

**PRESENTATION**

**Southeast States – Annual SALT Roundup**

**Chattanooga Tax Practitioners**

**June 19, 2013**

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**Overview**

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- National Developments
- Tennessee Business Tax Amendments
- Apportionment
- Related Party Transactions
- Nexus and Tax Jurisdiction
- Practice and Procedure
- Sales/Use Tax Developments
- Other Southeast State Tax Developments
- Unclaimed Property

## National Developments

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- **Marketplace Fairness Act – S. 743**
  - Passed U.S. Senate on May 6
  - Would allow states to compel collection of sales and use taxes by remote sellers having no physical presence in the state and sales of \$1 million or more
  - State must be a member of SSUTA or enact a statute that provides for a uniform state and local base, single tax agency administration, single tax return, and destination sourcing
  - Fate is uncertain in House of Representatives
  
- **New York: *Overstock.com, LLC v. New York Dept. of Taxation and Finance* (Mar. 28, 2013)**
  - New York Court of Appeals upholds the “click-through nexus” statute
  - Ruled statute was not facially unconstitutional
  - Similar statutes in AR, CT, GA, IL (declared unconstitutional by trial court; appeal pending), NC, PA, RI, VT

## National Developments (con't)

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- **California: *The Gillette Company v. Franchise Tax Board* (July 24, 2012)**
  - Court of Appeals ruled Multistate Tax Compact “taxpayer option” allowed taxpayer to elect equally-weighted three factor apportionment
  - Court of Appeals re-affirmed decision on Oct. 2, 2012; California Supreme Court has granted review
  - California has repealed the Multistate Tax Compact
  - FTB Notice 2012-01 provides protective refund claim procedures; FTB also announced will impose 20% “Large Corporate Underpayment Penalty” on original returns (if *Gillette* is reversed or vacated)
  - Similar “taxpayer option” cases so far rejected in Michigan and Texas; pending in Oregon
  
- **Economic Presence Nexus**
  - *Matter of Scioto Insurance Co.* (Okla., May 1, 2012)
  - *In re Washington Mutual, Inc.* (U.S. Bankr., Dec. 19, 2012)
  - *Griffith v. Conagra Brands, Inc.* (W.Va., May 24, 2012)

## National Developments (con't)

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- **Bloomberg BNA Survey of State Departments of Revenue**
  - **Web Server Nexus**
    - 26 states responded they would find nexus for out-of-state company that leased space on third party internet server
    - 24 states responded storing data on in-state server would constitute nexus
    - 12 states responded using web-hosting provider with a server in the state would constitute nexus
  - **Telecommuting Nexus**
    - 36 states (plus DC and New York City) responded that income tax nexus results for out-of-state company having an employee telecommuting from their home in the state
    - Single employee sufficient; back office and product development functions sufficient (sales activities of telecommuter not necessary)
  - **Non-U.S. Entities**
    - MS, TN, TX will not extend P.L. 86-272 protections to foreign corporation
    - AR, FL, LA, NC, VA will extend the protections
    - No response: AL, GA, SC
    - Permanent Establishment/Tax Treaty Exemptions apply: FL, LA, TN, VA
    - Don't apply: AR, MS, NC (no response: AL, GA, SC, TX)

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## Tennessee Business Tax Amendments

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- S.B. 183/H.B. 177
- Effective for tax periods that begin on or after Jan. 1, 2014
- **Extends (clarifies?) imposition of Business Tax on out-of-state businesses that do not have a physical place of business in TN**
  - Performing any service “in this state, to the extent such service is received by a customer located in” TN
  - Leasing tangible personal property that is “located in” TN
  - Delivering tangible personal property to a buyer in TN using the seller’s own vehicles
  - Purchasing and reselling tangible personal property in a wholly in-state (TN) transaction, where the purchase and sale are accomplished through the presence of the seller’s employee’s, agents, or independent contractors “acting on behalf of the seller”

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## Tennessee Business Tax Amendments (con't)

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- Amends how Business Tax is allocated/distributed to state and municipalities; tax on out-of-staters allocated wholly to the state
  - State keeps all tax, penalties and interest resulting from audit
  
- Exemptions and Credits
  - Business with sales of less than \$10,000 in a county or municipality (increased from \$3,000) is exempt with respect to sales sourced to that county or municipality
  - Business Tax will not apply to providers of direct-to-home satellite television programming services
  - Personal property tax credit allowed only if the property is taxed by the municipality or county that “receives the allocation of tax.”
  
- “Sales of services that are received by customers outside the state”
  - Amends prior deduction for services “substantially performed in other states”

## Tennessee Business Tax Amendments (con't)

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- Sourcing
  - Receipts are sourced to the county or municipality in which the taxpayer has its physical location, including receipts from sales made into other counties or municipalities in which taxpayer does not have a physical location
  - If taxpayer has no physical location in TN, receipts are sourced to the state
  
- Legislation overturns *Comcast of Nashville II, LP v. Farr* (invalidating Rule 28 that sourced statewide sales to the taxpayer’s physical location in TN)

## Apportionment Developments

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- Mississippi: *Equifax, Inc. v. Dept. of Revenue* (May 1, 2012), review granted by Mississippi Supreme Court Jan. 10, 2013
  - Court of Appeals rejected trial court's arbitrary and capricious standard and rebuttable presumption in favor of Department of Revenue and its alternative apportionment formula (market sourcing)
- Virginia: Ruling of Commissioner, P.D. 13-6 (Jan. 7, 2013)
  - Single sales factor election for manufacturers guidelines
  - Phased in – triple (years beginning before 7/1/13), then quadruple (until 7/1/14), then single factor
  - Wage and employment requirements; "recapture" with interest if fail
- Alabama: Reg. 810-27-1-4-.17.01
  - Regulations issued to implement market sourcing for sales of services
  - Substantial connection to geographic location(s) of recipient business enterprise
  - No substantial connection = Alabama commercial domicile of recipient business enterprise

## Apportionment Developments (con't)

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- Tennessee: *Vodafone Americas Holdings, Inc. v. Roberts* (Mar. 19, 2013)
  - Department of Revenue's market sourcing alternative formula upheld

## Related Party Transactions

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- **Louisiana: Revenue Information Bulletin No. 13-006 (Jan. 11, 2013)**
  - Borrowed capital is no longer included in franchise tax base
  - However, if total debt to all related parties exceeds capital stock and surplus and undivided profits, then 50% of the excess is reclassified and included in base
  
- **North Carolina: Forced Combination**
  - *Delhaize America, Inc. v. Lay* (N.C. Ct. App., Aug. 21, 2012): NC's prior statute and DOR practice upheld
  - 17 N.C.A.C. 05F.0101: New regulations mandated by 2012 legislation providing guidance and standards for DOR to exercise forced combination discretion issued
  - Regulations effective Jan. 31, 2013

## Related Party Transactions (con't)

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- **Tennessee: Letter Ruling #12-32 (Dec. 19, 2012)**
  - Accounts receivable factoring transactions not subject to Tennessee intangible expense add-back statute
  - Accounts receivable do not satisfy definition of "intangible property"
  
- **Tennessee: Revenue Ruling # 12-27 (Nov. 14, 2012)**
  - Patents licensed between related parties outside Tennessee; not used in Tennessee to manufacture
  - Owner/licensor of patents was not "doing business" in Tennessee just because products manufactured using patented process were distributed in Tennessee
  - However, in footnote Department of Revenue suggests it could assert economic presence nexus if intangibles licensed for use in Tennessee

## Nexus and Tax Jurisdiction

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- **Alabama: Rule 810-6-2-.90.01 (Aug. 12, 2012)**
  - Addresses when out-of-state seller is considered to have substantial nexus with Alabama and required to collect sales/use tax
  - Includes the usual offices, place of business, employees and representatives and (1) delivery using own vehicles, or (2) presence of affiliate that uses identical or substantially similar trade names, trademarks, or seller and affiliate pay for each other's services based on volume or value of sales, or seller and affiliate share a common business plan/coordinate business plans
- **Alabama: *Van Horn v. Dept. of Revenue* (Jan. 3, 2013)**
  - More than one salesman and more than one sales solicitation visit is needed to create local nexus

## Nexus and Tax Jurisdiction (con't)

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- **Georgia – H.B. 386**
  - Affiliate nexus: (1) out-of-state seller required to collect sales tax if related company sells a similar product under similar name or related company uses trademarks, service marks, or trade names similar to the seller's; or (2) Georgia person or entity delivers, installs, assembles, provides maintenance service, or customer pick-up services on seller's behalf
  - Affiliate nexus statute effective Oct. 1, 2012
  - "Click-through" nexus: (1) out-of-state seller made in excess of \$50,000 of sales to Georgia customers in the preceding 12 months, (2) that were referred to the seller via internet website link, in-person presentation, or telemarketing, and (3) seller pays a commission or other consideration to Georgia resident
- **West Virginia: H.B. 2754**
  - Sales and use tax "affiliate nexus" provisions enacted
  - Remote retailer with a "related entity," "related member", or "unitary business" in WV is a "retailer engaged in business in this state."

## Practice and Procedure

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- Georgia Tax Tribunal
  - Began Jan. 1, 2013
  - Petition stays enforcement and collection until case finalized
  - Decisions appealed to Fulton County Superior Court (except small claims cases)
  - No jurisdiction to hear property tax cases
  
- Virginia: Ruling of Commissioner, P.D. 12-200 (Dec. 6, 2012)
  - Merger of two affiliated group – Acquiring VA group filed separate; target VA group filed consolidated
  - Merger of equals means target group assets or net value greater than 45% of combined value of target and acquiror group; can elect new filing status
  - In ruling, target group net value less than 45% and required to change to separate VA returns

## Practice and Procedure (con't)

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- Mississippi: H.B. 892
  - Requires taxpayer consent to extend statute of limitations for audit examination (but DOR still has additional year to conclude audit if taxpayer does not consent)
  - Previously, DOR only required to issue audit notice within three-year SoL
  - IRS adjustments – three year SoL after DOR notified of adjustment
  - Previously-audited sales tax reporting methods – DOR estopped from collecting additional tax for periods prior to notice that prior method would result in additional tax
  - Tax periods beginning on or after Jan. 1, 2013
  
- Mississippi: *Dept. of Revenue v. AT&T Corp.* (Sept. 6, 2012)
  - Taxpayer appealed assessment; paid entire assessment but did not also post bond (for double amount in controversy), as required by statute
  - Mississippi Supreme Court: Chancery Court did not have jurisdiction
  - Current law: appeal to Board of Tax Appeals; further appeal to Chancery - post bond (1/2 of assessment) or pay assessment



## Sales/Use Tax Developments - General

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- Tennessee: Revenue Ruling # 13-03 (Jan. 14, 2013)
  - Sale of on-line advertising, receipts from advertisers, access to on-line database not subject to TN sales and use tax
- Tennessee: Revenue Ruling # 12-30 (Nov. 21, 2012)
  - Customers use of "loyalty points" exchanged for TPP, digital products, or taxable services, the net amount of cash is the taxable sales price
  - Loyalty rewards act as a nontaxable discount
- Tennessee: Letter Ruling # 12-19 (Oct. 15, 2012)
  - IT staff "augmentation services" – taxpayer's contract employees created software, repaired and installed IT equipment and software for clients = taxable
  - Provision of non-taxable services that were separate and optional and separately itemized on invoices = not taxable

## Sales/Use Tax Developments – General (con't)

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- Virginia: Ruling of Commissioner, P.D. 13-59 (May 2, 2013)
  - Streaming video digital products not subject to communications (sales/use) tax
  - Digital video content, as well as digital books and music also exempt from general sales and use tax because they are delivered electronically

## Sales/Use Tax Developments – Cloud Computing

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- **South Carolina: Private Letter Ruling # 12-2 (June 11, 2012)**
  - Taxable database access service if customer only accesses software on remote server or ASP
  - If customer inputs data or information that is manipulated by the server = nontaxable data processing service
  
- **Tennessee: Revenue Ruling # 12-25 (Oct. 31, 2012)**
  - Is access to the “cloud” a taxable telecommunications service or taxable “ancillary service”
  - Access to software on remote server that enabled online meeting and training was taxable as an ancillary service (taxable “conference bridging service”)
  - Letter Ruling # 11-58 (Dec. 10, 2011) – access to CRM software (no download) was ruled not taxable because software resided on remote server outside TN and delivery (if any) occurred outside TN

## Sales/Use Tax Developments – Cloud Computing (con't)

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- **Texas: Comptroller of Public Accts, Letter No. 201207533L (July 31, 2012)**
  - Access to the “cloud” software is taxable as a data processing service and/or information service (20% of charge exempt)
  
- **Virginia: Ruling of Commissioner, P.D. 12-2 (Jan. 19, 2012)**
  - Access to the “cloud” software is a nontaxable service transaction because no TPP (including software) is transferred

## Sales/Use Tax Developments – TN IME Rulings

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- Revenue Ruling # 12-24 (Oct. 31, 2012)
  - Items purchased to expand a manufacturing facility qualify for the industrial machinery exemption, except those items that become part of the facility building
  - Pilings that become part of base for machinery exempt; pilings that become part of building taxable
  - Concrete that becomes part of base for machinery exempt; concrete that becomes part of building taxable
  - Rebar accessories, structural steel (same)
  - Revenue Ruling #12-02 (April 30, 2012) – similar to #12-24, plus purchases made by contractor qualify only if contractor has its own IME authorization
  
- Letter Ruling # 13-02 (Jan. 9, 2013)
  - Food processor qualified as a manufacturer and freezer racks qualified for IME

## Sales/Use Tax Developments – TN IME Rulings

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- Letter Ruling # 12-12 (July 24, 2012)
  - Third party contractor charges for fabrication of portions of products, installation of parts on products, and production reworking of parts purchased by taxpayer are exempt as sales of industrial materials and supplies
  - Contractor charges for repairing or cleaning inventory items during the process of manufacturing are exempt as sales for resale

## Tax Credit Developments

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- **Georgia: Changes to Conservation Tax Credit Program**
  - Effective Jan. 1, 2013
  - Donation of property consistent with two, no longer one, conservation purpose
  - Required restrictions on use and buffers
  - New certification and appraisal requirements
  - Add-back federal charitable contribution deduction to GA income and other changes
  
- **Louisiana: Tax Credit Registry**
  - Dept. of Revenue and Dept. of Economic Development plan to create
  - Facilitate transfer of LA transferable tax credits

## Tax Credit Developments (con't)

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- **Mississippi: Headquarters Expansion Credit**
  - Tax credit for expansion to national or regional headquarters occurring after Jan. 1, 2013
  - \$500 per new full-time employee
  - \$1,000 if salary at least 125% of state's average annual wage
  - \$2,000 if 200% of state's average annual wage
  - At least 20 new jobs required
  - Sales tax exemption for component materials used in construction of headquarters building or an addition and for sales of machinery and equipment within three months of the building's completion
  - Sales tax exemption effective April 26, 2013
  
- **Tennessee: Job Tax Credit Amendments**
  - Adventure tourism job creation threshold reduced (usually 25 qualified jobs within the investment period)
  - Tier 2 counties: 19 jobs (annual credit available for three years)
  - Tier 3 counties: 13 jobs (annual credit available for five years)

## Other Southeast State Tax Developments

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- Florida: *Orbitz, LLC v. Broward County* (July 13, 2012) and *Alachua County v. Expedia, Inc.* (Feb. 28, 2013)
  - Florida tourist development tax applies only to amount online travel company pays the hotel, not on the full amount (retail price) a customer pays the travel company
  - *Alachua County* case has been certified by the Court of Appeal to the Florida Supreme Court on April 16, 2013
- Georgia: Clarification of LLC Classification
  - DOR issued a clarification that it treats LLCs the same as the IRS
  - Are LLCs subject to the GA net worth tax?

## Other Southeast State Tax Developments (con't)

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- Mississippi: *Commonwealth Brands, Inc. v. Morgan* (April 4, 2013)
  - “Nonsettling manufacturer” law held unconstitutional; imposed fee on cigarette manufacturers that were not part of the 1997 tobacco settlement with Mississippi
  - Violated “internal consistency” (cigarettes distributed in MS and sold in another state with NSM law would be subject to multiple taxation)
- North Carolina: *Bodford v. Dept. of Revenue* (April 10, 2013)
  - NC Superior Court held that shareholders of S corporation that converted from a C corporation precluded from claiming NC bonus depreciation related to property placed in service by the C
  - NC adds back federal bonus depreciation and allows it to be deducted over five years; C corporation took two years of deduction; S shareholders denied remaining three years

## Other Southeast State Tax Developments (con't)

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- Tennessee: *Oak Ridge Land Company, L.P. v. Roberts* (Nov. 29, 2012)
  - TN regulation (Rule 1320-6-1-.20) requiring use of book value for value of excise tax deduction for charitable contributions (and not fair market value) was valid and consistent with the statute
- Tennessee: H.B. 192 – “Hall Income Tax”
  - Exemption level for those 65 and older raised from \$26,200 for individuals and \$37,000 for joint filers to \$33,000 and \$59,000, respectively
  - Food tax rate also lowered to 5.25% from 5.5% (H.B. 193)
- Tennessee: “Green” Source Energy Property Tax (Public Chap. 297)
  - Solar source property valued at an initial rate of 12.5% of total installed costs
  - Wind source property valued at an initial rate of 1/3 of total installed costs
  - Other “green” source energy property to be set by SBOE in consultation with Department of Environment and Conservation

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## Other Southeast State Tax Developments (con't)

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- Tennessee: H.B. 175 – “Final Return Status”
  - If start the process of ceasing to exist, deemed to be “final return status” and must file a return for all subsequent tax periods regardless of whether any remaining in-state activity
- Texas: *City of San Antonio v. Hotels.Com, L.P.* (April 4, 2013)
  - Federal district court ruled that city hotel occupancy tax should be imposed on the retail price of hotel rooms, not the amount the online travel company paid the hotel
- Texas: *DTWC Corp. v. Combs* (April 11, 2013)
  - Hotel’s purchase of “hotel consumables” (soap, shampoo, mouthwash, shower caps, etc.) qualified for the resale exemption from sales and use tax.

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## Unclaimed Property

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- Tennessee: CFPB-2012-0036
  - Federal Consumer Financial Protection Bureau determined that TN's unclaimed property statute applicable to gift cards is preempted by federal law
  - TN: gift cards with dormancy charges or expiration date are subject to the TN statute
  - TN's two-year dormancy period determined to violate the federal prohibition on gift cards having less than five year expiration dates