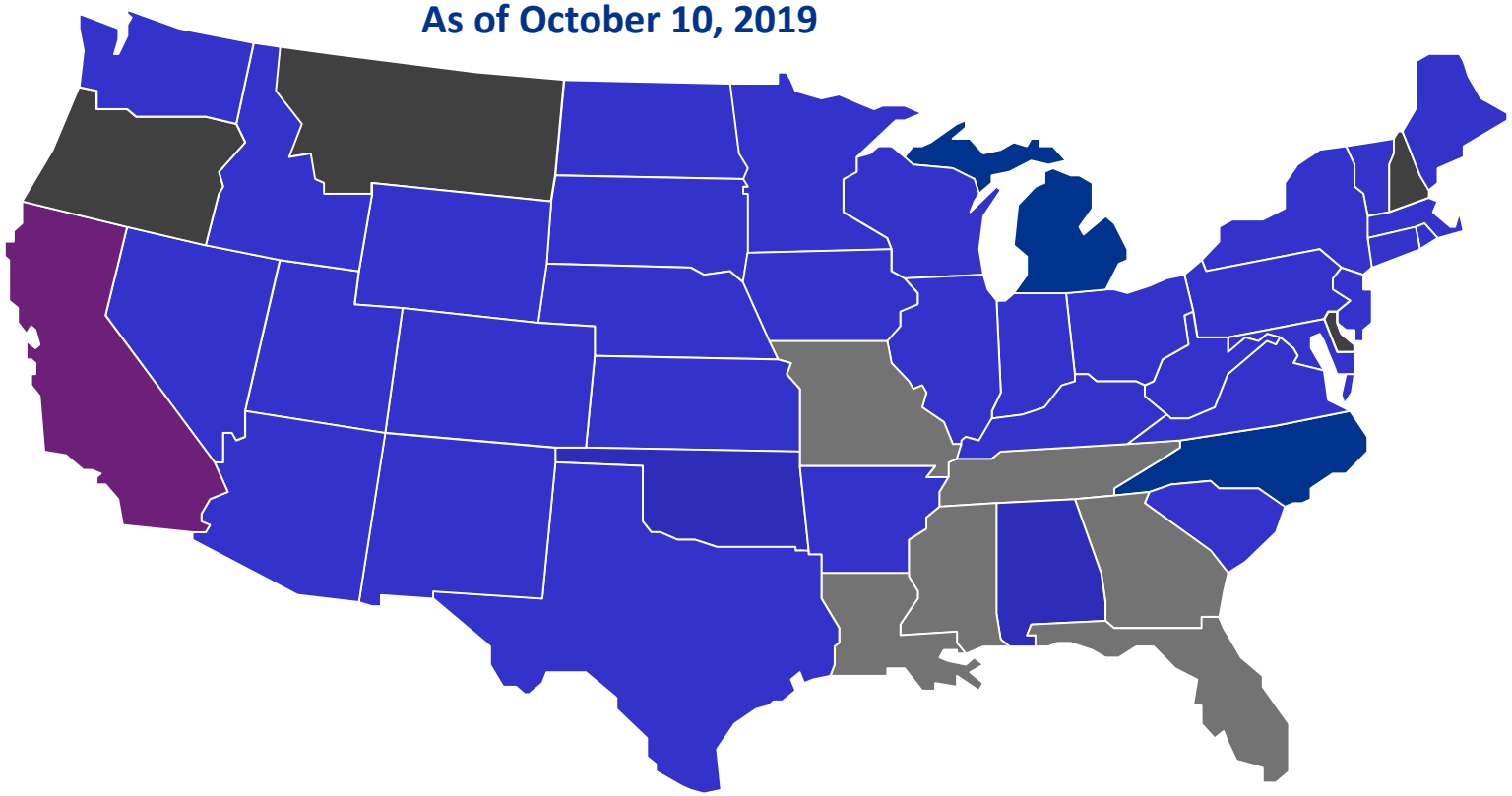
- Supreme Court rules that "the physical presence rule of *Quill* is unsound and incorrect" and is overruled.
  - It established a new test that is more or less parallel to the Due Process Clause.
  - New test for sales and use tax nexus is "economic or virtual" presence.
- SD law minimized burdens on interstate commerce by:
  - Including a transactional safe harbor (200 sales or $100,000 in sales)
  - Did not apply retroactively
  - South Dakota was a full member of SSUTA

Economic nexus



Marketplace Requirements

As of October 10, 2019



- Currently have marketplace requirements
- Proposed legislation in current session
- Collect-or-report
- No proposed legislation/legislative session ended
- No Sales Tax

Alaska
Hawaii
District of Columbia

Trust Tax Case - North Carolina – Insufficient Contacts

***Kimberley Rice Kaestner 1992 Family Trust v. Dep't of Revenue*, 814 S.E.2d 43 (N.C. June 8, 2018)**

- NC Sup. Ct held that the NC DOR unconstitutionally taxed the income of an irrevocable inter vivos out-of-state trust, based solely on the North Carolina residence of the beneficiaries - the court found that the Trust had insufficient contacts with the state to satisfy the Due Process Clauses of the federal and state constitutions - **mere contact with a North Carolina beneficiary was not sufficient**
- SCOTUS accepted case with w/oral argument on April 16, 2019; decision issued June 21, 2019 (one-year post-*Wayfair*); narrow decision focused trust's facts
- COST filed a brief asking the Court to address General Tax Jurisdiction and Specific Tax Jurisdiction – but the Court only addressed the specific facts of the Kaestner Trust
- Another case, *Fielding v. Comm'r of Revenue*, 916 N.W.2d 323 (Minn. Jul 18, 2018), where the grantor of a trust was a resident of the state, also held to be too insufficient by the MN Supreme Ct was denied SCOTUS review

California “doing business” Standard Cases

- ***In the Matter of Satview Broadband*** (September 25, 2018): The California’s Office of Tax Appeals (OTA) determined that holding a 25 percent non-managing interest in an LLC was <u>not</u> sufficient to create nexus under the state’s “doing business” standard - $800 minimum LLC tax.

- **FTB Legal Ruling 2018-1 (October 19, 2018)**: The FTB updated its 2014 ruling by softening certain absolute language, which provided that the members of an LLC are only “generally considered” to be doing business in California if the LLC is doing business in California.
  - The FTB also mentions *Swart* explicitly as a “narrow exception” and continues to aggressively keep in place an example using a non-managing member with a 15 percent interest – pointing out that 15 percent “greatly exceeds” the 0.2 percent in *Swart*

California “doing business” Standard Cases

- ***In the Matter of Jali, LLC*** (July 8, 2019): Again, OTA rejects FTB’s reliance on Swart’s 0.2% ownership threshold and notes that whether an out-of-state member is actively involved in an in-state LLC is important. Jali had no power to manage the in-state LLC, even though it had up to a 4.2% interest.
  - Note this opinion has been deemed precedential.

- ***In the Matter of Wright Capital Holdings LLC*** (August 21, 2019): The OTA determined that an out-of-state LLC that held a 50 percent interest in a pass-through entity that was registered to do business in California was doing business in California and, thus, subject to the California LLC Annual Tax.
  - OTA distinguished Wright Capital Holding's case from *Swart*, finding the LLC failed to show it was not a managing member of the in-state pass-through entity, and that "by virtue of holding a 50 percent interest" it had significant authority of the in-state entity's activities.

Other U.S. Supreme Court Cases of Interest

Pike Balancing Test: *Kansler v. Dep't of Revenue* (Mississippi November 29, 2018)

- The Mississippi Supreme Court held that Mississippi's statute of limitations for amending a state tax return did not discriminate against interstate commerce.
- Following the completion of a lengthy New York state tax audit, the Kanslers amended their Mississippi tax returns, requesting a refund of approximately $250k, based on Mississippi's credit for taxes paid to another state.
- The Department denied the Kanslers' refund request, asserting the claim was barred by the statute of limitations, and the Kanslers appealed, arguing the Department's denial of their request discriminated against interstate commerce under *Complete Auto*.
- The Court rejected the Kanslers' argument, noting the question is not whether government action presents a burden on commerce but rather whether it presents an *undue* burden and applied the *Pike v. Bruce Church, Inc.,* balancing test.
- The Court noted the discrimination alleged by the Kanslers was "incidental" an otherwise nondiscriminatory statute of limitations; therefore, the statute must "be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits."
- **Review denied by the U.S. Supreme Court** – Dkt 18-1485 (Miss DOR waived response)

Alternative Apportionment & Economic Substance: *Staples, Inc. v. Comptroller of the Treasury* (Maryland August 9, 2018)

- The Maryland Court of Special Appeals determined that a corporate group's subsidiaries operating in Maryland lacked economic substance apart from the rest of the group such that the entire group had nexus with the State.
  - The Court concluded the subsidiaries' "total financial dependence" and "total administrative and managerial dependence" on the parent companies – demonstrated through intercompany management, administration, and intellectual property licensing arrangements – showed there was a general absence of substantive activity from the subsidiaries that was meaningfully separate from the parent companies.
- The Court also determined the companies constituted a unitary group because "substantial mutual interdependence existed at all levels" between the companies in the corporate family, therefore permitting the Comptroller to impose an alternative apportionment formula that used franchise fees and interest payments made by the in-state subsidiaries to the corporate parents to determine the income attributable to Maryland for the parent companies.
- **Review pending before the U.S. Supreme Court** – Dkt 19-119 (MD DOR response requested 9/20/19 - conference set for 11/1/2019)

State-Versus-State Litigation/Legislation Addressing State and Local Taxation

— ***Arizona v. California***
- Arizona is arguing that California's $800 minimum tax on entities with passive investments in LLCs doing business in California violates Arizona's sovereignty and its citizens rights
  - Brief requesting review notes California's minimum tax "impressively violates all four prongs of the *Complete Auto Transit* test"
- Review and standing is tenuous – but it does draw attention to California's aggressive practices

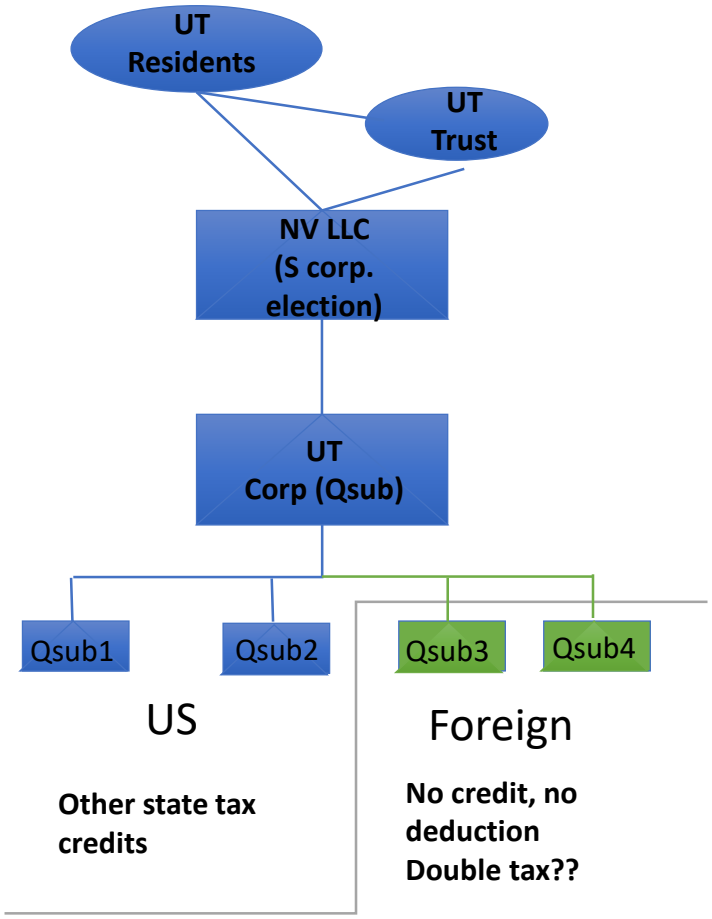
— ***Delaware v. Pennsylvania*** & ***Arkansas v. Delaware***
- Delaware claims it has unclaimed property rights for uncashed bank checks – other states argue a federal law, 12 U.S.C. § 2503, using location where a money or travel check is sold controls. Delaware asserts *Texas v. New Jersey* applies – no last known address the property escheats to holder's domicile state
- Special magistrate appointed to address evidence and file report to SCOTUS

— **New Hampshire's S.B. 242**
- Bill would prohibit sales tax states from requesting private customer information, conducing examinations, or impose sales/use tax on sellers in New Hampshire unless: 1) state provides at least 45-days notice and NH Justice Dep't approves request is constitutional and 2) state compensates sellers for installation and ongoing cost to collect that state's sales/use taxes

Does the Foreign Commerce Clause Apply to Individuals?

Steiner v. Utah State Tax Commission, 2019 UT 47 (Aug. 14, 2019)

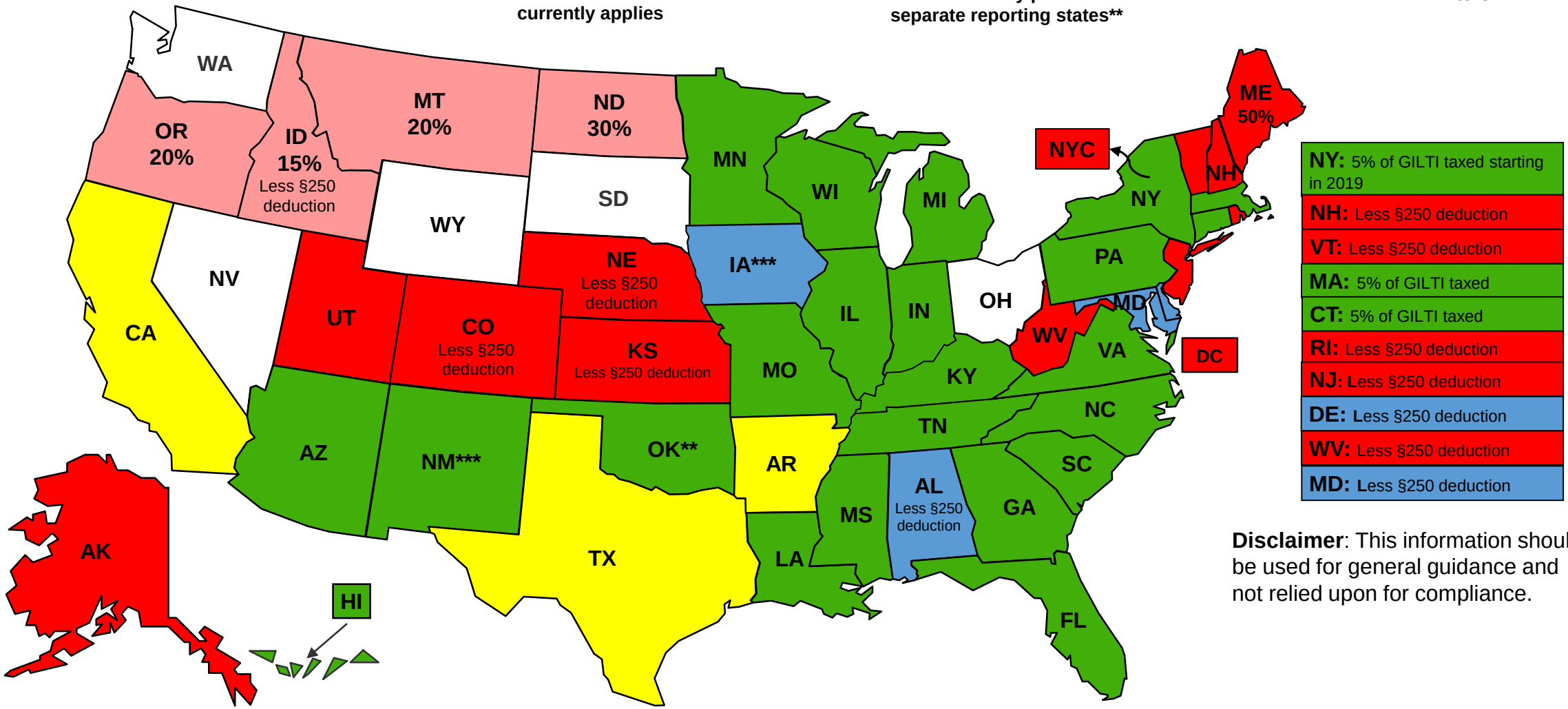
- Are individual resident taxpayers constitutionally entitled to either a deduction for foreign derived income or a credit for taxes paid to foreign countries?
- **Utah Supreme Court Holding**:
  - In light of *Wynne*, "[t]he continuing vitality of the *Complete Auto* [four prong] test is thus in serious doubt."
    - "Whatever life external consistency might have left [after *Wynne*], it is highly unlikely that it continues to apply in the context of an individual taxpayer's challenge to a state's taxation system." (responding to J. Alito's theoretical that the Maryland tax in *Wynne* would be internally consistent if it only taxed its residents' income)
  - No SCOTUS case has applied the Dormant Foreign Commerce Clause to individuals – those protections have only been extended to corporations.
    - "We would have no idea what test to apply or how to apply it."
- Utah Supreme Court's criticism of current Dormant Commerce Clause jurisprudence seems to invite a review … Steiner has received an extension from SCOTUS to file a review request by December 12, 2019



State Response to Federal Tax Reform

State Corporate Income Tax Conformity to GILTI*

- State does not impose a corporate income tax
- Decoupled from GILTI (or excludes 95%)
- Have not addressed IRC conformity and/or GILTI coupling specifically. Neither GILTI nor § 250 deduction currently applies
- Potentially coupled to GILTI, but inclusion may be constitutionally prohibited in separate reporting states**
- Coupled or potentially coupled to 10% to 30% of GILTI**
- Coupled or potentially coupled to GILTI**



- **NY:** 5% of GILTI taxed starting in 2019
- **NH:** Less §250 deduction
- **VT:** Less §250 deduction
- **MA:** 5% of GILTI taxed
- **CT:** 5% of GILTI taxed
- **RI:** Less §250 deduction
- **NJ:** Less §250 deduction
- **DE:** Less §250 deduction
- **WV:** Less §250 deduction
- **MD:** Less §250 deduction

Disclaimer: This information should be used for general guidance and not relied upon for compliance.

Note: Those states with "less §250 deduction" only tax 50% of GILTI (or 62.5% after 2025).

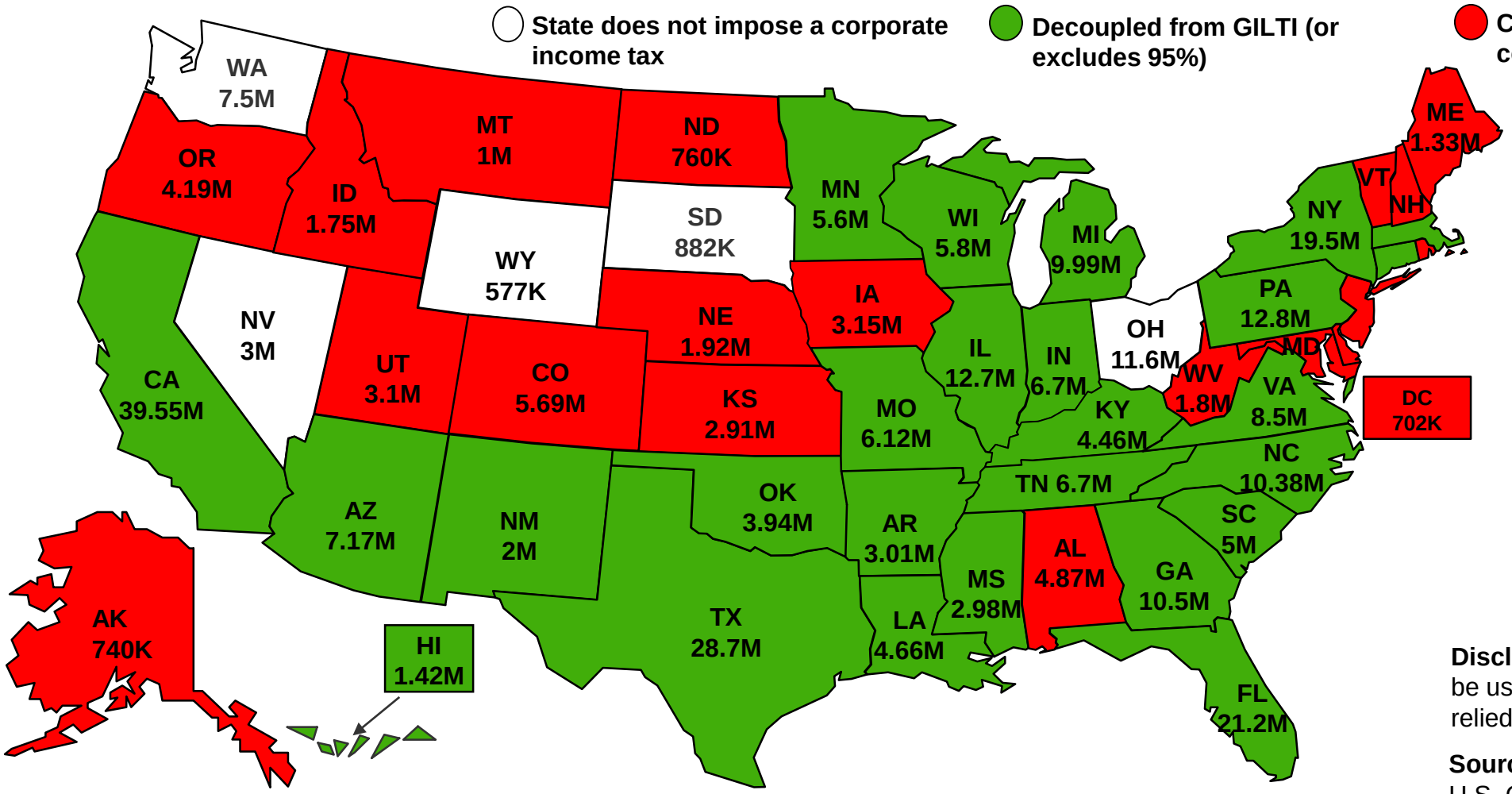
***** Based generally on 80% or more direct corporate ownership of foreign corporations. Other rules may apply for smaller % ownership or state personal income tax (PIT) purposes.

****** GILTI is not specifically referenced in many state conformity statutes so some states may still decouple from some or all of GILTI by administrative/legislative action.

******* Iowa conformity begins in 2019. New Mexico decouples starting in 2020.

Source: Council On State Taxation

States That Are Decoupled from GILTI Make Up 82.6% of the Population of States With Corporate Income Taxes



- CT: 3.57M
- DE: 967K
- MD: 6.04M
- MA: 6.9M
- NH: 1.35M
- NJ: 8.9M
- RI: 1.0M
- VT: 626K

Disclaimer: This information should be used for general guidance and not relied upon for compliance.

Sources: Council On State Taxation, U.S. Census Bureau

Total population in states that are decoupled from GILTI (or exclude 95%): 249.85M

Total population in states that are not decoupled from GILTI: 52.79M

Is the Impact of GILTI the Same for State Tax Purposes as It Is for Federal Tax Purposes?

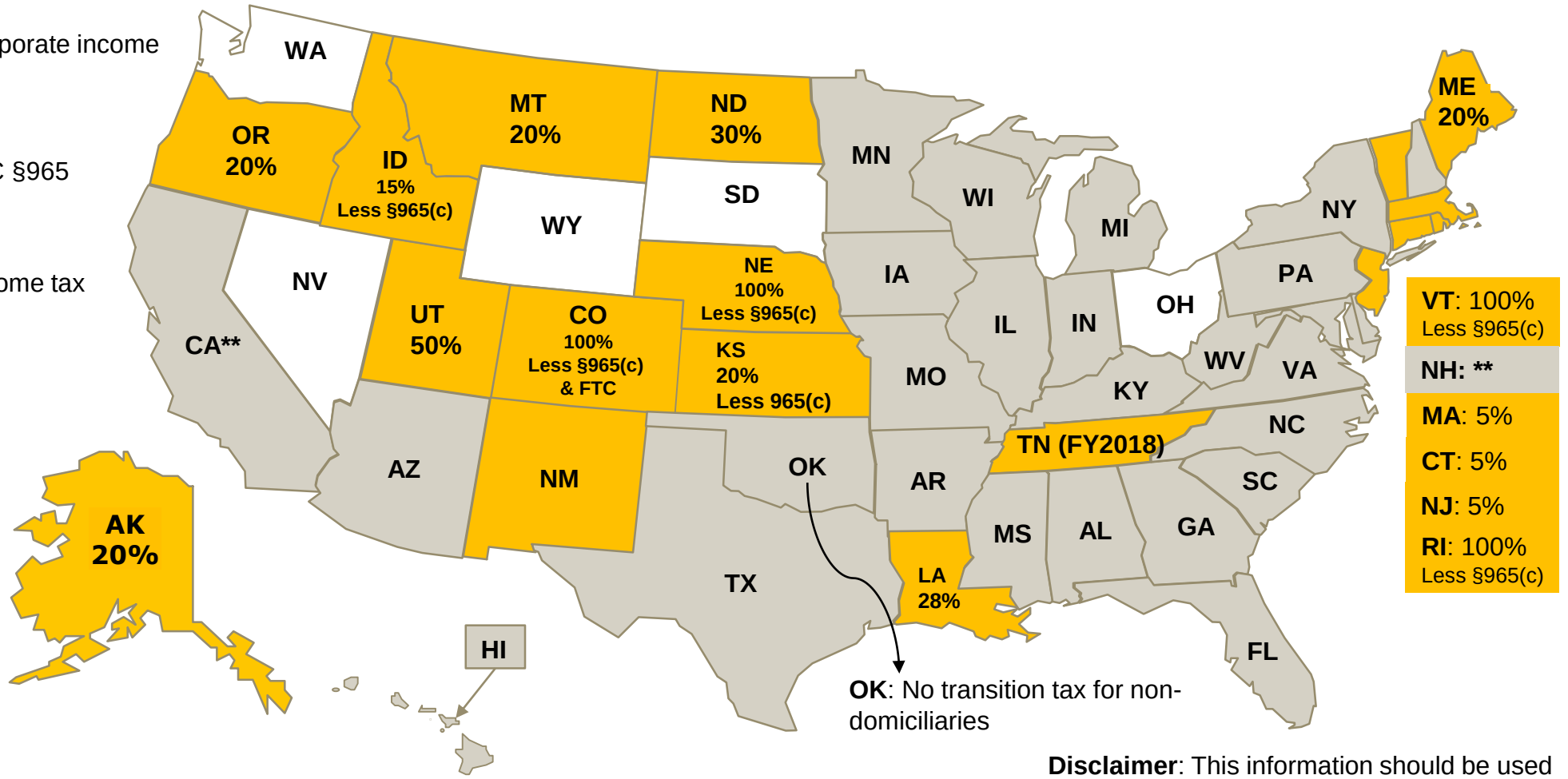
- **Global:** Yes, its starting point is all of the global income earned by the taxpayer's foreign subsidiaries.
- **Limited to Intangibles**: This is a misnomer – GILTI (global intangible low-taxed income) includes income from services, digital products, financial services, a sizable portion of tangible property sales, and intangibles.
- **Low-Taxed:** No, the states do not conform to the (80%) foreign tax credit allowed for federal tax purposes to offset the GILTI income. In addition, many of the states may not conform to IRC Section 250 that allows for a 50% deduction (reduced to 37.5% after 2025) for GILTI income.
- **Offset by Corporate Tax Cuts:** No, states do not conform to federal corporate tax cuts (Congress is raising $324 billion over 10 years from the international tax provisions to help pay for $654 billion in business tax cuts).
- **Favor Domestic Commerce over Foreign Commerce:** No, the states are limited by the Constitution's Commerce Clause and cannot treat foreign commerce differently than domestic.
- **Displaced US domestic income**: Proponents of state taxation of GILTI are making broad and unsubstantiated assertions that GILTI is all or primarily "**displaced US domestic income**"?
- **On why states should decouple from GILTI,** see generally: Joseph X. Donovan, Karl A. Frieden, Ferdinand S. Hogroian, and Chelsea A. Wood, "State Taxation of GILTI: Policy and Constitutional Ramifications,"
  State Tax Notes, October 22, 2018.

One Time Issue: State Corporate Income Tax Conformity to IRC §965 Repatriated Income*

State does not impose a corporate income tax

0%: State does not impose corporate income tax on IRC §965 repatriated income

State imposes corporate income tax on some or all of IRC §965 repatriated income



***** Based generally on 80% or more direct corporate ownership of foreign corporations. Other rules may apply for smaller % ownership or PIT purposes.

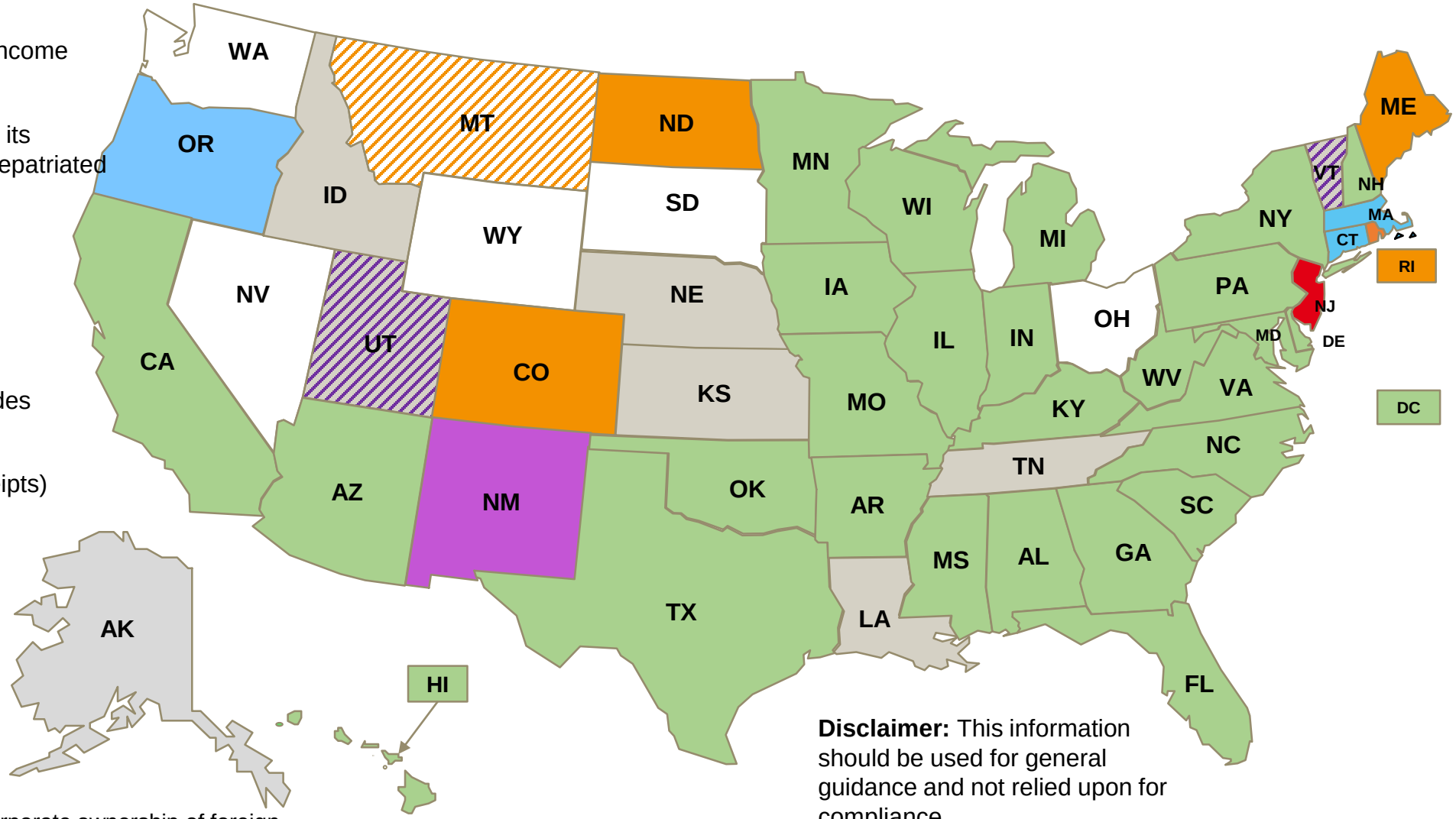
******No conformity update but taxes a portion of foreign dividends (when distributed) for water's edge filers.

Disclaimer: This information should be used for general guidance and not relied upon for compliance.

Source: Council On State Taxation

IRC §965 Repatriated Income State Factor Representation*

- State does not impose a corporate income tax
- The state currently does not impose its corporate income tax on IRC §965 repatriated income
- No factor representation allowed
- No new guidance
- Other methodology
- Sales factor denominator only includes net IRC §965 repatriated income.
- Foreign factors (including gross receipts) relating to taxable income allowed in denominator(s)
- Pattern indicates unofficial state positions (in appropriate colors)



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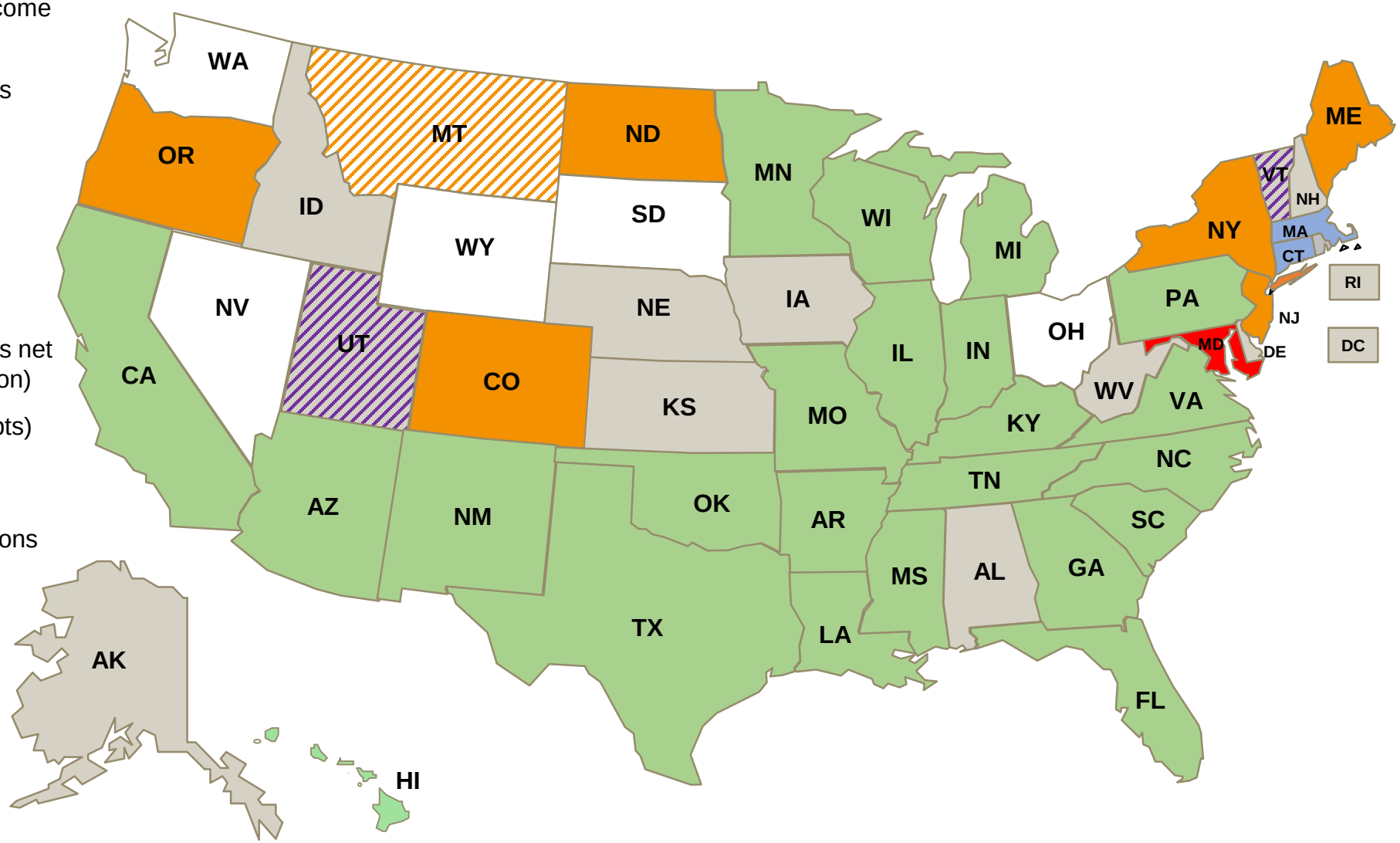
* Based generally on 80% or more direct corporate ownership of foreign corporations. Other rules may apply for smaller % ownership or PIT purposes.

Source: Council On State Taxation

GILTI State Factor Representation*

- State does not impose a corporate income tax
- The state currently does not impose its corporate income tax on GILTI
- No factor representation allowed
- No new guidance
- Other methodology
- Sales factor denominator only includes net GILTI (after Sec. 250 or other deduction)
- Foreign factors (including gross receipts) relating to taxable income allowed in denominator(s)
- Pattern indicates unofficial state positions (in appropriate colors)



***** Based generally on 80% or more direct corporate ownership of foreign corporations. Other rules may apply for smaller % ownership or PIT purposes.

Source: Council On State Taxation

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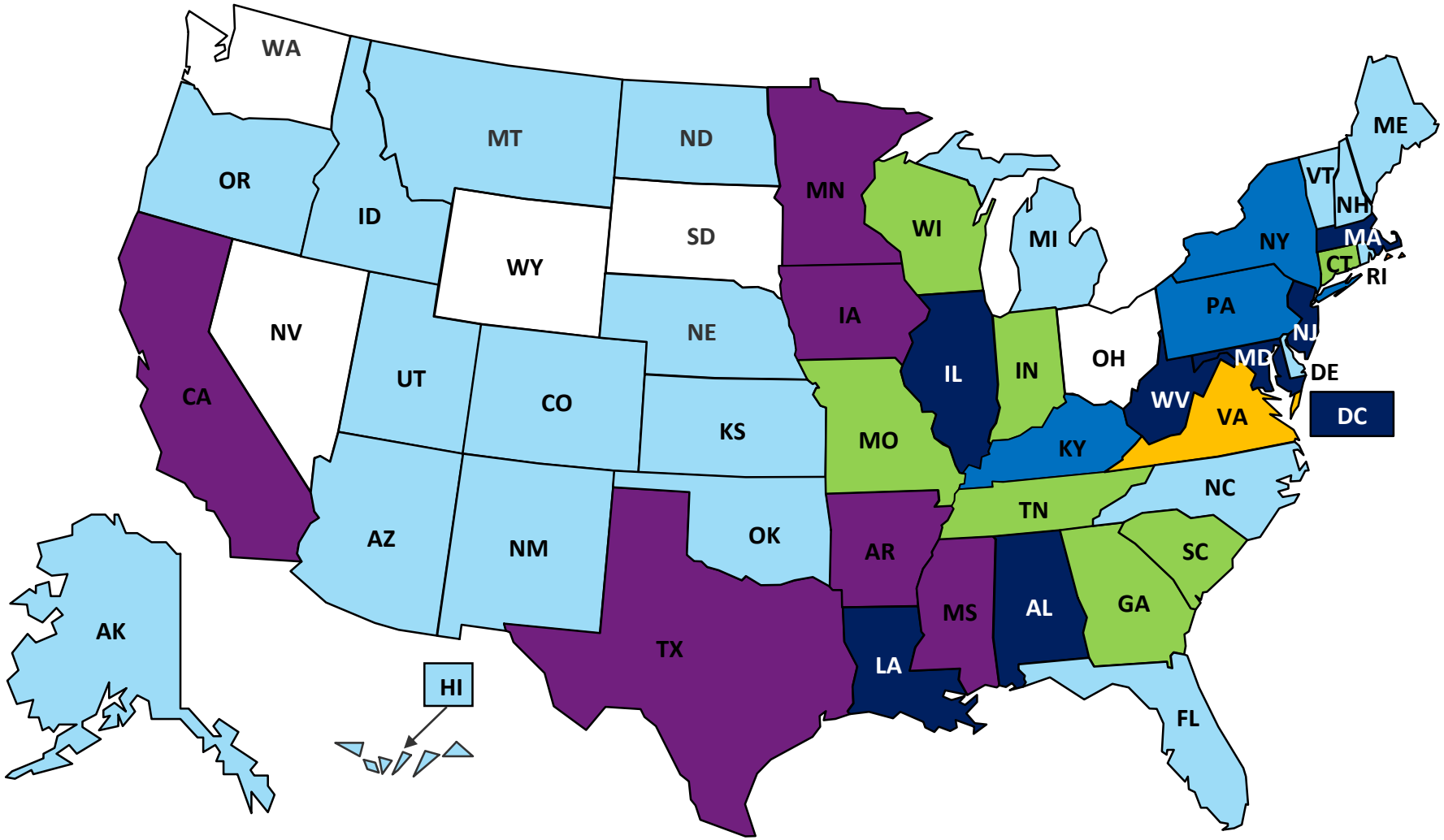
Future Litigation over State Taxation of GILTI and IRC §965 Repatriated income

- **Separate reporting states: Can the foreign source income be taxed at all?**
  - See *Kraft General Foods Inc. v. Iowa Department of Revenue*, 505 U.S. 71 (1992). A separate reporting state may not tax dividends from a controlled foreign corporation if it does not tax dividends from a controlled domestic corporation.
  - Seven separate reporting states are still coupled to GILTI (down from 11 in late 2018).
- **Combined reporting states: Can the foreign source income be taxed without appropriate factor representation (or a unitary relationship)?**
  - The state taxation of GILTI (and IRC §965 Repatriated income) in combined reporting states likely violates Commerce Clause limitations unless appropriate foreign "factor representation" is allowed.
  - The argument will likely focus on "discrimination" and not on "undue burden" – improving the taxpayers chances of prevailing. See *Oregon Waste Systems Inc. v. Department of Environmental Quality of Oregon,* 511 U.S. 93 (1994)
  - See contra:
    - *E.I. du Pont de Nemours & Co. v. State Tax Assessor*, 675 A.2d 82 (Maine 1996); and
    - *Appeal of Morton Thiokol, Inc.*, 864 P.2d 1175 (Kan. 1993).

State Conformity to 30% Interest Expense Limitation



- **Does not adopt IRC §163(j)**
- **Adopts IRC §163(j)**
- **Adopts IRC §163(j) with interest addback related to intangible income**
- **Adopts IRC §163(j) and has general interest addback provisions**
- **Enacted legislation decoupling from IRC §163(j)** [Note: Some of these states did not decouple as of 1/1/18 but decoupled later and some states may still have an intercompany interest expense adjustment]
- **Provides a corporate and individual subtraction equal to 20 percent of business interest disallowed pursuant to IRC §163(j)**
- **No general corporate income tax**

Source: Council On State Taxation

Disclaimer: This information should be used for general guidance and not relied upon for compliance.

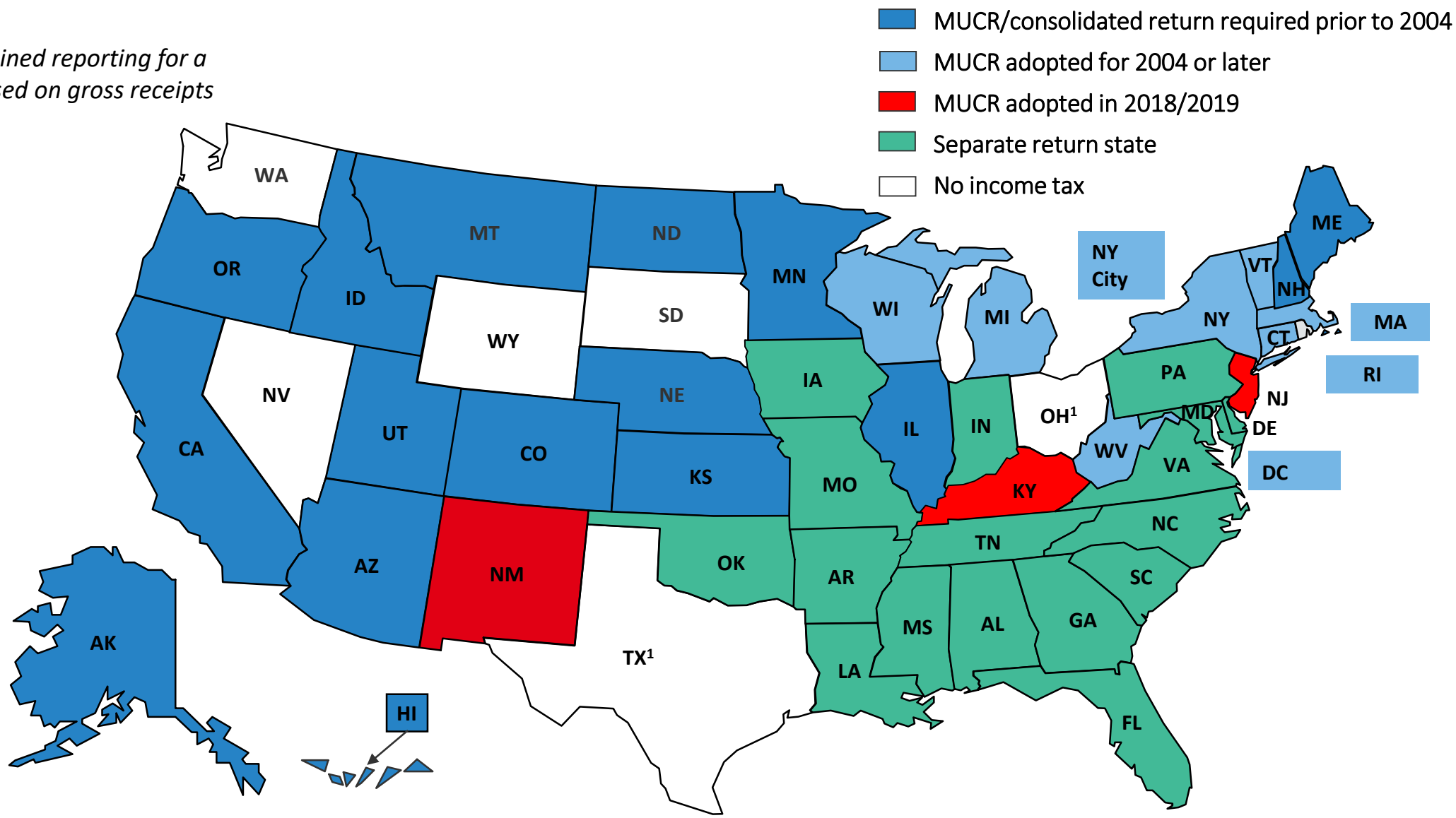
Interest Expense Limitation – IRC § 163(j)

- **General Overview:** Business interest expense cannot exceed 30% of adjusted taxable income (ATI) exclusive of business interest income and floor plan financing
  - ATI is essentially an EBITA (earnings before interest taxes and amortization) concept through 2021 and then EBIT (earnings before interest and taxes) thereafter.
  - Subject to carryforward.
- **State Tax Issues:**
  - Unlike most states, TCJA coupled the interest expense limitation at the federal level to 100% expensing for cost of capital.
  - How is the limitation computed for state purposes when state and federal filing methodologies differ? **When will state guidance be issued?**
  - External vs. internal debt (especially for separate return jurisdictions).
  - Will state allow indefinite carryforward of disallowed interest expense?
  - How will the federal limits interact with state related party interest expense disallowance statutes?

Combined Unitary Reporting

Mandatory Unitary Combined Reporting

[1] Combined reporting for a tax based on gross receipts



Mandatory Unitary Combined Reporting 2018/2019 Developments

- **Enacted**
  - Kentucky H.B. 366 / H.B. 487 (2018)
    - Kentucky H.B. 458 (2019) corrections bill
  - New Jersey A. 4202 (2018)
    - New Jersey A. 4495 (2018) corrections bill
  - New Mexico H.B. 6 (2019)
- **Proposed**
  - Florida S.B. 1692 / H.B. 1377
  - Maryland S.B. 377 / S.B. 76 (limited to retail and food and drink establishments)
  - New Jersey A. 5474
  - Oklahoma H.B. 1118, H.B. 1864, H.B. 2182
  - Pennsylvania H.B. 1445
- **States to Still Watch 2019/2020**
  - Pennsylvania, Indiana & Maryland

Renewed Interest in Worldwide Combined Reporting

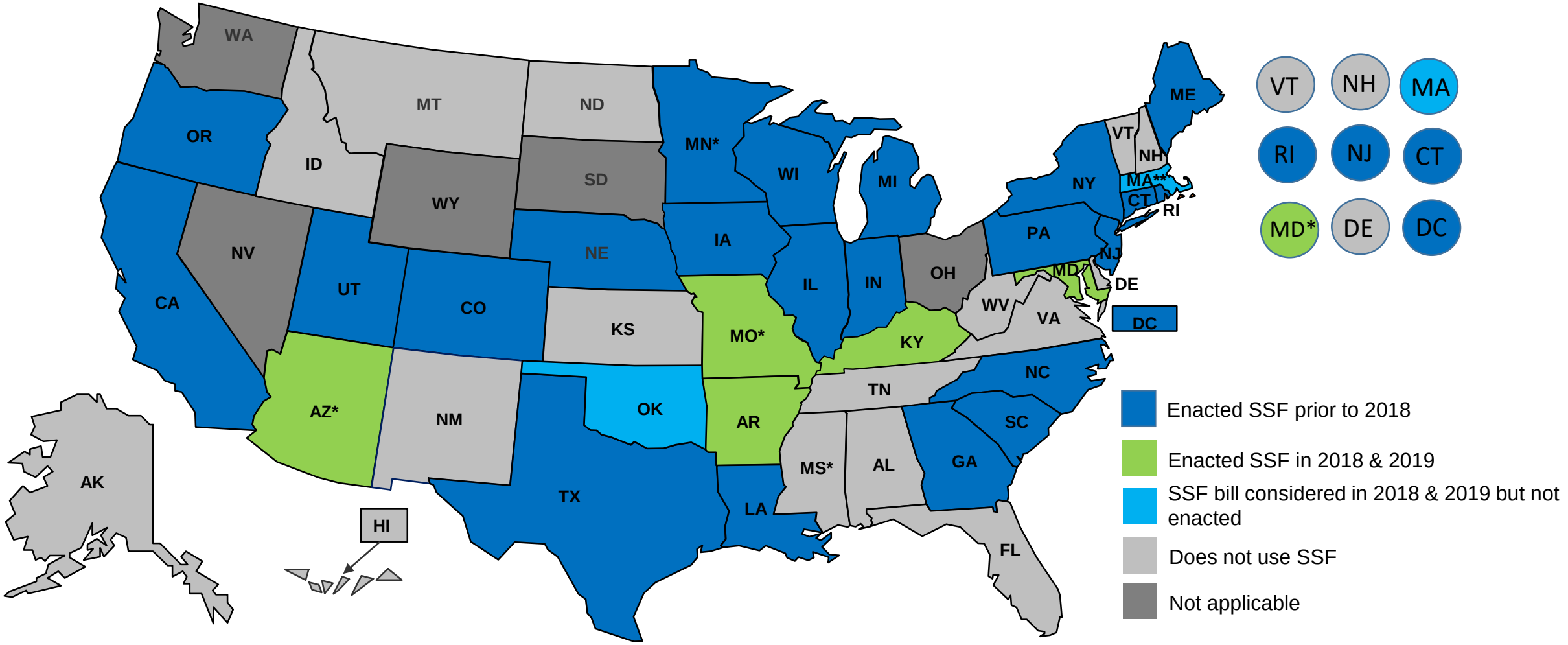
- **Hawaii**—S.R. 87 (passed) would convene a task force to study mandatory worldwide reporting.
- **Illinois**—H.B. 2085 (pending) would make worldwide combination the default and S.B. 1115 (pending) would allow a water's-edge election, but includes tax haven blacklist and cap on DRD of 75%.
- **Massachusetts**—H.B. 3787 and H.B. 3788 (pending) would implement mandatory worldwide reporting.
- **Minnesota**—H.F. 2125 (failed) would require unitary CFCs that create GILTI to be included in combined group and provides a worldwide election (10 years).
- **Montana**—S.B. 141 (died) would have repealed water's-edge election.
- **Oregon**—H.B. 2149 (died) and H.B. 2697 (died) would require foreign affiliates to be included in the unitary group.

Colorado Forced Combination Litigation

- ***Dep't of Revenue v. Agilent Technologies,*** 2019 CO 41 (May 28, 2019) and ***Dep't of Revenue v. Oracle,*** 2019 CO 42 (May 28, 2019)
  - The Colorado Supreme Court held the DOR erred in requiring a corporate taxpayer to include in its Colorado combined return an affiliated holding company that has no property or payroll of its own.
  - The affiliated holding companies did not meet the definition of "includable C corporation" having more than 20% of its property and payroll assigned to locations inside the US, and DOR's regulation supported taxpayer position.
  - State's general anti-abuse provision cannot be used to circumvent statute where there was no evidence the taxpayers' structures were abusive or intended to avoid tax
- **Colorado S.B. 233** (signed May 31, 2019):
  - Provides that C corporations with de minimus or no property or payroll are "includable" for purposes of the Colorado combined group, effective Aug. 2,2019.

Sourcing of Receipts

Corporate Income Tax - Single Sales Factor



Note*: **Arizona expanded single sales factor election to additional taxpayers in 2018. **Missouri** will use a single sales factor apportionment method beginning January 1, 2020. **Maryland** approved single sales factor in 2018, and it will be phased in by 2022. **Mississippi** taxpayers may choose their apportionment method using one or more of the three factors. **Minnesota** proposed a bill in 2019 to move back to Three-Factor apportionment.

** Notes states with legislation currently pending, but which has not yet been enacted

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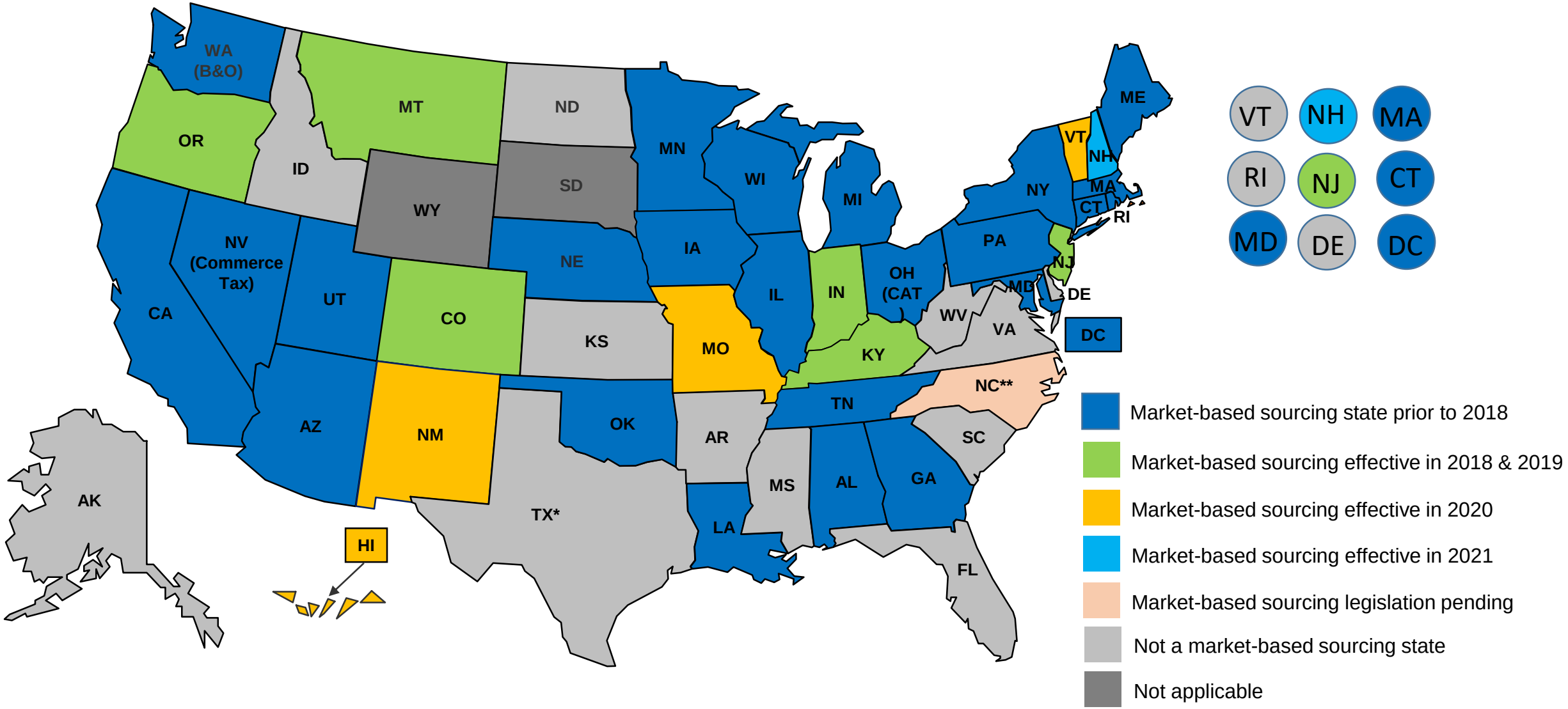
Corporate Income Tax – Market-Based Sourcing



*Receipts from the sale of services are sourced to **Texas** if the service is performed in Texas. If the service is performed both inside and outside of Texas, the receipts are sourced to Texas on the basis of the fair value of services rendered in the state.

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Cost of Performance: *Corporate Executive Board v. Virginia Dep't of Taxation* (Virginia February 7, 2019)

- The Virginia Supreme Court upheld Virginia's cost-of-performance sourcing methodology as constitutional.
- Corporate Executive Board (CEB), an advisory service firm headquartered in Virginia that sold mostly to customers outside of Virginia, sued the state of Virginia assert its cost of performance provisions violated the Due Process and dormant Commerce Clauses.
  - Specifically, CEB asserted that since many states have moved from cost-of-performance sourcing of intangibles to marketplace sourcing, these other states also included a portion of CEB's sales in their sales factor numerators, resulting in the taxation of over 120 percent of CEB's nationwide income.
- The Court acknowledged CEB was subject to double taxation but ultimately concluded that Virginia's apportionment formula did not create a "grossly distorted" result and, therefore, passed the external consistency test.

Other GRT and Corporate Income Tax Issues to Watch

Sourcing of Ohio CAT Sales

Greenscapes Home & Garden Prods. v. Testa (Ohio Feb. 7, 2019)

- Ohio Court of Appeals held that a Georgia garden supply company had sufficient Due Process nexus with Ohio to be liable for Ohio's commercial-activity tax ("CAT") because it knew its customers were bringing its products into Ohio even though its customers used their own trucks with title transfer at Greenscapes' loading dock Georgia

Defender Security Co. v. Testa (Ohio Sup. Ct. granted discretionary appeal,2019-0531)

- Court of Appeals concluded ultimate benefit of payments Defender received from ADT (purchaser not located in Ohio) for residential security contracts were correctly based on the location of ADT's customers which were located in Ohio – and not ADT's non-Ohio locations – denying Defender's refund request (arguably, ODT is using look-through approach to the purchaser's customers)

Mia Shoes v. McClain (Ohio BTA 8/8/2019, No. 2016-282)

- Taxpayer asserts Ohio's ultimate delivery rule should allow it to exclude shoes shipped to an Ohio warehouse and subsequently distributed to stores in and out of Ohio based on percentage of retail stores in Ohio v. non-Ohio – ODT, arguably not allowing the use of a look-through approach for the taxpayer (however, there is also a burden of proof issue)

Portland, Oregon Retail Gross Receipts Tax

- Gross Receipts Tax on Retail Sales: Effective for tax years beginning on or after 1/1/2019, Portland imposes a 1% "surcharge on gross revenues from sales within the City, unless otherwise exempted," on "Large Retailers"

  - Large Retailer is a "business" that:
    - Is subject to the Portland Business License Tax
    - Had annual gross revenue from retail sales from all locations in the U.S. where the taxpayer conducts business that exceeded $1 billion in prior year
    - Had annual gross revenue from retail sales within Portland of $500,000 or more in the prior tax year
  - Large Retailer excludes:
    - Any manufacturer or other business that is not engaged in retail sales within Portland
    - Any entity operating a utility within Portland
    - Any cooperative recognized under federal or state law
    - Any federal or state credit union

  - "Retail sale" is a sale to a consumer for use or consumption, not for resale, and includes services

Wyoming Corporate Income Tax Proposal on Large Retailers

- H.B. 220 (died)
  - Would have imposed a corporate income tax at a rate of 7% on certain "large retailers"
    - "Taxpayer" defined to include vendors with NAICS in the retail trade (sector 44 or 45) and accommodation and food services (sector 72) with more than 100 shareholders
  - Certain legislators believed this would not have created a "new" tax liability for impacted taxpayers based on throwback

Wyoming Corporate Income Tax Proposal on Large Retailers

- LSO-0073—National Corporate Tax Recapture Act
  - Would impose a corporate income tax at a rate of 7% on certain large taxpayers with more than 100 shareholders
    - NAICs codes removed
  - Current draft attempts to address some of technical raised during the legislative session and interim period, but continues to include significant drafting flaws
    - Includes COP and market-based sourcing provisions
    - Questionable filing group provisions
    - NOL provisions confusing at best, but likely fundamentally flawed

MTC Uniformity Projects—Public Law 86-272 Work Group

- Work Group began holding regular calls earlier this year to discuss whether the MTC's PL 86-272 statement should be updated to address internet sales and internet sellers
- Work Group has held a series of calls during which various scenarios have been discussed
  - For example:
    - Seller maintains a website offering various goods and services for sale
    - Seller maintains a website offering only items of TPP. The products are complicated to use and purchases often need post-sale assistance. Seller provides assistance in the following ways: toll-free numbers; electronic chat sessions; information posted on website; via email, etc.
  - The conversations on the calls have been lively regarding whether the scenarios being discussed would impact a taxpayer's PL 86-272 protection
  - General consensus on the calls by the state participants is that internet sellers are going beyond the protections of PL 86-272
- On April 26, the work group updated the Uniformity Committee and described the work group's analysis as a "work in progress"

MTC Uniformity Projects—Public Law 86-272 Work Group

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- On August 5, the work group again updated the Uniformity Committee and received significant blowback from the practitioners and the business community.

- On November 6, the work group is expected to update the Uniformity Committee, but has stated the current draft is "not ready for primetime"

Sales and Use Tax Developments

Marketplace Facilitator Collection: *Normand v. Walmart.com USA LLC* (Louisiana December 27, 2018)

- The Fifth Circuit Louisiana Court of Appeals affirmed a trial court judgment holding Walmart.com liable for approximately $1.8 million in unpaid taxes on sales made by third parties on Walmart.com's online marketplace, finding the trial court correctly determined the legislative intent was clear and statute was unambiguous.
  - The trial court found Walmart.com was liable as a "dealer" within the meaning of La. R.S. 47:301(4)(1) because providing the marketplace constituted "regular or systematic solicitation of a consumer market."
- Walmart.com argued it was not a "dealer" because it never had title or possession of the property being sold.
- In its appeal, Walmart.com argues that the parish imposes a discriminatory tax on electronic commerce that violates ITFA because the Collector does not require operators of similar offline marketplaces to collect local sales taxes.
  - For example, the owner of a shopping mall is not required to collect tax when a store that leases space in the mall makes a sale to its customer.
  - Nor is a newspaper required to collect tax when a seller advertising in the classified ads section makes a sale to a customer.
- On February 14, 2019, Walmart.com filed a petition for writ of review with the Louisiana Supreme Court.
- Oral arguments held on October 22, 2019.

Daily Sales Tax Remittance by Card Processors

- Concept to establish so-called “real-time” sales tax collection; would require vendors and payment processors to remit sales tax from purchases on a daily-basis
  - CT S.B. 877 (2019); S.B. 1057/S.B. 1047 (2017); H.B. 5636 (2016)
  - AZ S.B. 1091 (2018) passed by both houses, but vetoed by Governor
  - MA H.B. 2 (2018), Dropped from final budget sent to Governor, similar to 2017 proposal that ultimately failed after Department of Revenue feasibility analysis
- Staggering Costs to Implement
  - 2017 State Tax Research Institute study projects cost to comply $1.22 billion in up-front implementation costs and $28 million in annual recurring costs
- No Real Benefit to State
- All Asserted Benefits Can Be Achieved Through Estimated Prepayment
  - One-time revenue through acceleration
  - “Float” – requires state to invest and not spend one-time revenue
  - Delinquent Taxpayers
  - Cash Economy

Sales Taxation of Software

- ***Ex parte Russell County Community Hospital LLC v. Dep't of Revenue*** (Alabama May 2019)
  - The Alabama Supreme Court on May 19 determined all software is taxable tangible personal property, regardless of whether it is custom or canned software
  - Denied refund claim for sales tax paid on software purchased and then customized by the seller for a hospital's specific needs
  - The Court, however, noted, separately stated and invoiced charges for services rendered that "accompany the conveyance of software," including customization and implementation services, are nontaxable
  - "The pertinent distinction," the Court said, "is how the transaction is documented and invoiced, and that is left strictly in the hands of the seller and purchaser."

Qui Tam Actions

Qui Tam

- ***People v. Sprint Nextel Corporation*** (New York)
  - Whistleblower suit brought in 2011 under the New York False Claims Act alleged that Sprint violated state tax law by failing to collect sales tax on 100% of charges for flat rate wireless voice plans.
  - In 2012, the New York AG filed a superseding complaint, converting the whistleblower suit into a civil enforcement action.
  - On October 20, 2015, the New York Court of Appeals ruled that the False Claims Act action may proceed, affirming the lower court's denial of Sprint's Motion to Dismiss.
  - On December 21, 2018, Sprint agreed to pay $330 million to settle the False Claims Act suit with New York.

Treasury Offset Program

Treasury Offset Program (TOP) - Background

- COST members frustrated
- State Reciprocal Program (SRP) – 12 states
  - (DC, KS, KY, LA, MD, MN, NJ, NY, OR, VA, WV, and WI)
- Example
  - State certifies “debt” to TOP
  - TOP identifies federal vendor payments to be made to same EIN as TOP debtor
  - TOP diverts federal vendor payment to offset debt
- Issues
  - 60-day notice prior to sending debt to TOP
  - Offset notice contains very little detail about debt – just debtor
  - Large time commitment to unwind offset

Treasury Offset Program (TOP) – COST Activity

- Meeting with U.S. Treasury Department Bureau of the Fiscal Service (BFS)- agency responsible for administering TOP
  - G2G program
    - companies to sign up to receive monthly notification of any debts submitted to TOP
    - listed by employer identification number (EIN)
  - BFS annual certification document
    - Required to be signed by participating states
  - Follow-up meetings with individual states
  - COST Administrative Scorecard
- More information
  - Pat Reynolds, preynolds@cost.org, 202-484-5218
  - Doug Lindholm, dlindholm@cost.org, 202-484-5212

BUREAU OF THE Fiscal Service

Scorecard on Property Tax Administration June 2019

COST/IPTI Property Tax Scorecard

Evaluation of Three Categories of Property Tax Administration with each category having three subcategories that were evaluated:

- Transparency of Property Tax System
- Consistency of Property Tax Administration
- Procedural Fairness with Tax Appeal Process

Grading format for scorecard:

- No points if jurisdiction has good administrative process
- One point if jurisdiction has average administrative process
- Two points if jurisdiction needs improvement to administrative process

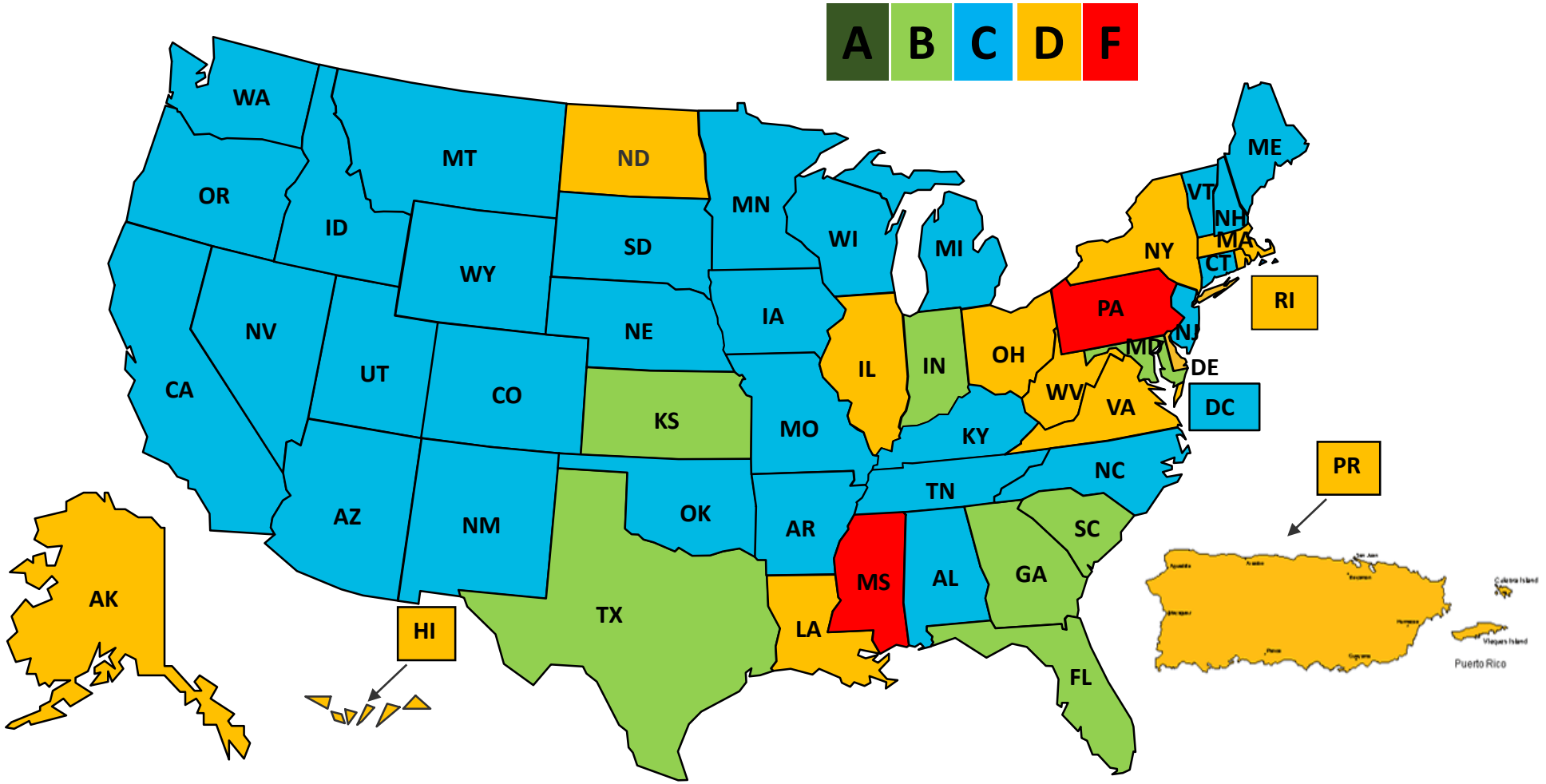
Target audience:

- Grading is not reflective of any tax administrators' practices, but property tax administration system in a state – targeted towards the states' policy makers

Best Practices Criteria

- **Transparency**
  - Laws adequately explained on website
  - Adequate notice of proposed valuation
  - Ability to compare values placed on other properties
  - No disclosure of income and expenses
  - Frequent revaluations
- **Consistency**
  - Tax forms, assessment ratios, training
  - Centralized oversight of local assessors' practices
- **Procedural Fairness**
  - Sufficient time for taxpayers to file appeals
  - Balanced burden of proof review before independent arbiter
  - Ability to partially pay disputed tax
  - Interest rate paid on refunds matches rate on underpayments

Overall Grades for U.S. States and Puerto Rico



Source: The Best (and Worst) of International Property Tax Administration, COST & IPTI, June 2019

2020 COST Legislative Initiatives: Compliance and Administration

1) Improving the **states' RAR practices** (reporting federal tax changes to the state revenue agencies), which includes states addressing the new federal partnership audit regime to avoid revenue losses;
2) Encouraging states that do not **allow at least one month** after the recently revised federal extended return due date to legislatively address this issue; and
3) Encouraging states to provide **at least a 30-day threshold** before nonresidents, including employers, are subject to a state's requirements to remit/withhold personal income taxes.

Questions???

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