

SALT Lunch and Learn: Hot Topics in State and Local Tax

DALLAS, TEXAS



Introductions

TODAY'S PRESENTERS



Section 1: Income And Franchise Tax

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Section 3: Indirect (Sales/Use) Tax

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Section 4: Sales and Use Tax Compliance Services

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Section 2: Texas Property Tax

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Section 1: Income & Franchise Tax

Topics of discussion

Overview

1. Facts and Figures
2. Margin Tax Legislative Update
3. Comptroller Priorities
4. Multi-state Developments
5. State impact on Federal tax law change

Facts & Figures

TAX REVENUE BY SOURCE

- ▶ Franchise tax: 10%
- ▶ Sales tax (includes motor vehicle sales tax): 70%
- ▶ Natural gas production tax: 2.2%
- ▶ Oil production and regulation taxes: 4.6%
- ▶ Alcoholic beverage taxes: 2.7%
- ▶ Cigarette and tobacco taxes: 3.1%
- ▶ Hotel occupancy tax: 1.1%



Facts & Figures

TAX REVENUE BY SOURCE

- ▶ Federal income: 37%
- ▶ Total tax collections: 43%
- ▶ Licenses, fees, permits, fines and penalties: 10%
- ▶ Interest and investment income: 1%



Franchise Tax

KEY LEGISLATIVE TOPICS – 2019 Legislature

Franchise tax bills – 43 bills introduced

Repeal of Franchise Tax

- » Big push in 2017 session
- » No traction in 2019

SB 66 Nelson This bill would require one half of any future biennial revenue growth above 5% be used to reduce the rates of the franchise tax. The bill would apply only to franchise tax reports due on or after January 1, 2022; consequently, the first report year for which rates may be reduced would be 2021, due in 2022.

Similar legislation (SB 17) was introduced in the 2017 regular session and was estimated to reduce taxes by a little more than \$500 million each year it would be in effect.

Last Action: Set for hearing in Finance on 4/15/19



Franchise Tax

2019 Legislation



HB 2611 Morrison Texas' franchise tax applies to corporations and other liability-protected entities including registered partnerships and limited liability companies; however, partnerships or trusts that are "passive entities" are exempt (a passive entity is one that does not actively manage a business and most of its income is dividends, interest, capital gains, royalties, etc., as opposed to sales). This bill would extend the definition of "passive entity" to include limited liability companies that meet the passive income test. The bill would take effect January 1, 2020 and would apply to reports due after that date.

Last Action: *Passed House, sent to Senate Finance*

HB 3823 Sherman This bill would exempt a corporation from the franchise tax if they adopt a family care leave policy that entitles their employees to a minimum of four weeks of paid leave after giving birth to a child, two weeks of paid leave following the birth of the employee's child and two weeks of paid leave following the adoption of a child or placement of a foster child with the employee. The bill would take effect January 1, 2020.

Last Action: *Voted favorably from Ways and Means 4/23/19*

Franchise Tax

2019 Legislation



HB 4198 Murphy This bill would allow a performing rights society that licenses the public performance of nondramatic musical works on behalf of a copyright owner to exclude from its total revenue payments made to the rights holder and copyright owner. The bill would take effect January 1, 2020.

Last Action: *Reported favorably from Ways and Means 4/16/19*

Companion: *SB 1824 Perry - Last Action: Placed on Senate Calendar 4/23/19*

HB 1089 Darby This bill would amend the definition of a retailer to include a taxpayer providing industrial uniforms, garments, and linen supplies for rental. This would allow these taxpayers to qualify for the 0.375% franchise tax rate, rather than the 0.75% tax rate they currently pay. The bill would take effect January 1, 2021 and apply to all reports due after that date.

Last Action: *Passed the House and now before Senate Finance Committee*

Franchise Tax

2019 Legislation



HB 3443 Springer This bill would equalize the interest rates applicable to tax delinquencies and tax refunds. Currently, tax delinquencies bear interest at prime plus one percent – 6.5% for 2019. In contrast, the interest applied to tax refunds is the lesser of prime plus one or the Treasury Pool rate – 2.42% for 2019.

The bill sets the Interest applicable to both delinquencies and refunds at prime plus one percent.

Effective 9/1/19.

The bill's fiscal note estimates a cost to the state from higher refund payments are \$3.6 million for the 20-21 biennium and growing to \$59.4 million for the following 22-23 biennium.

Last Action: *Voted favorably from Ways and Means 4/23/19*

Companion: *SB 2360 by Buckingham - Last Action: Left pending in Finance 4/24/19*

Research and Development Tax Credit

HB 800 by Murphy in 2013 provided taxpayers with a choice of a sales tax exemption on equipment used in R&D or a traditional IRC-style franchise tax credit

- » Substantial sales tax refund claims by oil and gas and construction for activities the agency does not view as R&D
- » Franchise tax credits claimed (and processed) have far exceeded initial estimates
- » Set to expire in December 31, 2026
- » 20 year credit carryforward
- » Will the legislature renew it?

HB 3598 by Martinez Fischer

This is a Comptroller bill to increase enforcement authority for recovering unclaimed property. Currently, statutorily authorized enforcement power is limited to a books and records examination and court action is required to compel audit compliance. The intent of this bill, in essence, is to provide the same enforcement authority for unclaimed property as is applicable to state tax collection. Major components of the bill include: Mandatory combined filing of unclaimed property reports by members of an affiliated group, A 10-year record-keeping and a 7-year audit period, A presumption of intent to avoid compliance if the amount initially reported is more than 25% less than that finally determined, and Empowers the Comptroller to take testimony, administer oaths and issue subpoenas to compel the production of records or to appear and give testimony under oath; these powers may be delegated only to an attorney employed by the Comptroller. The 7-year limitation period applies to examinations commenced after the bill's effective date, which is immediate if passed by 2/3 and 9/1/19 otherwise.

Last Action: *Passed House 5/3/19*

► Move Texas from **performance** state to **benefit** state for sourcing service revenues

» Examples

- › Web hosting services
- › SaaS services (letter ruling)
- › Sirius XM
 - Taxpayer apportioned its subscription receipts based on the locations where its primary production facilities were located, which were outside of Texas. Taxpayer did not operate any permanent studios in Texas
 - The Comptroller argued Taxpayer's subscription receipts should be apportioned to Texas based on the locations where the satellite transmissions were received by subscribers
 - The District Court held in favor of the Taxpayer
 - The Comptroller has appealed the decision

► Update Texas **margin tax** rules

- » Better interpretation of existing laws

Did you know ?

Nexus is a legal term that refers to the requirement for whether companies doing business are subject to tax in that state

- ▶ Will states follow economic threshold (factor presence) for income/franchise/gross receipts tax nexus as they have done with sales and use tax nexus under Wayfair
- ▶ States impose nexus based on economic/factor presence nexus
 - ▶ California, Tennessee, New York (only for corporations), Ohio, Alabama, Michigan, Connecticut, Washington, Colorado

Multi-state Developments



AR

Effective for tax years beginning on or after 1/1/2018, partnerships having income from both within and outside AR must apportion (prior law required allocation)

CT

Entity level tax for Pass-through entities
Starting in 2018

WI

Entity level tax for S-corporations
Starting in 2018

Annual election made by more than 50% (shares) of the shareholders to pay tax at entity level

Entity level tax for partnerships
Starting in 2019

Annual election made by more than 50% (capital and profits interest) of the partners to pay tax at entity level

OK

Oklahoma enacts pass-through entity tax for tax years beginning January 1, 2019.

Sourcing rule changes for Services

Effective for tax years beginning on or after 1/1/2018 - KY, MT, and OR sourcing revenue from services based on market benefit

- ▶ A number of states tax implications arise simply as a result of how/whether states conform to the federal IRC provision as modified by Congress
- ▶ Type of conformity
 - » Rolling conformity – states automatically conforms to the IRS as amended at any point in time
 - » Annual conformity – conformity date fixed until state legislature adopts a new date but state typically does so on an annual basis
 - » Fixed-date conformity – state conforms to the IRC as of a “fixed date,” until state legislature adopts a new “fixed date”
 - » Other
 - › Selectivity conforms to certain federal provisions but not others
 - › Conforms but decouples from certain provisions

- ▶ Federal law is new and there are many unclear and complex issues
- ▶ Understand how states will conform to new IRC laws
- ▶ How will states legislators react
 - » See significant state legislation
- ▶ Be pro-active as to the state impact



Section 2: Texas Property Tax

Primary Provisions

TEXAS PROPERTY TAX CODE (TPTC) BASICS

► Taxability

- » **Chapter 11:** All real and tangible personal property that this state has jurisdiction to tax is taxable unless exempt by law

► Market value

- » **Chapter 23:** All property is required to be assessed at Market value

► Renditions

- » **Chapter 22:** Required for all tangible personal property used for the production of income



Primary Provisions

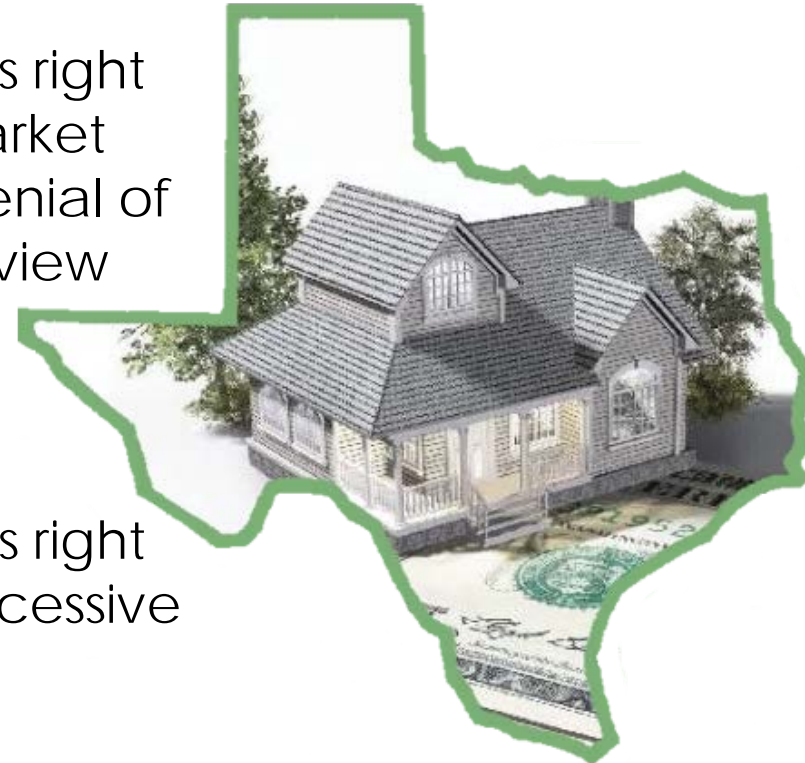
TEXAS PROPERTY TAX CODE (TPTC) BASICS

► Appeals

- » **Chapter 41:** Property owner has right to appeal determination of market value, unequal appraisal, or denial of exemption to the Appraisal Review Board

► Corrections

- » **Chapter 25:** Property owner has right to file correction petition for excessive appraisal or clerical error



Business Personal Property

UNDERSTANDING THE BASICS

► Renditions

- » **Required** per TPTC
- » Generally **report cost**
- » May report **opinion of value only**
- » CAD may issue “**21 day letter**” requesting basis for value
- » Due **April 1st** w/o extension; **May 1st** w/extension

► Primary Exemptions

- » **Freeport** inventory
- » Goods **in transit**
- » **Interstate/foreign** commerce
- » **TCEQ** pollution control equipment



Business Personal Property

FREEPORT INVENTORY EXEMPTION

- ▶ Applies to inventory:
 - » **Acquired or imported** into Texas to be forwarded out of state
 - » **Detained** in Texas for assembling, storing, manufacturing, processing, or fabricating by the person who acquired or imported it
- ▶ Must be transported out of state **within 175 days** after the date the person acquired or imported into Texas



REMEMBER

Petroleum products DO NOT qualify for Freeport Tax Exemption.

Business Personal Property

GOODS IN TRANSIT EXEMPTION

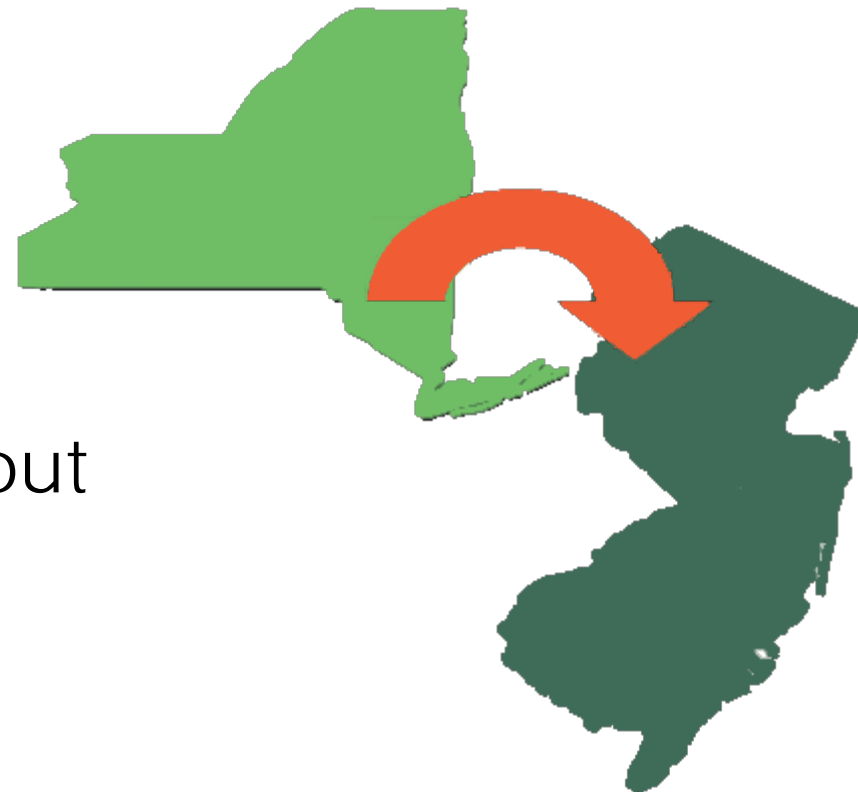
- ▶ Applies to product stored in **third-party warehouse**
- ▶ **Cannot** be owned or controlled by person owning inventory
- ▶ Must meet the **175 day** turnover requirement
- ▶ Not required to be **shipped out** of Texas



Business Personal Property

INTERSTATE/FOREIGN COMMERCE EXEMPTION

- ▶ Statutory exemptions per **Interstate Commerce Clause** and **TPTC 1.12**
- ▶ **Cannot** be processed, sliced or diced
- ▶ Must demonstrate **continual movement** out of state



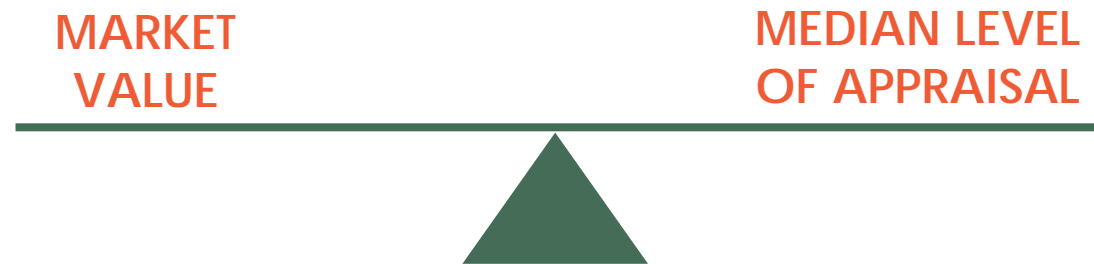
Business Personal Property

TCEQ POLLUTION CONTROL EXEMPTION



- ▶ Applies to **qualified** pollution control **equipment**
 - » Includes structures and site improvements
- ▶ Tier I, II or III
- ▶ Must secure approval from TCEQ and **Appraisal District**

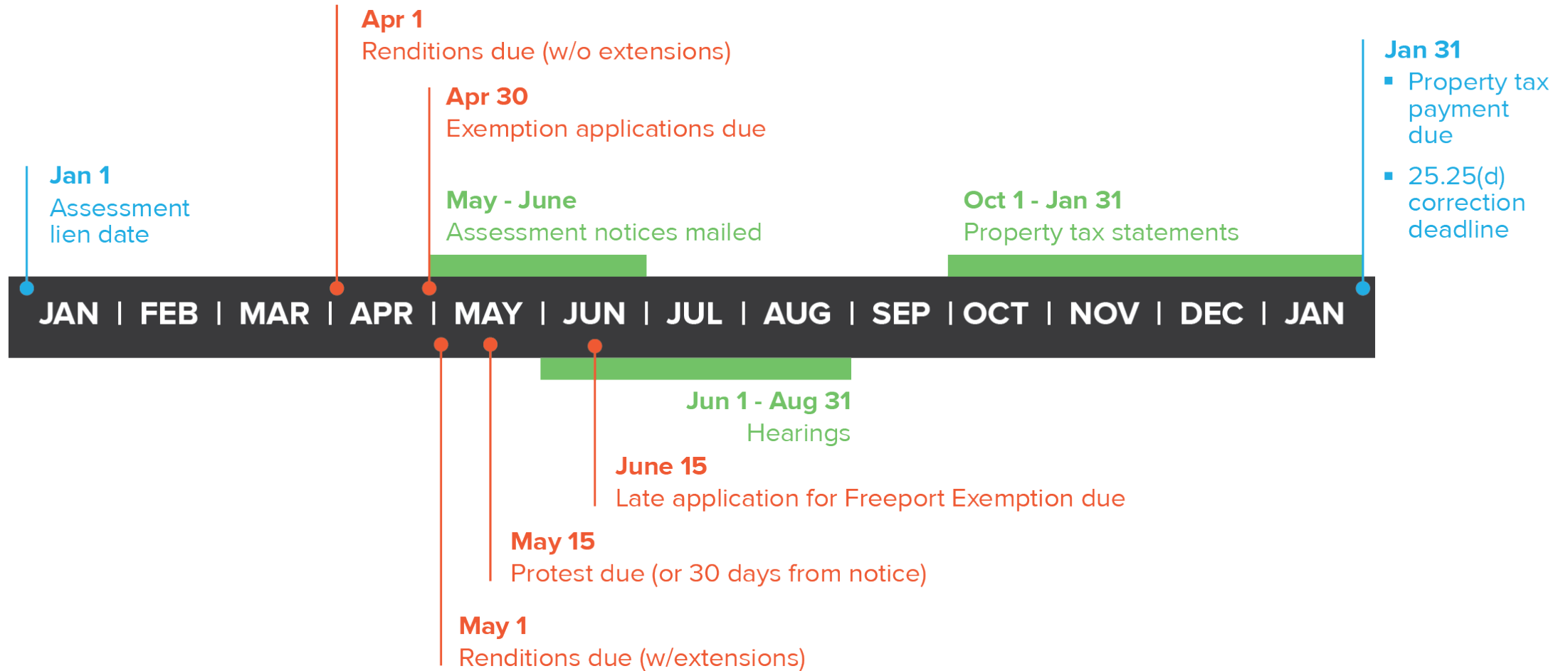
- ▶ Assessed at the **lower** of **market value** or the **median level** of appraisal



- ▶ Three **approaches** for determining value: cost, market/sales approach or income
- ▶ Basis for **appeal**: uniformity

Property Tax Timeline

IMPORTANT DATES TO REMEMBER



Property Tax Timeline

IMPORTANT DATES TO REMEMBER

Oct 1 – Jan 31

Property tax statements

OCT

NOV

DEC

JAN

Jan 31

- Property tax payment due
- 25.25(d) correction deadline



REMEMBER

*Petitions must
be filed with the
District Court
within 60 days
of ARB order.*



Section 3: Indirect (Sales/Use) Tax

Topics of Discussion

Overview

- ▶ Texas Legislative Update
- ▶ Compliance Nuances
- ▶ Planning Opportunities
 - » Exemptions/Exclusions
 - » Direct Payment Permits
- ▶ Wayfair / Economic Nexus Impact

Audience Survey

Sales and Use Taxes



What are your Sales Tax Painpoints?

- » Overpayments or Underpayments
- » Taxability Determinations
- » Did you know Sales Tax is a major expense to your operations?



Have you worked with a service provider to recover overpaid sales taxes?



Implemented a compliance process to eliminate overpayments and underpayments?



HB 1525 (Burrows) – “Marketplace”

» Relates to expanding the use tax collection responsibilities of non-resident sellers in response to the U.S. Supreme Court ‘s Wayfair decision.

- *Defines Marketplace, Marketplace Provider*
- *Requires Marketplace Sellers to furnish all info required for tax collection and provides that any tax deficiency is the responsibility of marketplace seller if the marketplace provider in good faith relied on the seller’s incorrect information*
- *Specifies that sales are considered consummated at the location to which a taxable item is shipped or delivered or where the customer takes possession*
- *Prohibit class action lawsuits against marketplace providers*
- *Bill would become effective September 1, 2019 if signed by Governor*





HB 2153 (Burrows)

Relates to a single local use tax rate as an alternative to combined local use tax rates for computing the amount of local use taxes remote sellers are required to collect and to the allocation of tax revenue collected at that rate.

- *Intended to reduce the compliance burden on remote sellers*
- *Purchasers at locations where the total local rate is less than the single rate may apply for a refund of overpaid tax.*
- *Tax receipts resulting from the use of a single combined rate are to be distributed to local taxing entities based on their percentage share of total state and local tax collections.*
- *Sent to the Governor on May 6, 2019*



Compliance Nuances

VENDOR TAX REIMBURSEMENT REQUESTS

► Why does this happen?

- » Vendor internal audit determined tax should have been collected
- » State Audit determined tax due and State allows vendor to seek reimbursement from its customer (TX, OK, Not NM)

► Should you pay?

- » Was the assessed tax due incorrectly determined by State?
- » Check to see if within Statute of Limitations Period
- » Consider the business relationship

Compliance Nuances

CUSTOMER REFUND REQUESTS



How do you handle a customer's request for a refund of taxes paid-in-error before you get the refund back from the state?

- » Look at open AR to offset
- » Can you provide a future credit for services?
- » Assign the Right to Refund to the Customer



What about gray issues or if a customer doesn't want to pay?

► Refund Assignment Forms

- » Increase in requests / Aggressive positions
- » Does customer/consultant have correct facts?
- » Review errors to minimize future similar errors



Compliance Nuances

Recent Trends with Auditors

- ▶ Auditors have increased workload
- ▶ New auditors with little/no industry experience
- ▶ Decision making ability at the auditor level has decreased
- ▶ Increased scrutiny of data and documentation provided
- ▶ Taxability determinations agreed upon during auditor meetings not reflected on auditor exam results.

Overpayments occur because...

- ▶ Failure to understand the taxability of the transaction.
- ▶ Purchaser did not issue the required exemption certificate.
- ▶ Invoice was not reviewed.
- ▶ Vendors typically charge tax unless requested otherwise.

► Exemptions

- » What is an exemption? Why do they exist?
- » Are you taking advantage of all qualified exemptions?
- » Created by State Legislatures to Entice Business Activities

► Exclusions

- » What is an exclusion?

► Difference between Exemptions & Exclusions

- ▶ Important Sales Tax Exemption/Exclusion Types
 - » Sale/Purchase for Resale
 - » Manufacturing
 - » New Construction
 - » Research & Development
 - » Non-taxable Services
 - » Environmental/Pollution Control
 - » Items subject to other sections of Tax Code
 - » Items shipped out of state

Planning Opportunities

Direct Payment Permits



► Qualifications

- » Currently over 855 Taxpayers with DPPs
- » Couple of those are represented in this room

► Making Use Tax Determinations

- » Who will be responsible? In-house or Outsource

► Benefits

- » Remove Tax Decisions from Suppliers
- » Local Tax Rate Savings

How Weaver can Help?

Direct Payment Permits



- ▶ Permit Application Assistance
- ▶ Planning Local Rate Saving Opportunity to Ensure Proper Application for Guaranteed Maximum Benefit
- ▶ Monthly review of direct payment permit purchases for taxability determinations, use tax accrual calculation, and sales/use tax return preparation and filing
- ▶ Taxability Determination Matrix for In-house Tax Decision-Making
- ▶ Audit Management

How Weaver can Help?

Overpayment Recovery Services



2 Phased Approach

➤ Phase 1 – *Assessment, Discovery, & Planning*

- ▶ Experienced SMEs (>\$150M in Savings Achieved)
- ▶ Sampling
- ▶ Issue-based focus
- ▶ Chronic Problem Vendor Identification
- ▶ Leverage Technology & Analytics
- ▶ Review Findings, Methodology, Recovery Options and Recommendations
Deliverable

➤ Phase 2 – *Tax Recovery & Achieving Compliance*

- ▶ Detailed transaction by transaction review & claim preparation, submission, auditor review, negotiation, settlement, refund receipt, in-house training



How Weaver can Help?

Overpayment Recovery Services



- ▶ In-depth experience in the energy industry.
- ▶ Minimal personnel time investment.
- ▶ Fees are a contingent percentage of total savings.
- ▶ We focus on the right purchases to maximize the benefit.
- ▶ Tax overpayments are corrected on recurring purchases.



Wayfair & Economic Nexus

South Dakota v. Wayfair

ECONOMIC NEXUS STANDARD

S.B. 106 Outcomes for Remote Sellers



Gross revenue from sale of tangible property, any products transferred electronically, or services delivered into South Dakota **exceeds \$100,000**



200 or more separate transactions of tangible property, any products transferred electronically or services delivered

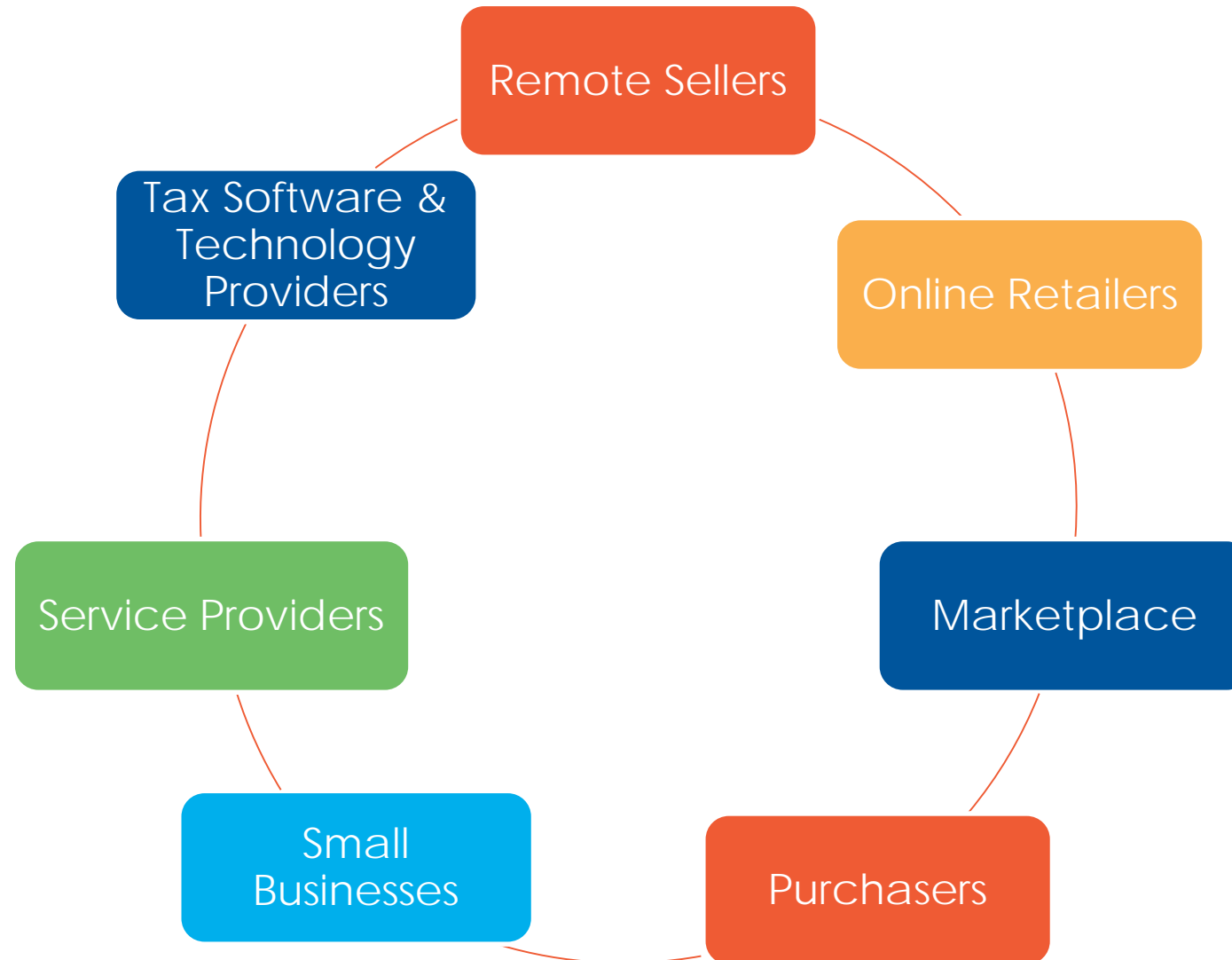
What Will The States Do Now?



- ▶ What are the considerations for local sales tax?
- ▶ Is there a small business exception?
 - » What's an "undue burden" now?
- ▶ What are the implications for other taxes?
- ▶ Will Congress act?

Impact on Businesses

WHO DOES THIS AFFECT?



Impact on Businesses

WHY DOES THIS MATTER?

Compliance
Costs (in-house
or outsource)

Registrations

Collection &
Filing
Requirements

Tax Audits

Tax Reserves

Certificate
Management

Technology
Improvements

Impact on Businesses

QUESTIONS TO ASK

- ▶ Which jurisdictions should register/collect sales tax?
- ▶ What the sales threshold is for each jurisdiction?
- ▶ When does tax collection start?
- ▶ What tax rate should be charged?
- ▶ Can our company handle the new compliance burden?
- ▶ Should our company pay tax when purchasing items in new jurisdictions or is an exemption available?

Section 4: Sales and Use Tax Compliance Services

- ▶ Compliance Outsourcing
 - » Return Prep & Filing Services
 - › Tax Data Processing
 - › Secure Payment Processing
 - › Monthly Reconciliations
 - › Notice Management
 - › Dedicated Team Member
 - › New Jurisdiction Registrations
 - › Activity Trends Report
 - › Dedicated Client Web Portal





Compliance Outsourcing

► Client Benefits

- » Leverage tax expertise
- » Free up internal resources to focus on more strategic activities
- » Eliminate need to add headcount
- » Avoid purchasing and supporting expensive tax filing software
- » Reduce overall cost of compliance
- » More accurate and consistent filings
- » Control audit exposure

Questions?

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