Multistate Taxation

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Developments in Multistate Taxation

Illinois

The Illinois Department of Revenue issued a private letter ruling to a corporation providing that if it elects to treat the income from the sale of all the assets of one of its business segments as business income, the receipts from the sale will be excluded from the numerator and denominator of the company's Illinois sales factor.[1] The corporation sold one of its two business segments to an unrelated third party. The sale of the assets was the only such sale in the course of the corporation's business and constituted an incidental or occasional sale. The Department reasoned that, under Illinois law, the corporation could elect to treat its gain on the sale as business income, regardless of whether the gain otherwise met the definition of business income. The Department also reasoned that, pursuant to a regulation, where gross receipts arise from an incidental or occasional sale of assets used in the regular course of a trade or business, such gross receipts must be excluded from the sales factor.

Indiana

The Indiana Department of Revenue sustained the protest of a manufacturer that did business in Indiana and in other states and ruled that certain tooling equipment should be excluded from the manufacturer's Indiana property factor for apportionment purposes.[2] The manufacturer contracted with third-party suppliers to design and produce component parts. Before the suppliers began their production processes, the manufacturer inspected, accepted and paid the suppliers for the cost of the tooling equipment used to produce the component parts. The component parts were then delivered to the manufacturer, where they were

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assembled to make finished products for sale. The manufacturer asserted that the tooling equipment should not be included in its property factor because it received no income from the equipment. Rather, the equipment "was merely provided by" the manufacturer "to be used by" the suppliers "to insure [sic] the parts [were] manufactured to [the manufacturer's] specifications." It also asserted that it did not use the tooling equipment to generate income. Rather, its suppliers used the equipment to manufacture the parts and received income from the manufacturer. The Department determined that because the manufacturer did not use the tooling equipment, it was not required to be included in the manufacturer's property factor.

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The Indiana Department of Revenue ruled that the state's "throwback" provision applied to some, but not all, of an Indiana manufacturer's sales of items shipped to foreign countries.[3] The Department stated that an Indiana company's income derived from its sales to other states (or foreign jurisdictions) is thrown back to Indiana for income tax purposes when the Indiana company's business activities in those states (or foreign jurisdictions) are protected and are not taxable pursuant to P.L. 86-272. The Department found that "e-mail correspondence among [the manufacturer's] employees, travel arrangements, sales invoices, and employee trip summary reports" submitted by the manufacturer demonstrated that its activities in Russia, Spain and Mexico exceeded P.L. 86-272 protection and, thus, the Indiana "throwback rule" did not apply to the income derived from sales to these countries. However, the Department found that the manufacturer's documentation regarding other foreign countries showed that its employees' visits "were primarily to attend fairs and sales conferences/meetings to promote its products or to test (or replace/repair) its prototypes (or demo equipment)" and concluded that such activities "at best were solicitation of orders for sales" that fell within P.L. 86-272's protection; therefore, sales to foreign countries other than Russia, Spain and Mexico could be "thrown back" to Indiana.

Texas

The Texas Comptroller of Public Accounts affirmed sales and use tax assessments against a store owner in Texas after finding that the four-year statute of limitations for assessments did not apply because the owner's reports contained "gross error."[4] The Comptroller reasoned that an assessment may be made at any time if "information contained in the report of the tax contains gross error." "Gross error" means that, "after correction of the error, the amount of tax due and payable exceeds the amount initially reported by at least 25%." The Comptroller determined that the Comptroller Staff demonstrated by a preponderance of the evidence that the gross-error exception to the general four-year period of limitation applied and affirmed the assessments against the owner of the stores.

Virginia

The Virginia Tax Commissioner issued a ruling addressing the applicability of retail sales and use tax to a company's sales of prewritten software maintenance agreements and updates.[5] The Commissioner found that the company's software maintenance agreements did not specifically express the terms of delivery of software releases and updates and determined that because the agreements did not "specify and restrict delivery only to the electronic delivery of the software," the agreements did not constitute sufficient evidence for the company to claim that its prewritten software was provided by electronic means only and, thus, not subject to retail sales and use tax. The Commissioner stated that, for retail sales and use tax purposes, software maintenance agreements "should include specific language as to the type of transfers allowed and not allowed so that the intention of the parties is clearly made known. Documentation (invoices, internal documentation establishing electronic downloads, etc.) supporting the transaction needs to establish the exact method of delivery actually intended and used, and such method of delivery needs to be verifiable." The Commissioner further stated that in "determining the intent and, thus, the application of the tax to the transaction, the Department looks to the underlying documents that support the transaction. To establish the intent of electronic delivery, it is important to plainly state in written agreements that updates, upgrades and other maintenance enhancements to a prewritten program are only delivered electronically."

Endnotes

1 Private Letter Ruling, IT 13-0001-PLR, Ill. Dep't of Rev., Mar. 1, 2013.
2 Letter of Findings, 02-20120525, Ind. Dep't of Rev., Apr. 24, 2013.
3 Letter of Findings, 02-20120352, Ind. Dep't of Rev., Mar. 27, 2013.
4 Comptroller's Dec. No. 201303686H, Tex. Comptroller of Pub. Accounts, Mar. 4, 2013.
5 Rulings of the Comm'r, No. 13-51, Va. Dep't of Tax'n., Apr. 29, 2013.