

MACPA MICHIGAN TAX CONFERENCE

Sales Tax & SSTP – Cases and Court Decision You Must Hear

Presented By: Carolynn S. Iafrate
Marilyn Wethekam

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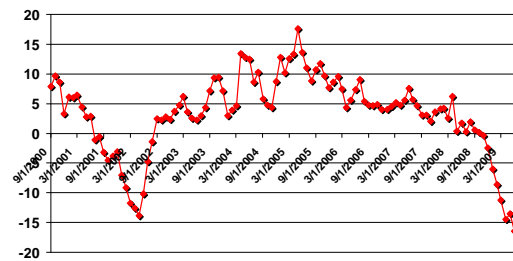
Agenda

- ▶ Fiscal Overview
- ▶ Nexus
- ▶ Revenue Raisers
- ▶ Hot Audit Issues
- ▶ Streamlined Sales Tax Project

Fiscal Overview

State Revenues – Total Taxes

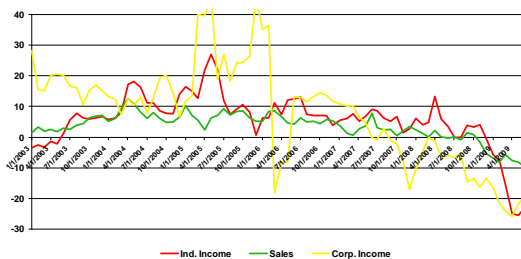
Year over year change on a monthly basis – 3-month moving average



Source: Federation of Tax Administrators

Breaking it Down By Source

Year over year change on a monthly basis – 3-month moving average

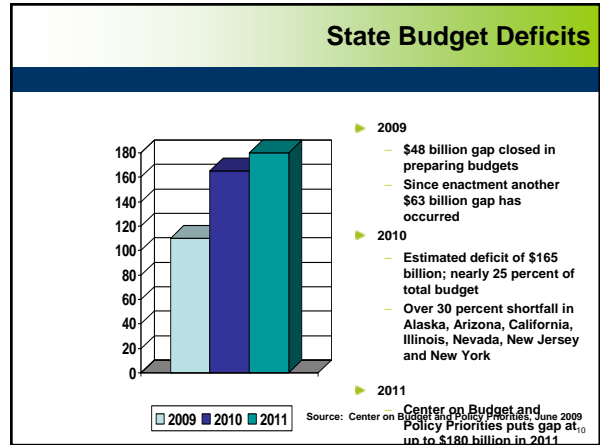
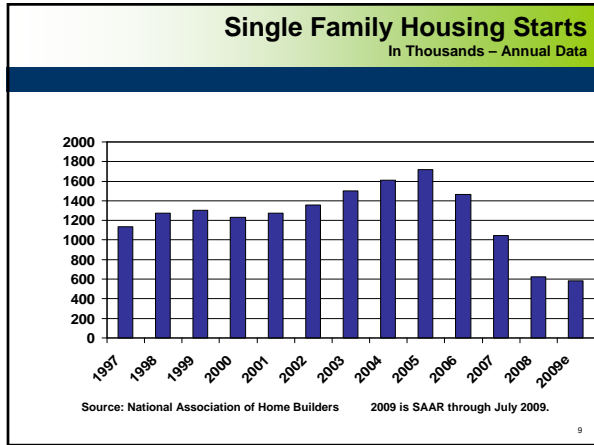
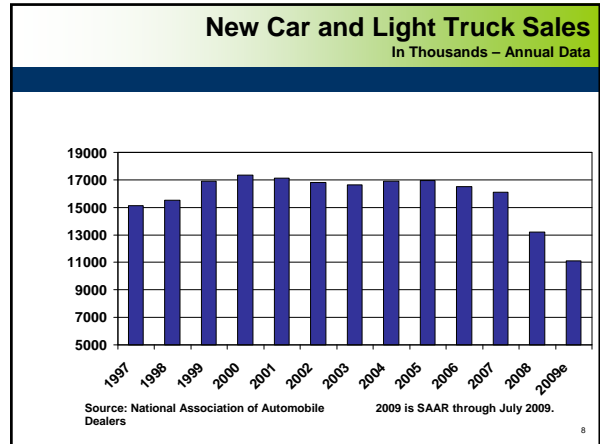
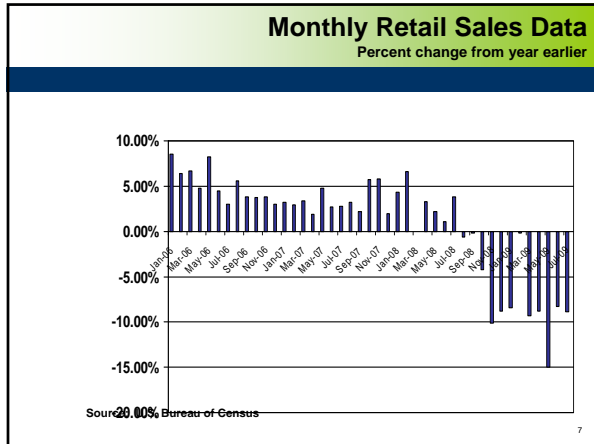


Source: Federation of Tax Administrators

NCSL Update – April 2009

- ▶ **Personal Income Tax**
 - FYTD receipts below prior year in 35 states
 - Greater than 10 percent drop in 21 states; more than 20 percent in five states
 - Three states – AL, KS, ND – reported year-over-year gains
- ▶ **Sales Tax**
 - FYTD receipts below prior year in 31 states
 - More than 10 percent below in five states
 - Nine states with year-over-year increase
- ▶ **Corporate Income Tax**
 - FYTD receipts were below prior year in 37 states
 - Greater than 10 percent in 34 states; more than 20 percent in 24 states
 - Two states – AR and MT – with year-over-year increase

Source: NCSL, State Tax Performance Through April 2009



Revenue Raisers

- ### Revenue Raisers
- **Nexus**
 - Discussed in next section.
 - **Proposals Related to Taxation of Digital Goods**
 - **Proposals Related to Taxation of Services**
 - **Reduced Vendor Discounts**
 - CO, NV, WI, SST
 - **Sales Tax Rate Increases**
 - CA, DC, MA, NC, & NYC

Revenue Raisers - Amnesty Programs

► Delaware – Voluntary Tax Compliance Initiative (H.B. 268, Laws of 2009)

- September 1 – October 31, 2009
- Waiver of penalty and interest on delinquencies owing as of Sept. 1, 2009 and on tax associated with previously unfiled returns or undisclosed amounts for periods ending prior to Jan. 1, 2009
- Payment of tax due must be made at time of filing or under payment plan prior to June 30, 2010
- No tax, interest or penalty will be assessed for periods prior to January 1, 2004 for participating taxpayers
- Applies to all taxes and fees administered by Division of Revenue

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Revenue Raisers - Amnesty Programs

► Louisiana (H.B. 720 (2009))

- September 1 – October 31, 2009
- Applies to all DOR taxes and generally to taxes coming due between July 1, 2001 and Jan. 1, 2009
- Waiver of penalties and one-half interest due based on payment of tax and one-half interest by end of amnesty
- Must forego claim to refund or appeal
- Amounts in protest and litigation are eligible for amnesty, but taxpayer must abide by DOR's interpretation for tax years 2010-2012
- 20 percent post-amnesty collection fee for subsequent deficiencies in periods for which amnesty was claimed; not applied in case of federal adjustment

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Revenue Raisers - Amnesty Programs

► Maine – 2009 Tax Receivables Reduction Initiative (Public Law, Ch. 213, 2009)

- September 1 - November 30, 2009
- Applies to tax liabilities assessed as of Sept. 1, 2009
- Waiver of 90 percent of penalties otherwise due
- Must pay tax, interest and penalty due by end of initiative period
- Must forego any right to refund or appeal

► Maryland

- September 1 – October 30, 2009
- Waiver of penalty and one half interest
- Limited to taxpayers with fewer than 500 employees
- Does not apply to periods eligible for prior amnesty or amounts eligible for IHC settlement program

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Revenue Raisers - Amnesty Programs

► Virginia (Ch. 611, 2009)

- To run for 60-75 days between July 1, 2009 - June 30, 2010
- All penalties and one-half interest waived for eligible taxpayers
- 20 percent post-amnesty penalty

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Revenue Raisers - Amnesty Programs

► Proposals under consideration in New York and Pennsylvania

► Recently completed programs

- Alabama
- Arizona
- Connecticut
- Hawaii
- New Jersey
- Vermont

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Nexus

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Attributional Nexus – Amazon (NY)

- ▶ Amazon.com challenged New York law (second suit by Overstock.com)
- ▶ Under statute, nexus exists because of contracts with N.Y. residents who link to Amazon.com from their Web sites
 - Presumption of nexus can be rebutted by demonstrating that no New York residents actively solicit sales on behalf of Amazon
- ▶ Trial court rejected Amazon's facial and as applied constitutional challenges to the revised vendor statute
 - "Amazon should not be permitted to escape tax collection indirectly, through use of an incentivized New York sales ..., when it would not be able to achieve tax avoidance directly through use of New York employees engaged in the very same activities." [N.Y. Superior Court 1/12/09]

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Attributional Nexus – Amazon

- ▶ Following lead of New York (2008) to assert nexus over remote seller that uses in-state affiliates to 'solicit' sales, directly or indirectly, via Web site or otherwise for remote seller
 - Rebuttable presumption – Can 'prove' affiliate is not actively soliciting
 - Presumed nexus if over \$10,000 in sales via this arrangement in previous 4 calendar quarters
- ▶ Rhode Island
 - \$5,000 threshold
- ▶ North Carolina
 - \$10,000 threshold
- ▶ Vetoed in California and Hawaii
- ▶ Proposed in Connecticut, Illinois, Maryland, Minnesota and Tennessee

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Attributional Nexus

- ▶ *AT&T Communications of Maryland, Inc. v. Comptroller* (Md. Ct. of Special App. 6/12/08)
 - Court held AT&T was not a vendor required to collect sales and use tax on sales of 900 number calls where the content was provided by a third-party
 - Maryland law provides that certain "vendors" providing service on behalf of third-parties are required to collect tax from a purchaser of taxable services
 - However, the court held that AT&T was a "common carrier" that could not be deemed to be an agent of an out-of-state seller for the purpose of creating nexus
 - The court noted that common carriers are generally obliged to serve all who are willing to pay for a service. Because AT&T offered its "900" number services to anyone willing to pay, the court considered it a common carrier
 - Furthermore, in providing its services AT&T did not exceed its role as a common carrier

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Attributional Nexus

- ▶ *Scholastic Book Clubs, Inc. v. Commissioner of Revenue Services* (Conn. Super. 4/9/09)
 - Department asserted teachers actions (e.g., passing out and remitting order forms, earning bonus points when books were sold) created nexus for seller of books to students
 - Issue: Were teachers acting as "representatives" on behalf of the taxpayer in Connecticut
 - Court held that the teachers were not a "sales force"
 - The decision to participate in the program was at the teacher's discretion, the teachers often purchased books for themselves, and the bonus points remained with the classroom

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Duty to Collect

- ▶ *Town Fair Tire Centers Inc. v. Commissioner of Revenue* (Mass. Supreme Judicial Court, Aug. 25, 2009)
 - Taxpayer operating tires stores in both N.H. and Mass. was required to collect and remit use tax on tires sold to Mass. residents at its N.H. stores.
 - Appellate Tax Board ruled that the taxpayer could determine based on drivers' licenses and license plates that sales to Mass. residents were **intended to be used** in Mass.
 - Supreme Judicial Court overturned ATB finding that **actual use** in Mass. was required and Town Fair did not know that
 - Court did not address constitutional issues

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New Hampshire Response

- ▶ AN ACT prohibiting retailers from disclosing private customer information to foreign states in connection with the collection of certain sales and use taxes
- ▶ "No retailer shall provide to a foreign state any private customer information for use in the determination of sales or use tax liability of the customer in the foreign state or for use in the determination, collection, and remittance of sales or use tax by the retailer with respect to a New Hampshire retail purchase transaction, unless the foreign state has first provided to the retailer written confirmation that the foreign state provided prior written notice of its intent to collect a use tax on such retail transaction to the commissioner of revenue administration, and no later than 60 days following the commissioner's receipt of such notice by the foreign state, the department of justice has submitted to the commissioner its determination that the foreign state's sales and use tax statutes" meets 9 separately stated requirements.

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Affiliate Nexus -- Wisconsin

- ▶ **Effective July 1, 2009, legislation redefines retailer (with a requirement to collect tax) to include any person who:**
 - Has an affiliate in Wisconsin
 - Retailer is related to the affiliate
 - Affiliate uses facilities or employees in the state to advertise, promote or facilitate the establishment of a market for sales of items by the retailer in Wisconsin or for providing services to the retailer's customers in Wisconsin, including accepting returns or resolving customer complaints

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Affiliate Nexus – New York State

- ▶ **Effective June 1, 2009, the definition of "vendor" includes sellers who are affiliated with a New York business if one of two conditions is met:**
 - The New York business is a sales tax vendor that uses a trademark, service mark or trade name in New York that is the same as that used by the affiliated remote seller, or
 - There is more than fifty percent direct or indirect common ownership between the in-state and out of state affiliates and the in-state affiliate performs certain activities in New York that benefit the remote affiliate in its development of a market for its goods and services

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Unrelated In-State Presence

- ▶ **Dell Catalog Sales LP v. New Mexico Taxation & Revenue Dep't., (N.M. Ct. App. 2008)**
 - Taxpayer's principal place of business was Texas. It did not own or lease property in New Mexico, had no retail stores in the state and no employees or agents in the state. All orders are placed by phone, mail, fax or internet. All shipments are made by common carrier.
 - Taxpayer offers a limited warranty, which is a return to factor.
 - Taxpayer also offers service contracts, which provide at-home repair services via an unrelated third-party service provider. Customers contact Taxpayer when a repair is needed.
 - New Mexico audited the taxpayer and assessed gross receipts tax.
 - Taxpayer protested assessment:
 - Administrative hearing held for the State.
 - Court held on behalf of State.
 - A Petition for writ of certiorari to the U.S. Supreme Court was filed on December 15, 2008.

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Hot Audit Issues

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Hot Audit Issues

Software & Related Services

▶ Canned v. Custom

- ▶ **Wisconsin Department of Revenue v. Menasha Corp. (Wis. 7/11/08)**
 - ▶ Two key issues
 - ▶ First, what level of deference should be given a Tax Appeals Commission ruling
 - ▶ Second, was the Commission correct in applying the Department's rule and concluding that the software at issue was custom software exempt from sale and use tax
 - ▶ Court held that controlling weight deference should be given to the Commission's interpretation of the rule
 - ▶ The Commission was not required to give deference to the Department's interpretation of its own rules
 - ▶ Furthermore, the Commission properly determined the software at issue was exempt custom software
 - ▶ Overturned by legislation

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Hot Audit Issues

▶ Services Necessary to Complete Sale

- Florida
- Texas
- Virginia
- ▶ **Fabrication Labor**
 - Minnesota
 - New Jersey
 - NJ Proposed Regulation

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Hot Audit Issues

► **Teksystems v. Farr (Tenn. Court of Appeals, May 11, 2009)**

- Court affirmed lower court decision holding that software fabricated and installed by contract employees of temporary IT staffing company is not a taxable sale of software.
- Tennessee has exemption that applies to “the fabrication of software by a person for such person’s own use or consumption”; software must be fabricated by the user and consumer to qualify.
- Despite contrary language in contract, court observed that the clients exercised extensive, if not complete, control over the contract employees and noted the contract employees were not hired to develop a predetermined “end product.”
- Court concluded that the contract employees were agents of the clients and, thus, their computer software related services were not subject to tax because the in-house exemption applied

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Hot Audit Issues

► **Employment Services**

- *Manpower Inc. v Wisconsin Department of Revenue*, Docket No. 05-S-046, Wisconsin Tax Appeals Commission, August 12, 2009
 - Temporary help services are not subject to tax despite the fact that the underlying service performed by the temporary worker may otherwise be subject to tax.
 - The Wisconsin Department of Revenue sought to impose tax on any temporary services that matched those services enumerated as taxable under Wisconsin code.
 - Temporary help services themselves are not specifically enumerated as taxable.
 - The Wisconsin Tax Appeals Commission held that temporary help services are not subject to tax.

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Streamlined Sales Tax Project (“SSTP”)

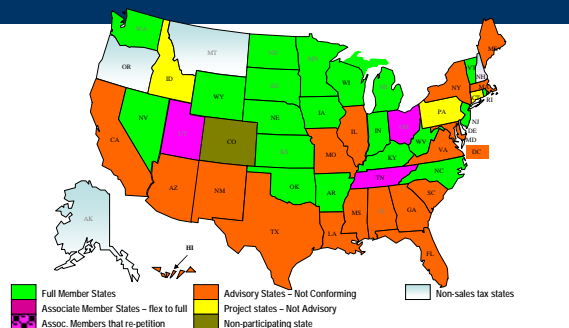
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What is the SSTP?

- **Project to modernize sales tax**
 - Project organized in March, 2000
- **Impacts all taxpayers and all commerce (bricks-and-mortar and remote sellers)**
 - Why the momentum?

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Streamlined State Status 10-01-09



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Streamlined Sales Tax

- **Twenty full-member states**
 - Wisconsin full-member state as of Oct. 1, 2009
- **Looking to expand**
 - Sourcing – Utah, Texas, Tennessee, Ohio, Missouri
 - Others – Massachusetts, Virginia, Florida
- **Current issues**
 - Exemption Certificate and Good Faith
 - Continuation of associate states and intra-state sourcing
 - Sourcing Services
- **What to watch**
 - New states (Texas?);
 - Problem states (Michigan?, Nevada?)
 - Movement on federal legislation

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Streamlined Statistics

- ▶ **Amnesty ended in all full member states except Washington and Wisconsin**
- ▶ **Statistics:**
 - Companies registered – 1,163 as of May 1, 2009
 - 133 are Model 1 and 29 are Model 2
 - Revenue - \$384.6M collected from 10-1-05 to 3-31-09
- ▶ **Amnesty still exists for Ohio, Tennessee and Utah**

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E-Commerce Study Updated

- ▶ **2009 study updating 2004 study:**
 - By 2012 \$11.4 billion in state and local revenue losses from B2B and B2C electronic remote commerce
 - By 2012 \$6.8 billion in state and local revenue losses from B2C non-electronic remote commerce

Source: "State and Local Government Sales Tax Revenue Losses from Electronic Commerce" by Donald Bruce, William F. Fox, LeAnn Luna dated April 13, 2009

- ▶ **2009 study by DOR economists underway on state and local revenue losses from B2B non-electronic remote commerce**

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Remote Sales Legislation

- ▶ **Require remote sellers to collect if:**
 - SST Agreement is operational
 - Member of the Agreement
 - If Agreement meets standards in legislation
 - If seller is above "Small Business Exception"
- ▶ **Federal Legislation**
 - Reintroduction expected 'soon'
 - Rep. Delahunt (D-Mass.) and Sen. Enzi (R-Wyo.)
- ▶ **Issues**
 - SST Board to set "Small Seller Exception"
 - Vendor Compensation
 - Telecommunications simplification
 - Court of Claims jurisdiction

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Outlook for Transaction Taxes

- ▶ **What's the impact of the crisis on sales and use taxes?**
- ▶ **What is the future of including services in the sales and use tax base?**
- ▶ **What's the best approach to dealing with the digital/online revolution?**
- ▶ **How do alternative entity-level tax bases coordinate with sales and use taxes?**
- ▶ **What happens if there is a Federal Value Added Tax?**

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Questions?

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Contact Information

- ▶ **Carolynn S. Iafate**
 - (610) 458-7227
 - csiafate@industrysalestax.com
- ▶ **Marilyn Wethekam**
 - (312) 606-3240
 - mwethekam@hmbllaw.com

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