

SALES AND USE TAX PUBLIC PARTICIPATION WORKING GROUP

Teleconference Minutes

of

Phase II Task Force Two

held **January 30, 1998**, 11:00 am to 12:30pm

I. Welcome and Introductions.

Identified teleconference participants:

Mark Wainwright (UT) Jeff Friedman

Facilitator

Gary Anderson (ND) Ray Jordan

René Y. Blocker (MTC) Diane Lubbering (MO)

Peter Bloom Paull Mines (MTC)

Karen Boucher Martha Mote (IL)

Merle Buff Art Rosen

Kaye Caldwell Marshall Stranburg (FL)

II. Public Comment Period.

Paull Mines reminded the group that participants had been asked to provide specific written proposals for the items sought to be included in the Phase II document. The MTC had received no proposals related to the subjects to be addressed by this Task Force. He indicated that more productive discussions may be held where specific proposals have been developed.

There was no other public comment.

III. Phase II Task Force Two evaluation/consideration of proposed topics.

- a. Establishment of a policy that affiliate nexus will not be asserted if the sole basis is common ownership/control; likewise establishment of a policy that a unitary relationship with another affiliate will not be asserted as grounds for sales/use tax nexus.

Paull Mines disclosed to the Task Force that the latest draft of the nexus guideline, the *State Participant Revised Public Participation Working Group Draft of the Constitutional Nexus Guideline for Application of a State's Sales and Use Tax to an Out-of-State Business (D*R*A*F*T—01/98)*, now contains examples that illustrate when the presence of an affiliate in the taxing State may give rise to nexus. See examples 2 and 3 to II.B.3.b. (affiliate in State selling same type of merchandise allows imposition of non-burdensome use tax collection duty for out-of-state seller), example 4 of II.C.2. (subsidiary's interest in real estate in taxing State attributed to out-of-

state seller), example 5 to II.C.5. (in-state affiliate supplying out-of-state seller's catalogs in its store or accepting return of merchandise of out-of-state seller is representative of out-of-state seller).

Business representatives urged respect for the sanctity of separate entity organization. One business representative urged review of *New York Law Firm Issues Comments on FTB Draft Reg*, 14 STATE TAX NOTES 383 (1998), to gain a proper appreciation of the limits that are placed on the States with respect to ignoring separately organized business entities for tax purposes. State representatives indicated that at this stage the States believed that the Phase I document should reflect a constitutional understanding of when "entity isolation" would not avoid sales tax or a use tax nexus.

Business inquired whether the States would be receptive to limiting affiliate nexus to circumstances where the affiliate was actually acting as a representative of the out-of-state seller. Business representatives stated that recognition of affiliate nexus borders on bad faith and is totally questionable.

None of the state representatives on the teleconference were prepared to state whether their States would recognize in the Phase II context a pull-back from the affiliate nexus principles now included in the most current Phase I guideline.

- b. Identify indirect property interests that are not deemed to create nexus (e.g., security interests, financing leases, etc.).

This issue was raised by the business representatives stating that they did not think any security interest could rise to the level of establishing nexus. Business was willing to note that once the inchoate rights of a security interest were transformed into a present interest in property, as might occur in a foreclosure, then the potential for nexus did arise. Business noted that there are some States that provide minimal present property interests arising from foreclosure does not establish nexus. One State representative inquired whether security agreement restrictions on movement of the property providing security changed these understandings. Business rejected the suggestion, indicating that whether a security interest in property should be treated as an interest in property should be analogized to the *Nebraska Dept. of Revenue v. Lowenstein*, 513 U.S. 123 (1994) (repurchase agreements different from federal obligations).

The following language was suggested by business for recognizing the rule sought—

Inchoate rights to property shall not be considered in making a determination of nexus.

State representatives indicated that they would consider this statement.

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