

# **GBQuarterly: State & Local Tax** 2020 Developments

September 24, 2020

### Note

- 1. This presentation is intended to make participants aware of tax issues that may apply to this audience.
- 2. Information presented herein is not intended to be tax advice.
- 3. Please consult with a qualified practitioner for tax advice related to specific transactions.



### **Speakers**







Sara Goldhardt, CPA
Director,
State & Local Tax Services
614.947.5243
sgoldhardt@gbq.com



Matt Stamp, JD, LLM
Director of State & Local
Tax Services
614.947.5302
mstamp@gbq.com



### Agenda

- Ohio audit hot topics, identification of potential overpayments and enforcement
- Wayfair Nexus Requirements
- Telecommuting employment and income tax updates
- Real and personal property
   valuations and tax assessments
- Application of recent Ohio legal decisions and other Ohio developments





Ohio Audit Hot Topics, Refunds and Enforcement

### Ohio Audit Hot Topics, Refunds and Enforcement

#### **Ohio Audits**

- COVID-19 shut down or temporarily paused many audits altogether
- Shutdown created a backlog at review level
  - Delay in receiving assessments
  - Interest continues to toll
- Many decisions at audit level are being made by administration
- Penalty waiver requests are being considered on a case-by-case basis.
   Considerations include:
  - Past compliance history
  - Taxpayer cooperation during audit
  - Auditor/Manager input
- Targeted industries for enforcement
  - Construction
  - Manufacturing



### Ohio Audit Hot Topics, Refunds and Enforcement

#### **Ohio Refunds**

- Waiting period for refund to be reviewed is approximately six months.
- Once assigned to review, ODT is expediting as quickly as possible
- Providing voluminous documentation to satisfy refund request still remains an issue
  - Invoices
  - Proofs of payment
  - Contracts
- Common Refund Exemptions
  - Manufacturing
  - Packaging
  - Software Multiple Points of Use
  - Temporary Employment (if certain conditions are met)





#### Sales Tax - Current Status

- Majority (43 states plus DC and AK localities) enforcing some form of economic nexus on sales tax
- Many states have implemented economic nexus post Wayfair decision
- Others relying on previously existing statutes
- Trends
  - Retroactivity Trend is toward prospective enforcement
  - Movement away from transactional thresholds
  - Use tax notification requirements
  - Movement away from physical presence Does economic nexus truly replace the physical presence test?
- Adjustment of nexus thresholds since initial legislation



#### Sales Tax - Other Considerations

- Local Enforcement
  - State administered localities vs. true home rule (self-administered)
  - Rules may differ between state vs. local jurisdictions
  - Does the state threshold apply to individual localities?
- Marketplace Facilitators
- Registration Requirements
  - Other Tax Types (Withholding, Income/Franchise, Gross Receipts, etc.)
  - "Business Start Date"
- Risk of non-compliance



#### **Income Tax Nexus**

- Whether physical presence is necessary to create income tax nexus has been a topic of debate for many years.
- In 1993, in Geoffrey, Inc. v. South Carolina Tax Commission, the South Carolina Supreme Court held that physical presence was not required for the imposition of income tax.
- The court concluded that the presence in South Carolina of Geoffrey's intangibles was enough to establish substantial nexus for corporation income tax.
- Quill is a sales and use tax case only!
- Given the uncertainty of the concept of economic nexus, we began to see the adoption of factor-presence, or bright-line, nexus standards.



#### **Factor-Presence Nexus**

- For corporate income tax and gross receipts tax purposes, some states have already enacted factor-presence nexus standards.
- Out-of-state corporations are deemed to have nexus for corporate income tax or gross receipts tax purposes where they have property, payroll, or sales in those states that exceed the statutory thresholds.
- States with a factor-presence nexus standard for income tax include Alabama,
   California, Connecticut, Colorado, Michigan, New York and Tennessee.
- States with a factor-presence nexus standard for gross receipts tax include Nevada, Ohio and Washington.
- In 2016, the Ohio Supreme Court ruled that the bright-line presence standard of the Ohio Commercial Activity Tax (CAT) satisfied the substantial nexus requirement under the Commerce Clause of the U.S. Constitution.



#### Public Law 86-272

- P.L. 86-272 is a federal law that prohibits states from imposing a net income tax upon an out-of-state company if the company's activities in a state are limited to the solicitation of orders for the sale of tangible personal property and the orders are approved and filled from outside the state.
- P.L. 86-272 does not protect a company from state franchise tax.
- Wayfair does not overrule P.L. 86-272.
- P.L. 86-272 will remain in force unless Congress decides to change it.
- The general consensus currently in the state tax community is that Congress will not eliminate P.L. 86-272.
- Federal Bill H.R. 3063 Business Activity Tax Simplification Act of 2019



#### What's next?

- Washington recently updated its economic nexus standard for B&O Tax.
   Effective 1/1/20, the threshold matches the \$100K (gross income) sales tax threshold.
- Hawaii was the first state to enact a sales or transaction nexus standard for an income tax based on the economic sales tax nexus thresholds at issue in Wayfair.
- Effective for tax years beginning after December 31, 2019, if a business engages in or solicits 200 or more business transactions with persons in Hawaii or the person's gross income attributable to Hawaiian sources is \$100,000 or more, it will be subject to Hawaii business taxes.
- Texas, Pennsylvania, Massachusetts and the City of Philadelphia have followed with economic nexus thresholds.



#### What's next?

- As a result of Wayfair, states will likely be more aggressive in trying to impose income tax nexus.
- More states may enact factor-presence nexus standards for corporation income tax purposes.
- Companies may need to evaluate their no nexus positions for income tax purposes.
- Companies should continue to assess if they can take a de minimis or economic presence only nexus position.
- Companies should also evaluate any potential financial statement implications.
- When registering for sales tax, it is good time to review income tax nexus positions.





### Mobile or Telecommuting Employees

- With the advancement of technology, the use of the Internet to reach more customers, and the increase of business travel, a greater number of companies have employees who:
  - Work remotely from home;
  - Travel to new states for short periods of time on a project-by-project basis.
- In 2020, we are seeing unprecedented telecommuting due to COVID-19.
   Telecommuting employees can create tax obligations or liabilities for businesses in a state where a business doesn't otherwise have nexus.
- Registering for one tax type will put a company on a state's radar for other taxes.



#### Income/Franchise Tax and Sales/Use Tax Nexus

- What types of business activities does the employee perform? With whom does the employee interact?
- In the Bloomberg BNA 2019 Survey of State Tax Departments, 39 states and the District of Columbia say income tax nexus would result for an outof-state corporation with employees who telecommute from homes within their jurisdiction.
- 37 jurisdictions report income tax nexus would arise from a single telecommuter who performed back-office administrative business functions.
- Is the employee an in-state salesperson? The employee's activity may still be protected by P.L. 86-272.
- P.L. 86-272 does not protect a company from state franchise tax, gross receipts taxes or employment taxes.



### **Income Tax Withholding**

- States will generally tax an employee based on where the employee works.
- States will also tax an employee based on where an employee lives (e.g. Georgia).
- When a reciprocal agreement has been reached between two or more states, agreeing states are precluded from taxing the earned income of employees who are residents of reciprocal states.
- Some states allow for work site withholding exceptions based on number of days in state or dollars earned from a state.
- Examples:
  - Arizona & Hawaii: 60-day threshold
  - Wisconsin: In-state wages less than \$1,500
  - New Jersey: Not specifically based on days or dollar amount



### Impact of Telecommuting Due to COVID-19

- Some states have announced that a temporary presence of telecommuting employees due to COVID-19 will not create nexus.
- Other states have announced that they will either not change nexus standards for telecommuting or have not addresses it at all.
- Will the employee be telecommuting temporarily or permanently?
- Local rules may differ from state rules.
- Employers must understand income tax withholding for remote workers and the nexus implications of income tax withholding.
- Telecommuters may have an impact on state income tax apportionment and sales sourcing for apportionment purposes.
- Review state unemployment tax implications.



### Ohio Municipal Tax Withholding due to COVID-19

- Ohio House Bill 197 allowed employers to continue to withhold municipal income tax in the city of the employee's traditional workplace during the health emergency plus 30 days.
- Senate Bill 352 was recently introduced to repeal this piece of legislation.
- The Buckeye Institute filed a lawsuit against the City of Columbus and the State of Ohio.



### **Federal Legislation**

- Over the years, legislation has been introduced to both the House of Representatives and the Senate in order to simplify state income tax issues for mobile workforces.
- The Remote and Mobile Worker Relief Act of 2020 (S. 3995) was introduced on June 18<sup>th</sup>.
- Employees and employers would be relieved of nonresident income tax and withholding if employees are working in the nonresident state for less than 30 days in the calendar year.
- S. 3995 would, through December 31, 2020, increase the 30-day threshold to 90 days for employees temporarily working in a state due to COVID-19. S. 3995 also provides nexus relief for purposes of the imposition of state business taxes due solely to employees temporarily working in the state because of COVID-19.



#### Challenges of the Mobile Workforce

- As we've seen, all of the states and cities are different.
- Employers and employees have difficulty tracking and documenting travel.
- Employers find that allocating wages to multiple taxing jurisdictions is difficult...if not impossible.
- Lack of communication between internal departments can also make tracking employees difficult.



#### Challenges of the Mobile Workforce - continued

- How to tackle the challenges of the mobile workforce?
  - Identify ways to better track employee travel
  - Pinpoint improvements to internal communication in order to be proactive
  - Assess current workforce and quantify any risks / exposure across all tax types
  - Develop a mobile workforce policy
  - Develop or review a telecommuting policy
  - Consider how to communicate the policy to employees





#### Karvo Paving Co. v. Testa

- Construction contractor provided traffic maintenance equipment (concrete barriers, lights, signs and message boards) as part of a contract with ODOT.
- Because items were purchased as a requirement of ODOT, including approval of placement on jobsite, Karvo successfully claimed that equipment was exempt as a purchase for resale.
- Successfully utilized affiliated group exemption for temporary employment services despite Karvo not meeting 50% ownership test.
- Key Takeaways:
  - Limited application (Department of Taxation will only accept holding in the 9<sup>th</sup> District)
  - Could create sales tax liability for contractors in certain situations



#### Nationwide Mutual Insurance Company v. McClain

- Nationwide installed data cabling as part of a building-wide rehabilitation and paid sales tax on entire project.
- A refund claim was filed claiming that the installation constituted an exempt improvement to real estate.
- BTA reversed its decision in Newcome Corp. v. Tracey (Dec. 11, 1998), BTA No. 97-M-320 which held that data cabling was a taxable business fixture since it was not common to buildings (at that time)
- Key Takeaways:
  - Holding of case is narrow and only contemplates CAT5/CAT6 data cabling
  - Does not apply to business fixtures/specialty data cabling.



#### Other Notable Cases

- Great Lakes Bar Control, Inc., v. Testa, 156 Ohio St.3d 199, 2018-Ohio-5207
- Paccar Inc., v. McClain, BTA No. 2018-906
- Time Warner Cable, Inc. & Subsidiaries v. City of Cincinnati, Ohio Ct. App. (1st App. Dist.), Dkt. No. C-190375, 08/26/2020
- Nissan North America, Inc. v. McClain, BTA Case No. 2016-1076 (10/9/2019)



### Other Notable Ohio Developments

### **Ohio Commercial Activity Tax Updates**

- Per the Ohio Department of Taxation COVID-19 Tax Relief website:
  - The amount of a PPP loan and any amount of the loan that is forgiven under the CARES Act is excluded from a taxpayer's gross receipts for purposes of the Ohio CAT.
  - Economic injury disaster loan (EIDL) advance grants of up to \$10,000 authorized by the CARES Act are not excluded from CAT gross receipts under uncodified section 36 of Am. Sub. H.B. 481.
  - The employee retention tax credits authorized by the CARES Act are excluded from CAT gross receipts under R.C. 5751.01(F)(2)(m), which excludes tax refunds and other tax benefit recoveries.



### Other Notable Ohio Developments

#### Ohio Commercial Activity Tax Updates - cont'd

- Per the Ohio Department of Taxation COVID-19 Tax Relief website:
  - The CARES Act established the Coronavirus Relief Fund which some local governments have used to establish grant programs to support businesses. The receipt of such a grant by a business is not excluded from gross receipts for the CAT. If the local government extends a loan to a business using these funds (and the loan was not forgiven), the amount of the loan is excluded from gross receipts for the CAT under R.C. 5751.01(F)(2)(e).



### Other Notable Ohio Developments

#### Ohio Business Income Deduction

- The Ohio Department of Taxation continues to heavily review the Ohio Business Income Deduction and related business income tax rate.
- This issue is particularly important when selling a business.
- Taxpayers also need to be aware of ORC §5747.212 and the impact of *Corrigan v. Testa*, 149 Ohio St.3d 18, 2016-Ohio-2805.





Real and Personal Property Tax Valuation and Assessments

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### **Ohio Real Property Tax**

- 2020 Revaluation Cycle
  - Tentative values delayed due to COVID-19
  - Some counties are not offering informal appeal hearings
  - Increases have averaged between 15% 20% depending on county
- Increased Scrutiny
  - Entity swaps
  - Charitable Use Exemptions
- Appeal Process
  - Many counties still issuing no change or nominal reductions at Board of Revision
  - Board of Tax Appeals encouraging settlement where possible



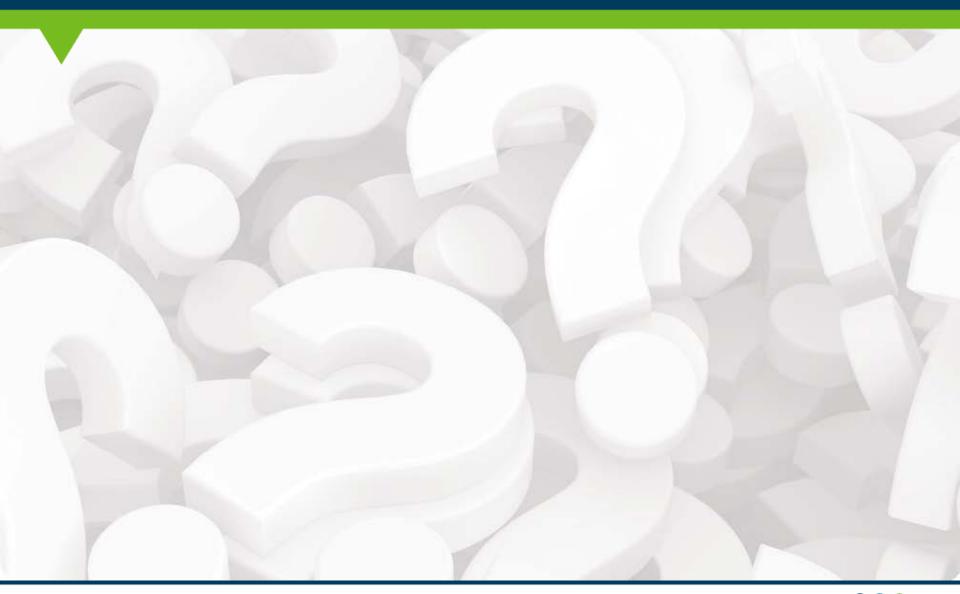
### Real and Personal Property Tax Valuation and Assessments

### **Personal Property Tax**

- Audit activity increasing
  - Most prevalent in southern states
  - Completed in conjunction with other indirect tax audits (sales/use)
  - Use of third party auditors
- Increased scrutiny on claimed exemptions
  - Freeport exemptions
  - Incentive reporting
- Billing errors/Incorrect assessments
- Leased Property
  - Lessors receiving notices/questionnaires from local jurisdictions
  - Escape assessments



### Questions



### **Contact Information**







Sara Goldhardt, CPA
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