

State and Local Taxation: Headline News and Trends

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Special Guest:
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President, Taxpayers Federation of Illinois

Taxpayers' Federation of Illinois



TAXPAYERS'
FEDERATION
OF ILLINOIS

About TFI:

Nonprofit research and advocacy group focused on State and Local Taxes and Tax Policy in Illinois, since 1940

- Provide spin-free data for policy-makers and the public
- Lobby for sound tax policy, not specific taxpayers (or industries)
- Act as an information conduit between policy-makers and the taxpayers impacted by their actions

Today's Agenda

Section I: Megatrends	(3-15)
Section II: Business Activities Taxes	(16-42)
Section III: Transaction Taxes	(43-55)
Section IV: Miscellaneous	(56-67)

Megatrends and Developments

US Supreme Court



Still pending: *Delaware v. Pennsylvania* and *Arkansas v. Delaware*,
Dkt. Nos. 220145 and 220146 (consolidated October 3, 2016)
Escheat of unclaimed property; at Special Master

Megatrends and Developments

US Supreme Court



Arguments held December 1, 2020: *CIC Services, LLC v. IRS*, Dkt. No. 19-930
Does the Anti-Injunction Act bar challenges to tax reporting and recordkeeping rules?
Possible interplay with the Tax Injunction Act (*see DMA v. Brohl*, 135 S. Ct. 1124 (2015))

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Megatrends and Developments

US Supreme Court



Cert. Petition Filed: *Americans for Prosperity Foundation v. Xavier Becerra*, Nos. 19-251/19-255. Can state require disclosure of charitable donors' identities? On Nov. 24, 2020, the Solicitor General filed a brief supporting the petition for certiorari.

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Megatrends and Developments

US Supreme Court



Cert Denied October 19, 2020:
Rogers County Bd. of Tax Roll Corrections v. Video Gaming Technologies, Inc.,
No. 19-1298. *But see* Thomas, J. dissent:

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Megatrends and Developments

US Supreme Court

“Earlier this year, the Court “disregard[ed] the ‘well settled’ approach required by our precedents” and transformed half of Oklahoma into tribal land. *McGirt v. Oklahoma*, 591 U. S. ___, ___-___ (2020) (ROBERTS, C. J., dissenting) (slip op., at 1-2)... That decision “profoundly destabilized the governance of eastern Oklahoma” and “create[d] significant uncertainty” about basic government functions like “taxation.” Ibid. The least we could do now is mitigate some of that uncertainty. This case presents a square conflict on an important question: Does federal law silently pre-empt state laws assessing taxes on ownership of electronic gambling equipment when that equipment is located on tribal land but owned by non-Indians?”

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Megatrends and Developments

COVID 19 -- Revenues



State revenue numbers from income and sales taxes exceed expectations

Megatrends and Developments

COVID 19



Shelter-in-place consequences. Can we treat you as working there when you are really here? Can we treat you as working here when you are really there? What are the business nexus consequences? Throwback? What about payroll taxes? Etc.

Megatrends and Developments

US Supreme Court



***New Hampshire v. Massachusetts,
No. 220154, Motion for Leave to File a Bill of Complaint
(October 19, 2020)***

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Megatrends and Developments

COVID 19



Constantly changing. But a few items:

- Federal legislation?
- Ohio brawl.
- Massachusetts update.
- OECD example (Spain ruling regarding presence of a resident of a tax haven country).

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Megatrends and Developments

Due Process – Personal Jurisdiction

Louisiana: Petition to impose taxes on out of state corporation dismissed due to lack of personal jurisdiction.

Have we seen this before in Louisiana? Yes...



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Megatrends and Developments

Due Process – Personal Jurisdiction

From 2005: *Bridges v. Autozone*, 900 So 2d 784 Calogero, J. concurring in denial of rehearing:

In my view, the court's decision improperly conflates two issues that should be treated separately. The first of those issues focuses on whether a state has jurisdiction or authority to impose a given tax ('authority to tax'), while the second focuses on whether the prospective taxpayer has sufficient contacts with the state to allow that state's courts to exercise personal jurisdiction over that taxpayer in the state's suit to collect the tax ('personal jurisdiction').

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Megatrends and Developments

Due Process – Personal Jurisdiction

Be on the look-out for taxing bodies asserting that tax “substantial nexus” has the playing field entirely to itself.

It does not.



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Business Activities Taxes

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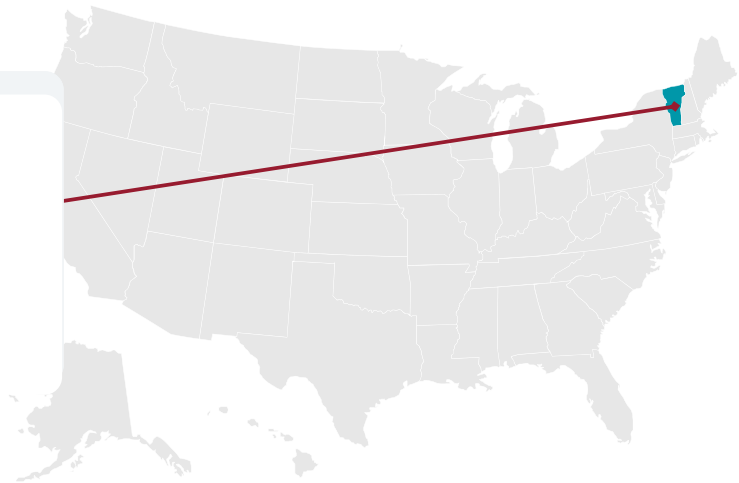
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Business Activities Taxes

Nonbusiness Income

Vermont.

Gain on sale of FCC licenses was nonbusiness income taxable in Vermont. Penalties were properly imposed.

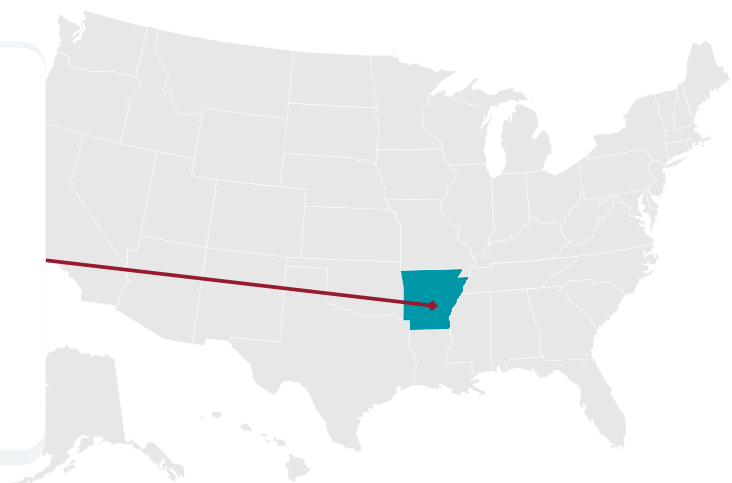


Business Activities Taxes

Business Income

Arkansas.

State's position is reviewed *de novo*, so no presumption of correctness for final assessment or determination. However, repeated sales of state credits in the regular course of business satisfied the transactional test of business income.

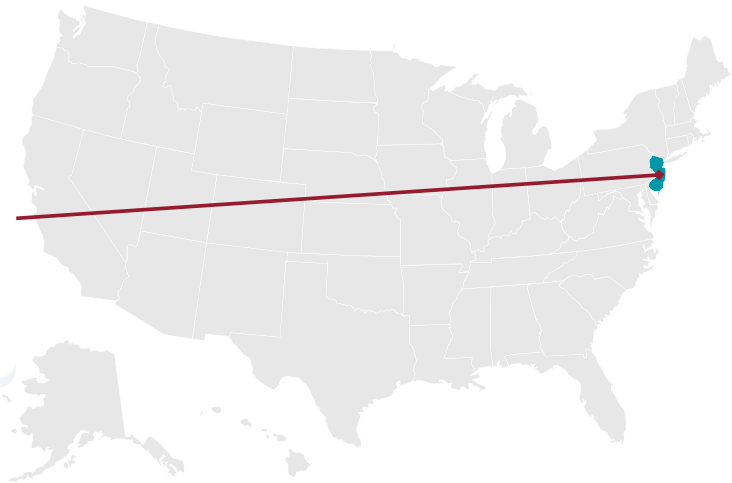


Business Activities Taxes

Retractive Surtax Enacted

New Jersey.

2.5% corporate surtax enacted. Effective for all years beginning on or after January 1, 2020.

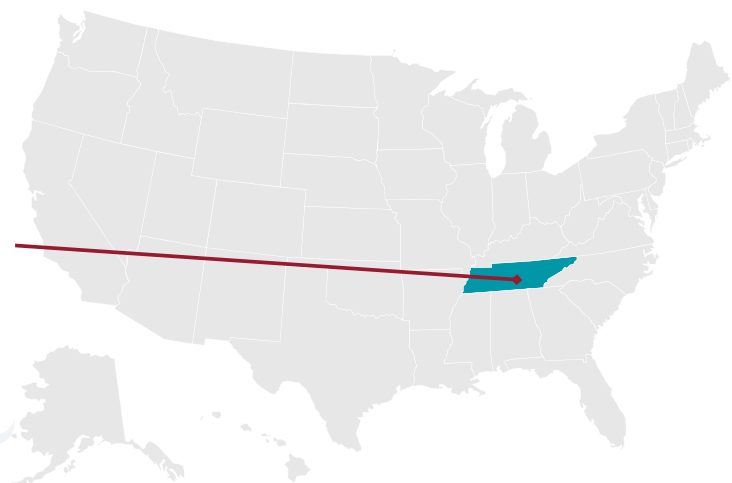


Business Activities Taxes

Taxability Under State Law

Tennessee.

Ruling that foreign corporation with in-state inventory sometimes shipped to in-state customers is not subject to Tennessee franchise tax.

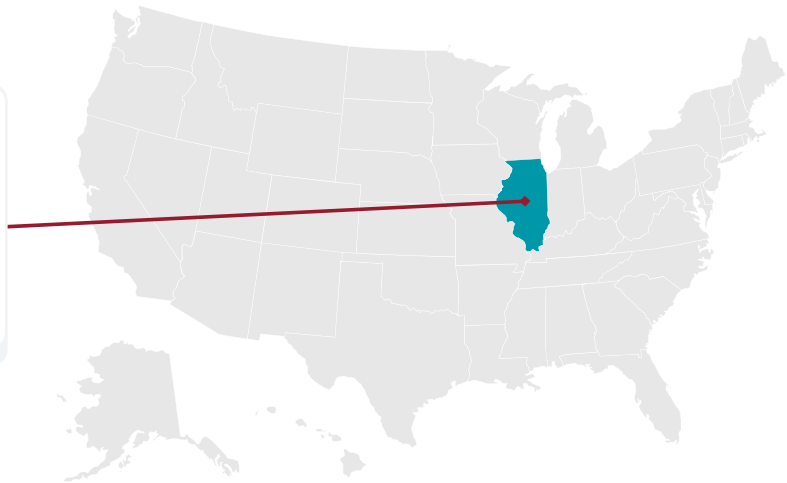


Business Activities Taxes

Policy: World-Wide Combined Reporting?

Illinois.

Illinois continues to flirt with world-wide combined reporting.



Business Activities Taxes

Policy: World-Wide Combined Reporting?



New Hampshire General Court (legislature) considering a bill to repeal water's edge combined reporting. HB 1567. Last action on October 5, 2020 **“Interim Study Report : Recommended for Future Legislation.”**

Business Activities Taxes

Policy: World-Wide Combined Reporting? And More?



Montana Budget and Policy Center:

Recommendations: Due to decline in corporate income tax collections, Montana should repeal water's edge election, repeal NOL carrybacks, and enact a gross receipts tax.

Business Activities Taxes

Policy Trend: Services

1 Move to single-factor, market-based sales, apportionment formula. Consequences:

- Nexus determinations via apportionment results
- Justifiable apportionment results?

2 P.L. 86-272 interpreted to not protect sales of services

Business Activities Taxes

Policy Trend: Services

History in 120 seconds (1/3):

YEAR

1957

UDITPA developed.
Equally-weighted three-factor apportionment formula with cost of performance (COP) for sales of other than TPP.

Q/A: *Why this approach?*

Seeking each state's "contribution...toward the production of the income..." (Pierce, Taxes "The Uniform Division of Income for State Tax Purposes" Oct. 1957 at 780).

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Business Activities Taxes

Policy Trend: Services

History in 120 seconds (2/3):

YEAR

1966/7

Multistate Tax Compact: Incorporated UDITPA.

YEAR

1978

Moorman Manufacturing Company v. Bair, Director of Revenue of Iowa, 437 U.S. 267.

Q:

In Moorman, what did the Supreme Court actually say? And see Brennan, J. dissent, (which further references a dissent from 1964): "Where a sale exhibits contacts with more than one state...it is the commercial activity within the state, and not sales volume, which determines the State's power to tax, and by which the tax must be apportioned."

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Business Activities Taxes

Policy Trend: Services

History in 120 seconds (3/3):

YEARS

**2015
and
2016**

Several state courts held that the Multistate Tax Compact is not binding on the states

Business Activities Taxes

Policy Trend: Services

2020 – Where are we now?

38 states (plus D.C. and NYC) have moved away from an equally weighted three-factor formula using COP for sales

33 states have adopted a market-sourcing rule for sales of other than tangible personal property

23 states (plus D.C. and NYC) have adopted a single-factor (sales) formula

22 states have a single-factor formula and market-sourcing

Source: Bloomberg Law: Tax Chart Builder Nov. 22, 2020

Business Activities Taxes

Policy Trend: Services

Using market-based apportionment as the basis for apportioning income.

A *primary* exposure that the states have created for themselves

- States are using (and increasingly will use) these formula to evaluate tax presence
- Under *Complete Auto Transit v. Brady*, 430 U.S. 274 (1977) substantial nexus and fair apportionment are distinct tests
- Using apportionment results to determine income tax presence is presumptively improper, and the states know it. See e.g., Illinois reg. 100.9720 (“However, the fact that Article 3 of the IITA requires a non-resident taxpayer to allocate or apportion income to this State does not create a presumption that the taxpayer has nexus.”)

Business Activities Taxes

Policy Trend: Services



Using market-based apportionment as the exclusive basis for apportioning income.

A *secondary* exposure that the states have created for themselves...

Business Activities Taxes

Policy Trend: Services

How can it be true that:

- an equally weighted three-factor formula with sales of services sourced based on cost of performance fairly measures a state's "contribution...toward the production of the income..." **and that**
- a single-factor (sales) formula based on market-sourcing also fairly measures a state's "contribution...toward the production of the income..." ?



Business Activities Taxes

Policy Trend: Services



Battle looming as to whether P.L. 86-272 (15 U.S. Code §381) already protects sales of services.

What does this mean for economic nexus states?

Business Activities Taxes

Policy Trend: Services

P.L. 86-272 (15 U.S.C. §381) provides:
“No State...shall have power to impose...a net income tax on the income derived within such State by any person from interstate commerce if the only business activities within such State by or on behalf of such person during such taxable year are either, or both, of the following: (1) the solicitation of orders by such person, or his representative, in such State for sales of tangible personal property...”



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Business Activities Taxes

Policy Trend: Services

Does P.L. 86-272 protect vendors of services lacking physical presence in the state?



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Business Activities Taxes

Policy Trend: Services

Some pro-tax advocates believe that P.L. 86-272 is limited to sellers of tangible personal property (i.e., the law does not protect vendors of services who lack physical presence in the state):

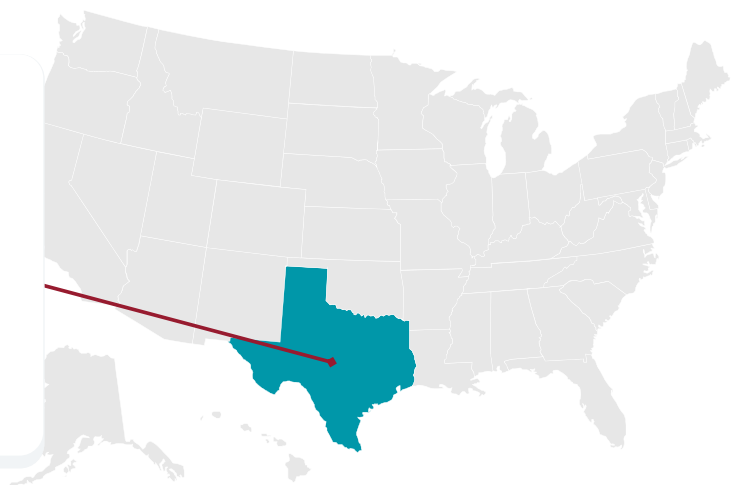
What P.L. 86-272 says: No State...shall have power to impose...a net income tax on the income derived within such State by any person from interstate commerce...

What pro-tax advocates read: No State...shall have power to impose...a net income tax on the income derived within such State by any person from *the sale of tangible personal property in* interstate commerce...

Business Activities Taxes

Insurance Taxes

Texas.
Insurance was surplus lines insurance and not “export property” within the meaning of Texas Administrative Code. Also, the imposition of the insurance premium tax did not violate the US Constitution’s Commerce or Import-Export Clauses.

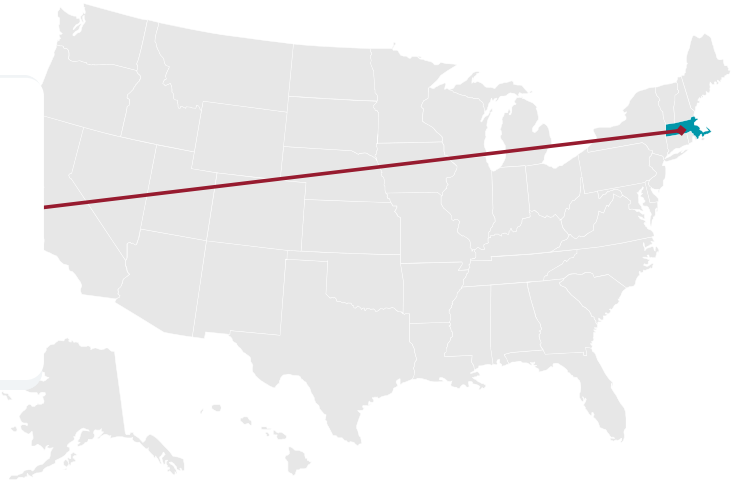


Business Activities Taxes

Tax on Sale of Pass-Through Interests

Massachusetts.

Complicated Facts: A nonresident S corporation was subject to income tax on the gain on the sale of its interest in a Massachusetts LLC that was treated as a partnership.



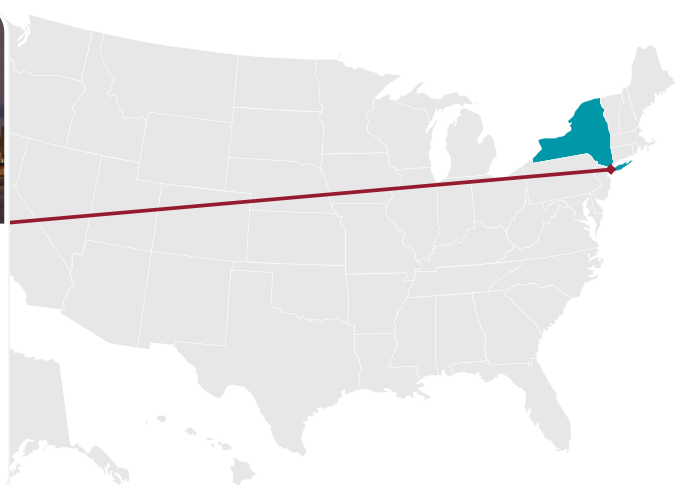
Business Activities Taxes

No Tax on Sale of Pass-Through Interests



New York City

Complicated Redacting: No Unincorporated Business Tax on LLC due to its members' sales of their interests in LLC. And no UBT on selling member due solely to its holding and disposition of interest in LLC.



Business Activities Taxes

Limited Partners

Proposed Regulation replaces “*is not doing business*” with “*does not have physical presence*” and asserts that the obtaining of a Texas use tax permit creates franchise tax presence.



Business Activities Taxes

Sourcing Receipts



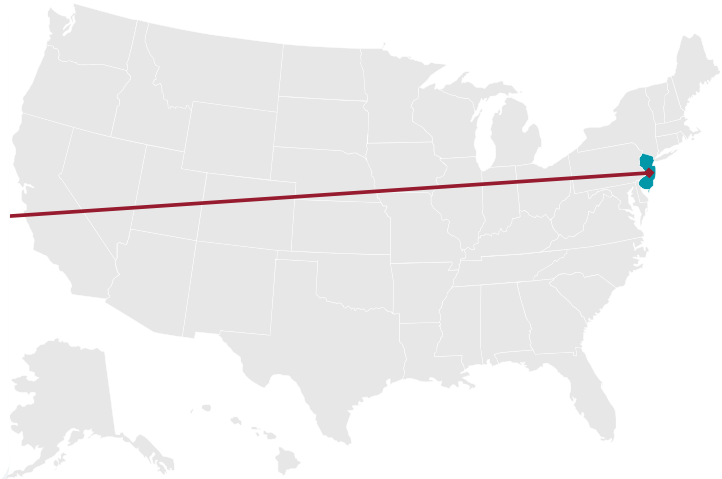
Ohio Supreme Court grants Commercial Activity Tax refund claim, finding that the benefit of the company’s service was “used or received” outside of Ohio.

Business Activities Taxes

Insurance Taxes

New Jersey.

State Supreme Court affirmed appellate division's holding that premiums paid to an (unauthorized) captive insurer are not subject to NJ premiums tax. (Tax applies to surplus lines premiums only.) Unusual: One paragraph affirmance and 17-page dissent.



Save The Date: Next State and Local Taxation: Headline News and Trends

MARCH

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11:00 a.m. Eastern

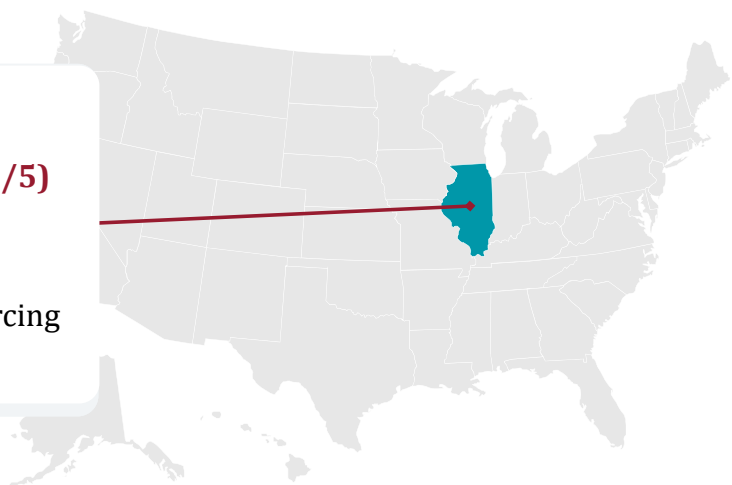
Transaction Taxes

Transaction Taxes

Unequal Sales and Use Taxes

Illinois' **"Level the Playing Field" Law (1/5)**

Enacted South Dakota type thresholds, effective 10/1/2018.
Ignored marketplaces. Local sourcing still origin-based.

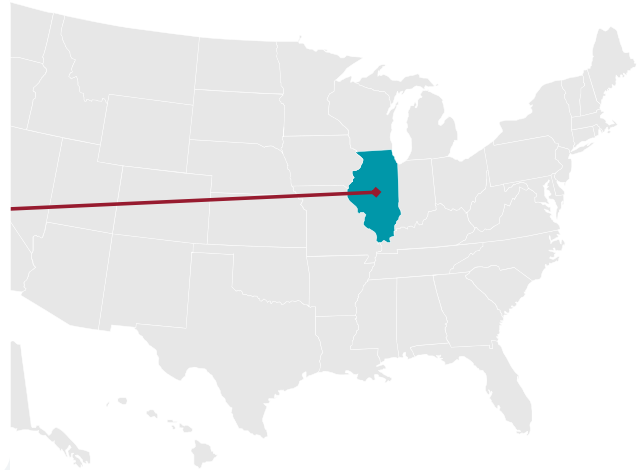


Transaction Taxes

Unequal Sales and Use Taxes

Illinois' **"Level the Playing Field" Law (2/5)**

Effective 1/1/2020: marketplace *facilitators* exceeding same thresholds must collect and remit Use Tax on all sales. Marketplace *sellers* are off the hook. Local sourcing irrelevant because no local use tax. However: ROT (sales tax) was not amended, so sellers with Illinois presence still owed local tax if sale originated in Illinois.

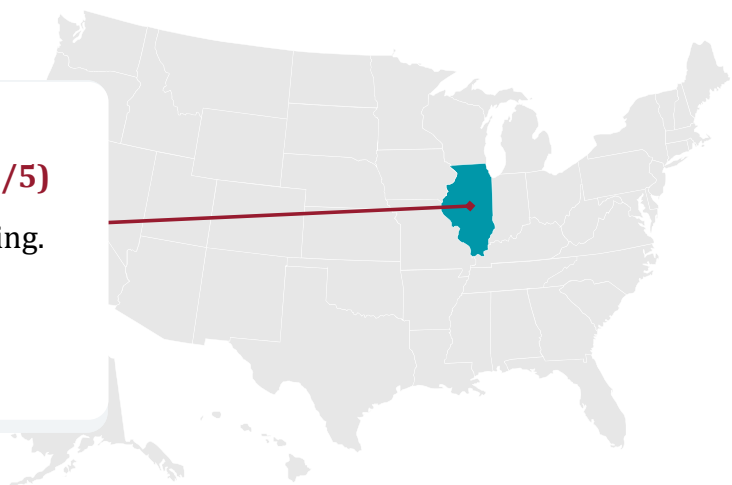


Transaction Taxes

Unequal Sales and Use Taxes

Illinois' **"Level the Playing Field" Law (3/5)**

Effective 1/1/2021: hybrid sourcing. Use Tax, Origin-based ROT and Destination-based ROT are all possibilities, depending on facts



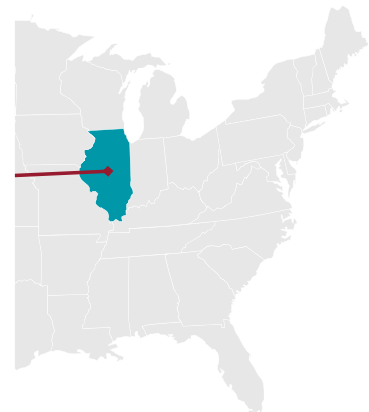
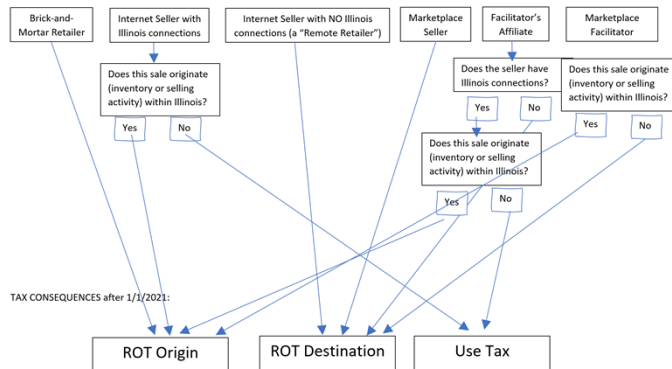
Transaction Taxes

Unequal Sales and Use Taxes

Illinois' "Level the Playing Field" Law (4/5)

Effective 1/1/2021:

TYPES OF SELLERS/SALES:



Transaction Taxes

Unequal Sales and Use Taxes

Illinois' "Level the Playing Field" Law (5/5).

Example of In-State v. Out-of-State Difference

"Carol buys two new chairs for office in Downers Grove, Illinois, from two nearly identical sellers."

Seller One:

- Sells through its own website
- Meets the *Wayfair* thresholds for Illinois
- HQ and warehouse are in Iowa
- All employees are in Iowa
- Chair shipped by common carrier
- Meets the definition of "remote seller"
- **Tax due: 8.0%** (IL 6.25%, DuPage county 0.75%, Downers Grove 1.0%)

Seller Two:

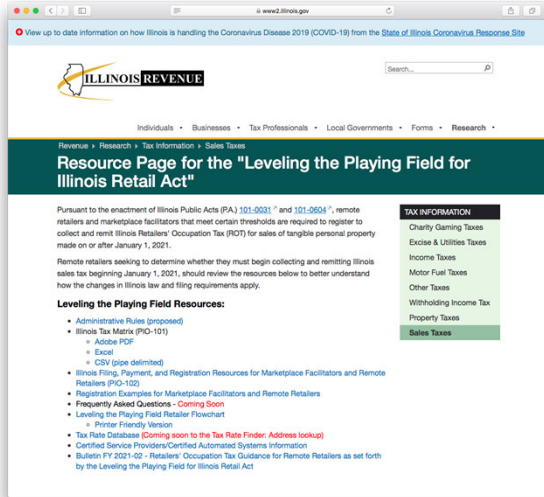
- Sells through its own website
- Meets the *Wayfair* thresholds for Illinois
- HQ and warehouse are in Iowa
- All employees are in Iowa, **except Tax VP lives and works in Chicago**
- Chair shipped by common carrier
- Does not meet the definition of "remote seller"
- **Tax due: 6.25%**

Transaction Taxes

Unequal Sales and Use Taxes



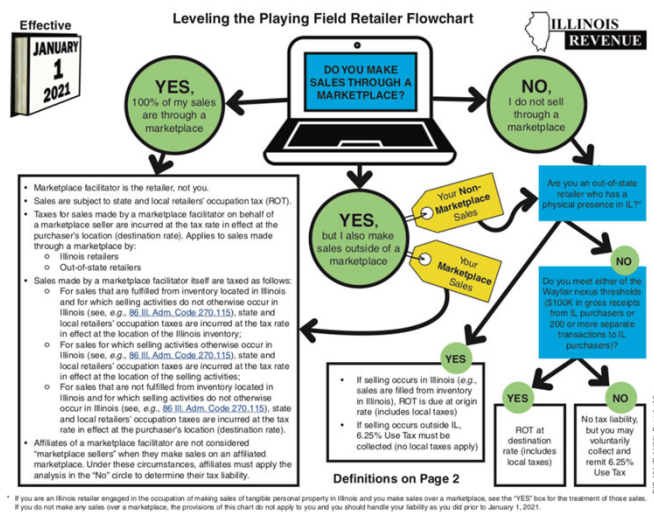
For the Illinois Department of Revenue's guidance on this, see its "Resource Page for the 'Leveling the Playing Field for Illinois Retail Act'", which includes the following alternative flowchart...



Transaction Taxes

Unequal Sales and Use Taxes

The Department's Chart ("Definitions on Page 2"):

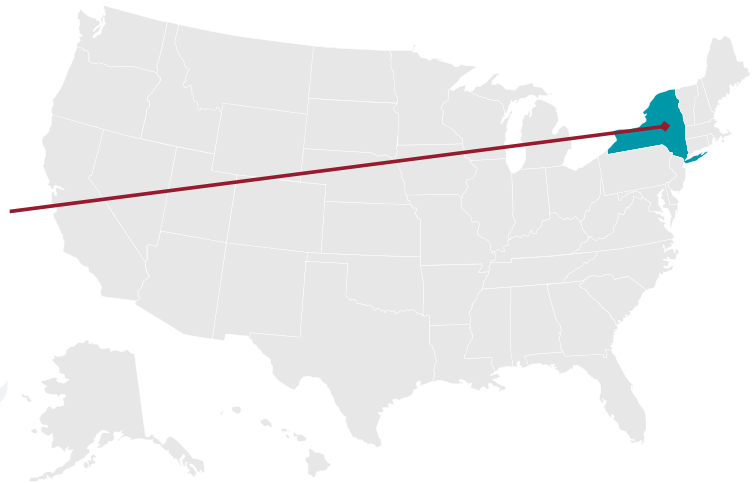


Transaction Taxes

False Claims Action

New York.

False claims action filed against auction house alleging participation in a scheme to defraud the state of taxes on \$27 million in sales.

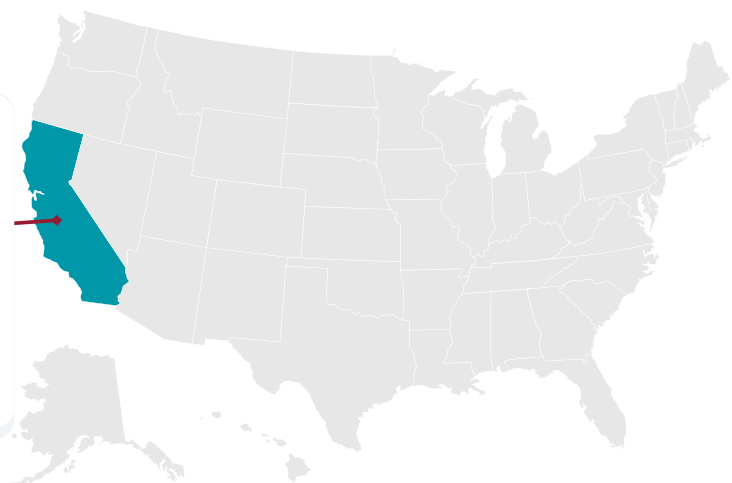


Miscellaneous

Unlawful bias?

California.

Online businesses file suit alleging severe state bias in determining who is responsible for collecting sales taxes “all to preserve” economic and political subsidies.

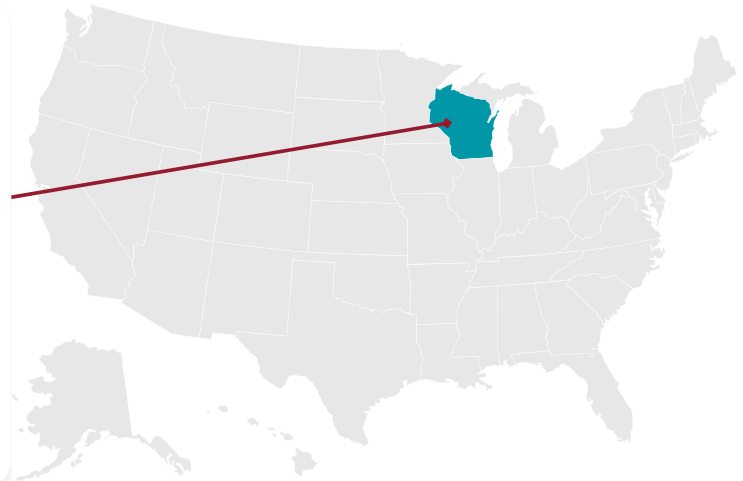


Transaction Taxes

Aircraft Leasing

Wisconsin.

Is an aircraft lessor required to pay sales tax on charges to its customers for aircraft repairs and maintenance when, under the leases, the lessees are required to reimburse the lessor for their proportionate share of those costs? Does the answer change if the amounts are separately invoiced to the lessees?

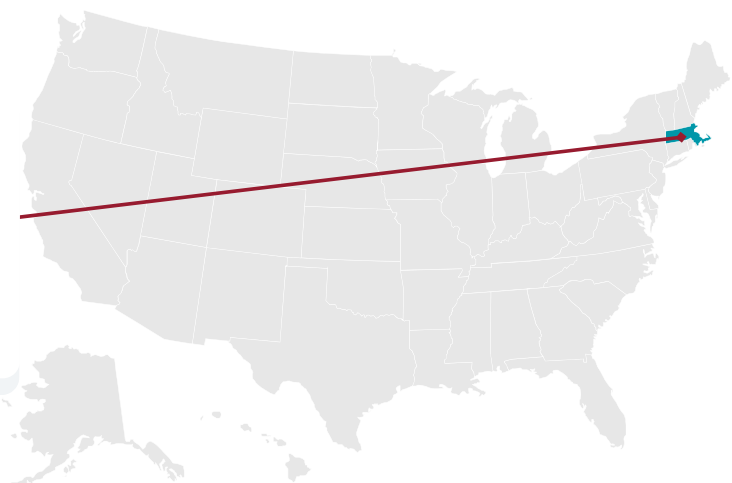


Transaction Taxes

Real Time Collections?

Massachusetts.

2021 Budget proposes collecting sales taxes in real time.
Will refunds be paid in the same time-frame?

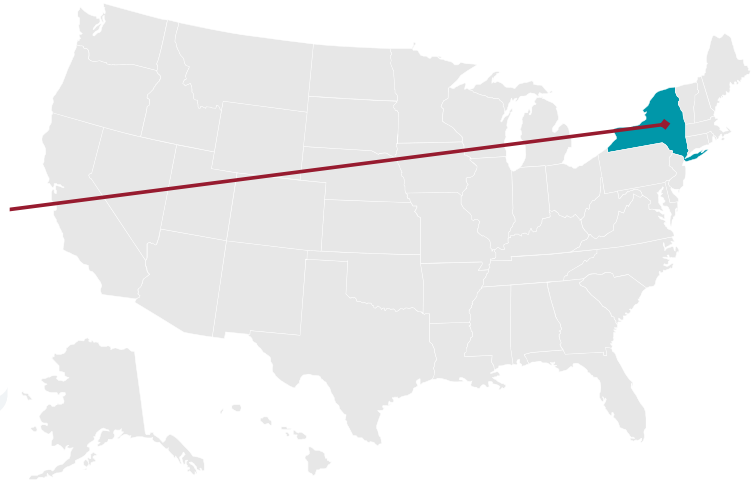


Transaction Taxes

Digital Services

New York State.

Digital service allowing users to track marketing effectiveness was not subject to sales tax. But would be taxed if bundled with the sale of third-party software license.



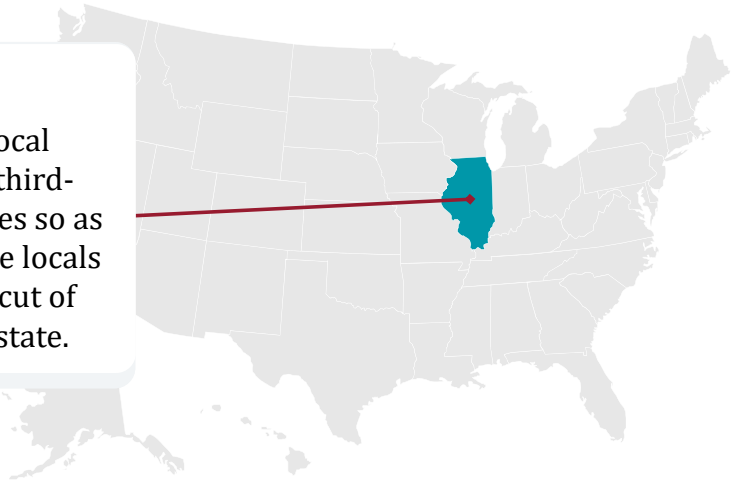
Miscellaneous

Miscellaneous

Outside tax adjusters/collectors

Illinois.

Effective 1/1/2021 local governments can hire third-parties to audit businesses so as to determine whether the locals are receiving their full cut of taxes collected by the state.



* 57

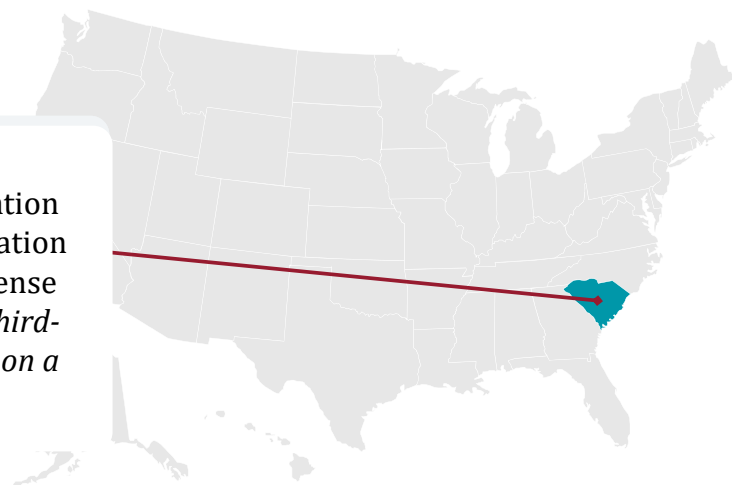
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Miscellaneous

Business License Tax: Bitter with the Sweet

South Carolina.

New law standardizes application forms, deadlines, and classification systems for local business license taxes. *Also authorizes use of third-party tax collectors who work on a contingent fee basis.*



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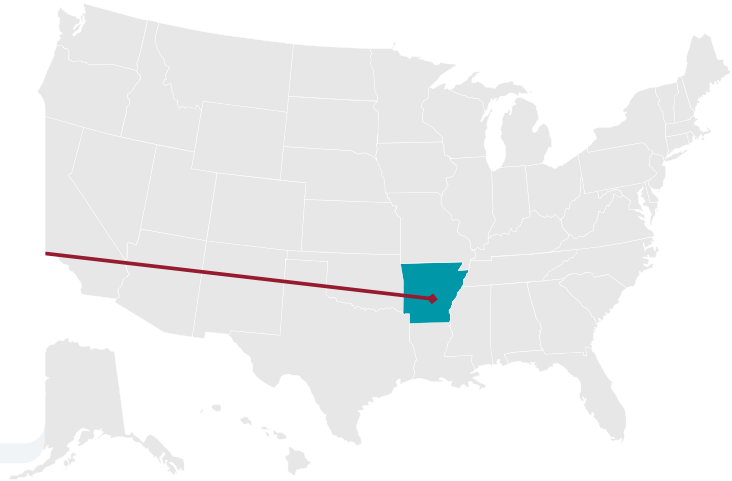
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Miscellaneous

Public Purpose Exemption

Arkansas.

Airport property qualified for the “exclusive public-purpose” exemption from property taxes when not leased to private parties – even though the airport was seeking private party lessees.

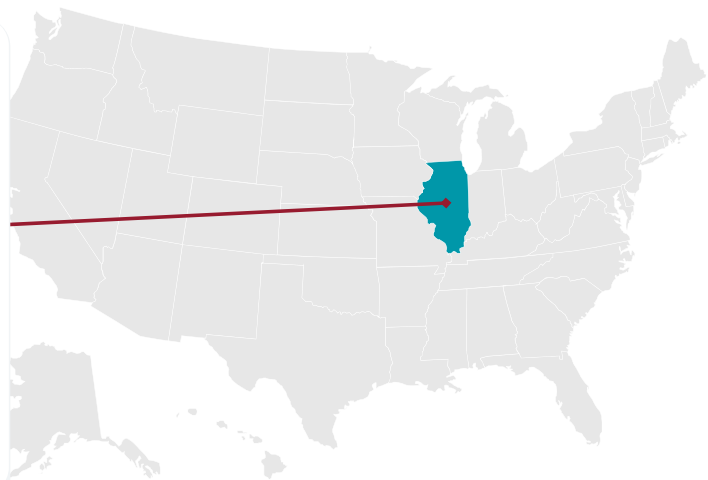


Miscellaneous

Endless Litigation



The circus is in town! Cook County alleges no state remedy for claimed harm--and then argues that Tax Injunction Act bars suit in federal court. Records destroyed, and so much more...



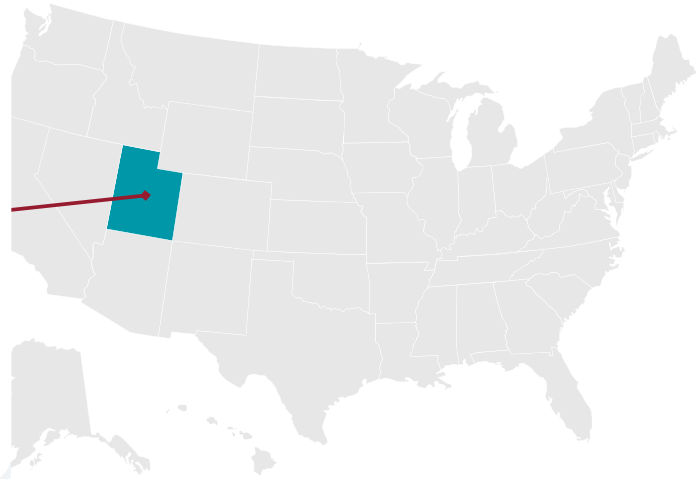
Miscellaneous

Oops!



Utah.

13,000 notices asserting penalties and interest for late filing were issued in error. Tax Commission Sending Corrected notices.

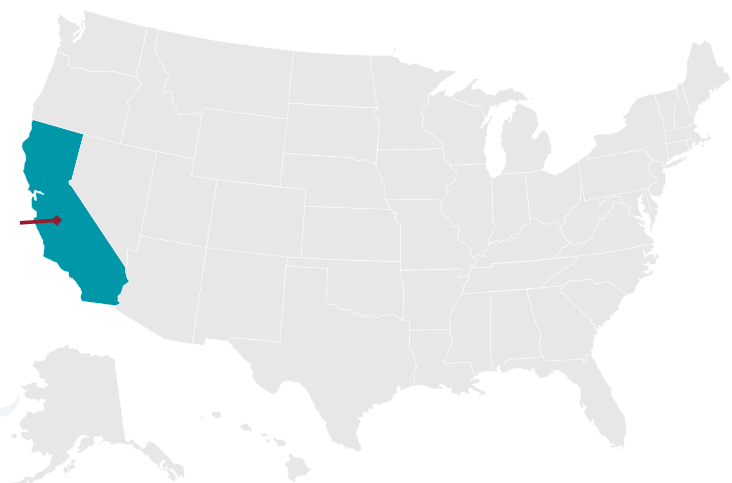


Miscellaneous

Foreign Employees

California.

New law eases compliance for qualifying nonresident aliens traveling to California for work. No need for SSN or individual TIN.

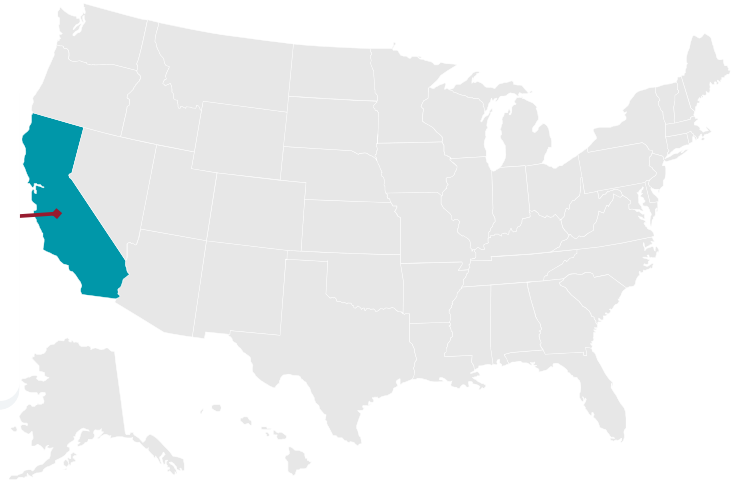


Miscellaneous

Tax or Fee?

California.

California Supreme Court to decide:
Is a bridge toll increase a tax
requiring a 2/3 majority vote? Or is
it a fee for which the 55% approval
by voters is satisfactory?

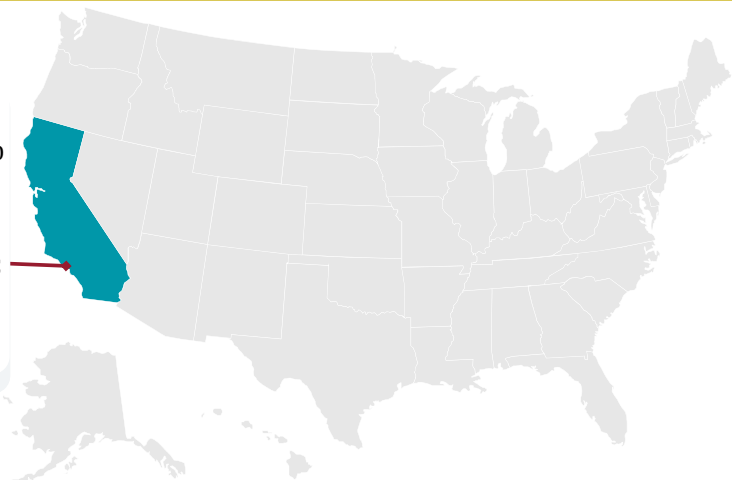


Miscellaneous

Tax or Fee?

Los Angeles.

Annual utility overcharges of 5-8%
of gross revenue that are
transferred to the city's general
fund rather than returned to users
or spent on infrastructure are not
"taxes" requiring voter approval.



Miscellaneous

Misclassifying Employees

Washington D.C.
\$200,000 penalty imposed on general contractor due to its subcontractor's misclassification of employees as independent contractors.

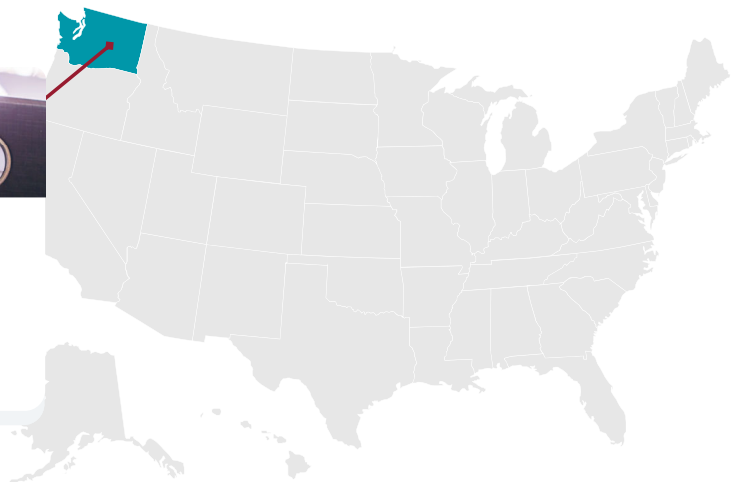


Miscellaneous

Right to Earn a Living



Seattle payroll tax challenged as an illegal excise tax on the right to work



Miscellaneous

Evasion Settlement

New York Attorney General obtained \$4.7 million from supermarket chain for paying employees “off the books,” fraudulently recording returns, and fraudulently making unrecorded cash sales.



Questions????



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David Fruchtman provides state and local tax planning and controversy advice. His representations involve almost all subnational taxes for businesses and individuals, including income, franchise, sales, use, real property transfer, and a variety of other state and local taxes. His clients include public and privately held heavy equipment manufacturers, marketing companies, travel lodging providers, and vehicle rental companies, as well as mid-sized retailers and other businesses.

David's tax planning work includes tax efficient structuring of businesses and transactions, and regularly requires working with tax authorities to obtain favorable guidance, as circumstances require. He advises foreign companies expanding into the United States, and his experience includes assisting an American affiliate of an Israeli company in one of Wall Street's most successful IPOs of 2010.

You can read David's full firm biography [here](#).

Carol Shuman Portman

President, Taxpayer's Federation of Illinois



Carol Shuman Portman has been the President of the Taxpayers' Federation of Illinois since January 2013. Prior to joining TFI in the fall of 2012, she was Assistant General Counsel – Tax with Sears Holdings Corporation for 12 years, where she was responsible for providing legal support on all state and local tax matters nationwide. Ms. Portman held similar in-house corporate tax counsel positions with Ameritech (now AT&T) and Waste Management Corporation. Her first legal experience in the state and local tax area was in the Chicago office of McDermott, Will & Emery. A former chair of TFI, Ms. Portman served on the Board of Trustees from 2000 - 2012, and the Executive Committee from 2002 - 2012. Originally from Sullivan, Illinois, Carol's first exposure to Illinois government and fiscal policy came at an early age—her father, Charles W. Shuman, was a delegate to the 1970 Illinois Constitutional Convention and her grandfather, Charles B. Shuman, was president of the Illinois Farm Bureau and the America Farm Bureau Federation. She is a 1984 graduate of the University of Illinois and received her law degree in 1987 from the University of Michigan Law School. She lives in Downers Grove with her husband, Chris. They have two almost-grown daughters, Erin and Katie.

Disclaimer

This presentation and these materials address recent state and local tax developments. Because of the generality of the information provided, the materials and information might not be applicable in all situations and should not be acted upon without specific legal advice based on particular situations. Neither participation in this presentation nor receipt of these materials establishes an attorney-client relationship.

Notes

SLIDE 13

Robinson v. Jeopardy Productions, Inc, No. 2019 CA 1095 (LA Ct. App. 10/21/20).

SLIDE 17

Vermont National Telephone Company v. Dept of Taxes, 2020 VT 83 (VT S. Ct. 10/9/20)

SLIDE 18

American Honda Motor Co., Inc. v. Walthier, Dept of Fin. and Admin,
No. CV-19-700 (S. Ct. AK, 10/29/20)

SLIDE 19

P.L. 2020, c. 95 (September 29, 2020)

Notes

SLIDE 20

Revenue Ruling #20-08 (10/9/20).

SLIDE 23

“Policy Basics: Corporate Income Taxes in Montana” (November 2020)

SLIDE 36

Rekerdres & Sons Insurance Agency v. Hegar, No. 07-19-00209-CV
(Texas Ct. App. September 24, 2020)

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SLIDE 37

VAS Holding & Investments LLC v. Commissioner, ATB Dkt. Nos. C332269 & 332270
(October 23, 2020)

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FLR 20-5002 (July 10, 2020)

SLIDE 39

TRD-202004929 (November 20, 2020) proposing revisions to 34 TAC §3.586.

SLIDE 40

Defender Security Company v. McClain, Slip Opinion No 2020-Ohio-4594 (September 29, 2020)

SLIDE 41

Johnson & Johnson v. Director, Division of Taxation, (A-51-19) (083612)

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SLIDE 44 Paragraph (9) of definition of “retailer [or serviceman] maintaining a place of business in this state” at 35 ILCS 105/2 (Illinois Use Tax) and 35 ILCS 110/2 (Illinois Service Use Tax). Public Act 100-0587

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35 ILCS 105/2d and 35 ILCS 110/2d. Public Act 101-0009

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Numerous changes throughout the sales and use tax laws. Public Act 101-0031 and 101-0064

SLIDE 51

People of State of New York v. Sotheby's, Inc., (Complaint filed with the Supreme Court of New York County, November 6, 2020)

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SLIDE 52 *Online Merchants Guild v. Maduros, Director CDTFA*. USDC E.D. CA, Sacramento Div. Case 2:20 (filed September 29, 2020).

SLIDE 53

Citation Partners, LLC v. DOR, Dane County Circuit Court August 20, 2020), appeal pending.

SLIDE 55 and 57

NYS TSB-A-20(27)S June 30, 2020. Illinois Public Act 101-0628.

SLIDE 58

H. 4431, signed by Governor McMaster on September 30, 2020 and generally effective January 1, 2022.

SLIDE 59

City of Little Rock v. Pulaski County Assessor, 2020 Ark. 399 (Ark. S. Ct. December 3, 2020)

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SLIDE 60 *Maria Pappas, Cook County Treasurer, et al., Petitioners v. A.F. Moore & Associates, Inc., et al*, 7th Circuit, 1/29/2020, Nos. 19-1971,19-1979, cert denied 11/16

SLIDE 61
Utah State Tax Commission release (December 1, 2020)

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A.B. 2660, generally effective January 1, 2021.

SLIDE 63
Howard Jarvis Taxpayer's Association v. Bay Area Toll Authority, Case No. S263835
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Humphreville v. City of Los Angeles, B299132 (CA Ct. App. December 3, 2020)

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Office of the Attorney General for the District of Columbia press release (October 1, 2020).

SLIDE 66
Greater Seattle Chamber of Commerce v. City of Seattle, No. 20-2-17576-5 SEA (Sup. Ct. King County Complaint filed December 8, 2020)

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NY AG press release December 7, 2020