EVERSHEDS SUTHERLAND

Eversheds Sutherland (US) LLP
999 Peachtree St., N.E., Suite 2300
Atlanta, GA 30309-3996

D: +1 404.853.0100
F: +1 404.853.8806

January 19, 2023

Via E-Mail @ bhamer@mtc.gov
Brian Hamer
Counsel, Multistate Tax Commission
444 North Capitol Street NW, Suite 425
Washington, DC 20002

Re: Model Sourcing Regulations – Transportation Companies

Dear Brian:

Thank you for the opportunity to participate in the Multistate Tax Commission's Model Sourcing Regulations Work Group. During the Work Group's meeting on December 15, 2022, we expressed concern that some of the initial questions posed to participants about how states source revenue from transportation services could produce disparate results for states and similarly situated taxpayers, and in some cases may be inconsistent with federal law. We explained that there are many different types of companies and business models associated, directly or indirectly, with the transportation of people and property. Some of these companies may use different types of transportation services to move people and property. In response to these comments, the Work Group asked if we would provide a summary of some of the different business models we referenced and some additional detail regarding our concerns. This letter responds to that request.

In evaluating any changes to its model regulations, it is important to many in the business community that the Work Group consider the federal limitations on state taxation of people and property, the desire to treat similarly situated companies equally within the contours of these federal prohibitions, and the fair apportionment of revenue among the states. There are numerous federal, state, and local regulations that may apply to transportation companies based on the services offered, the company's registration status, the types of property and/or people transported, and/or the assets the company owns or leases to transport such property/people. We believe it is particularly important to fairly apportion receipts among the states to ensure that densely populated states are not assigned a disproportionate share of receipts relative to low population states. For example, a package may be picked-up and delivered in the same state but the majority of the transportation services necessary to deliver that package are provided in one or more additional states. Careful consideration of these issues will help to ensure that transportation services are not subject to claims that the proposed sourcing methodologies do not fairly reflect income in any particular taxing jurisdiction.

A. Delivery and Transportation Services

A company that provides "**package delivery**" or "**package transportation**" services may transport and deliver property through various modes of transportation. For example, there are several types of companies that transport property including trucking companies, railroads, air carriers, and carriers on foot. Companies may also use independent contractors and other vendors to provide all or part of the transportation service. Or companies, such as Internet-based platforms, may connect transportation providers to customers without touching the property. Moreover, it is common for package delivery companies to transport property using multiple modes of transportation, even in a single delivery transaction.

Companies that offer package transportation services may provide these services, depending on the service offered, by using their own employees, independent contractors, and assets to deliver its goods or by hiring outside service providers. Moreover, whether these employees and assets are in a different legal entity may effect whether such services are being provided by a package delivery company. For example, whether the trucking and air transportation services are in separate legal entities may impact how the company is classified under state and federal law.

Ground transportation

There are a number of different kinds of companies that transport property on the ground such as trucking companies, railroads, couriers, and gig drivers (i.e., drivers that are hired to make deliveries on a per-task basis, rather than working as an employee or independent contractor). And even companies that may appear to be the similarly situated, i.e., trucking companies, may use different modes of transportation or may operate differently.

A company that transports property on the ground may own or lease trucks, vans, or other commercial motor vehicles to transport property. Examples of modes of transportation applicable to these companies: long-haul trucking (cross country); intra-state/city driving, temperature-controlled/refrigerated trucking; and armed transportation. The company, its employees, independent contractors, and/or its assets may be regulated by federal agencies including the Department of Transportation (DOT), the Federal Motor Carrier Safety Administration (FMCSA), and/or state governments.

A railroad company or company that owns or leases railcars also transports property on the ground. Examples of modes of transportation applicable to these companies: small package and parcel transportation; rail freight transportation including special or hazardous cargo freight transportation; and reefer transport (i.e., refrigerated/temperature controlled boxcars). The company, its employees, independent contractors, and/or its assets (e.g., railcars) may be regulated by: federal agencies including the DOT and the Federal Railroad Administration (FRA).

Couriers also transport property on the ground, to varying degrees. For instance, some couriers will transport property from New York City to Mumbai, India in less than 24 hours. Other couriers provide intra-city package delivery services of prepared food, laundry, groceries, by hand carry (i.e., on foot), bicycle, wheeled hand-cart, or motorized vehicle (e.g., electric bicycle, car). Depending on a courier's services, the company, employees, and/or independent contractors may be subject to federal regulation by the DOT and state or local laws (e.g., local licensing requirements).

Air transportation

Companies that deliver property via air transportation may include an air carrier or company that owns or leases airplanes, or rents space on an airplane. Air transportation may include any of the following services: special cargo air transportation (e.g., dangerous goods, live animals, perishable cargo, wet cargo, time and temperature sensitive products); general cargo; regional air transportation; national/international air transportation; and same-day, next-flight-out, overnight, economy, charter, door-to-door, airport-to-airport, door-to-airport, airport-to-door, and hand carry transportation. There are a few federal agencies that may regulate a company providing air transportation, its employees (*e.g.*, pilots, airport ground-personnel), and/or its assets (e.g., airplanes) including the DOT and the Federal Aviation Administration (FAA).

Water transportation

A waterborne transportation company (e.g., merchant marine) or a company that owns or leases a cargo carrier, barge, or vessel transports property by water. Examples of modes of transportation applicable to these companies: maritime transport including short-sea shipping (i.e., coastal transport) and deep-sea shipping (i.e., long-trade navigation); inland waterway transport; and river transport. The company, its employees (*e.g.,* captains), and/or its assets (e.g., barge) may be regulated by: the DOT and the Maritime Administration.

Other direct or indirect forms of transportation

There are several different types of companies that may be directly or indirectly involved in the transportation of property such as freight-forwarders, brokers, and Internet platforms.

A freight-forwarder is a company that takes possession of the property to be transported, arranges for and coordinates the transportation of such property, and may also provide packaging, storage, refrigeration, insurance, and customs services on behalf of retail customers or other transportation companies. Examples of freight-forwarder services are: arranging for transportation between the carrier and the shipper including ground (i.e., less-than-truckload and full-truck-load), rail, ocean, air, or intermodal transportation; and tracking transportation (preparing shipping and export documents, warehousing, negotiating freight charges, arranging cargo insurance, freight consolidation, filing insurance claims).

A transportation broker is company that coordinates the transportation of property but does not take possession of such property. Examples of broker transportation services include: facilitating communication between carrier and shipper for transportation services including ground (i.e., less-than-truckload and full-truck-load), rail, ocean, air, or intermodal transportation; and tracking transportation, preparing shipping and export documents, negotiating freight charges, arranging cargo insurance, freight consolidation, and filing insurance claims. Freight-forwarders and transportation brokers may be regulated by the DOT and FMCSA.

A company that owns an Internet-based platform may also be indirectly involved in the transportation of property because it connects sellers, buyers, and transportation providers. Examples of Internet-based transportation platform services: pick-up/delivery of prepared food; intra-city deliveries; and inter-state deliveries.

B. <u>Package</u>

A "**package**" could include any "thing" being transported such as tangible personal property, commodities, freight, food, livestock, and people. The type of property or persons being transported affects the services provided as well as the regulation. For example, art is often transported by freight-forwarders who specialize in transporting art. These freight-forwarders provide additional services such as packaging, storage, arranging insurance, import/export services, and installation at the customer's premises.

The federal government regulates most interstate carriers, which may affect the goods transported. For example:

1. FMCSA and the Pipeline and Hazardous Materials Safety Administration (PHMSA) oversee the transportation and delivery of hazardous materials, which includes lithium cells and batteries. The service used to transport lithium cells and batteries impacts how the transportation of such goods are regulated; and

2. Truckers transporting more than 2,000 pounds of fresh or frozen fruits or vegetables in a given day must obtain a PACA (Perishable Agricultural Commodities Act) license. *See* 7 U.S.C. §§ 499a-499t. PACA authorizes receivers to reject a shipment of produce within a certain period of time after delivery.

Furthermore, "package" is defined differently by different service providers. It may include envelops and packages weighing over 150 lbs.

C. Examples of Intermodal Package Delivery and Transportation

The mode of transportation and the route over which the package is transported changes regularly. In general, companies use the most efficient mode depending on the type of property and delivery service purchased. Factors that may affect the transportation modes include: origination/destination, size/weight of the property, delivery service, weather, or available means of transportation. For example, a package traveling from Boston, Massachusetts, to Charlotte, North Carolina, may usually travel by truck. However, if there is a blizzard in Maryland, the package may be transported in part by an air carrier.

Below is one example and four scenarios that illustrate the complexity of package transportation.

Example: A company (seller) located in Philadelphia, Pennsylvania needs to ship a sweater to a customer in San Diego, California. The seller packages the sweater and purchases transportation services from "carrier". Carrier owns commercial motor vehicles and airplanes used to transport packages. Carrier picks up the package at the seller's location in Philadelphia.

Scenario 1: the seller purchases overnight shipping from carrier.

> Day 1: Carrier drives the package to the airport in Philadelphia. At the airport, carrier unloads the truck into a ground vehicle, drives the package to the carrier's airplane, and loads the package onto the airplane around.
>
> > *Ground transportation*: ~ 15 miles in Pennsylvania
>
> Day 2: The airplane flies from Philadelphia to San Francisco. Carrier unloads the airplane, sorts, and loads the package onto an airport transfer ground vehicle. The package is loaded onto a truck driving to San Diego. The trucker drives the package to San Diego and delivers the package to the seller's customer.
>
> > *Air transportation*: ~ 2400 miles from Pennsylvania to California
> >
> > > Potential fly-over states: West Virginia; Ohio; Indiana; Illinois; Missouri; Kansas; Colorado; New Mexico; and Arizona.
> >
> > *Ground transportation*: ~ 10 miles in California

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Scenario 2: assume the same facts as Scenario 1 except the seller purchases standard shipping, 5-7 business days.

> Day 1: carrier drives the package to its sorting facility in Newark, New Jersey. The package is unloaded from the truck and placed in carrier's warehouse in Newark before midnight.
>
> > *Ground transportation*: ~ 90 miles from Pennsylvania to New Jersey
>
> Day 2: the package is sorted and loaded onto a truck driving to Springfield, Illinois.
>
> Days 3 – 4: carrier drives to Springfield.
>
> > *Ground transportation*: ~ 915 miles from New Jersey to Illinois
> >
> > > Potential drive-through states: Pennsylvania; West Virginia; Ohio; and Indiana.
>
> Days 4 – 6: The package arrives in Springfield and is loaded onto a truck driving to Phoenix, Arizona. The package arrives in Phoenix, and it is loaded onto a truck driving to San Diego. In San Diego, the package is loaded onto a delivery van.
>
> > *Ground transportation*: ~ 1990 miles from Illinois to California

Potential drive-through states: Missouri; Oklahoma; Texas; New Mexico; and Arizona.

Day 7: the package is delivered to the customer.

Ground transportation: ~10 miles in California

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Scenario 3: assume the same facts as Scenario 2.

Days 4: the package is sorted and put into carrier's warehouse in Springfield, Illinois.

Day 5 – 6: the package is loaded onto a truck and driven to St. Louis, Missouri, where it is loaded on a third-party's railroad, and transported to Los Angeles, California. Third-party unloads the package from the railcar and loads it onto an independent contractor's truck. The independent contractor/trucker drives the package to third-party's warehouse, which is 60 miles outside of San Diego. Third-party unloads the package at the warehouse and puts it into storage.

Ground transportation: ~ 105 miles from Illinois to Missouri

Rail transportation: ~ 1590 miles from Missouri to California

Potential ride-through states: Arkansas; Texas; New Mexico; Arizona; and California.

Ground transportation: ~ 60 miles in California

Day 7: carrier picks-up the package from the warehouse, loads into onto carrier's truck, and drives the package to the customer in San Diego.

Ground transportation: ~ 20 miles in California

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Scenario 4: assume the same facts as Scenario 3, except on Day 4, there is a blizzard traveling across the mid-west.

Days 3 – 5: the package is sorted and put into carrier's warehouse in Springfield, Illinois.

Day 5: the package is loaded onto a third-party's airplane, and flown to Newark, New Jersey. Third-party unloads the package from the airplane, carrier collects package from third-party's sorting facility, loads the package onto carrier's truck, and puts it into carrier's warehouse in Newark.

Air transportation: ~ 910 miles from Illinois to New Jersey

Potential fly-over states: Indiana; Ohio; and Pennsylvania.

Day 6: carrier withdraws the package from its warehouse and loads it onto carrier's airplane. Airplane flies to San Diego.

Air transportation: ~ 2420 miles from New Jersey to California

Potential fly-over states: Pennsylvania; West Virginia; Ohio; Indiana; Illinois; Missouri, Kansas; Colorado; New Mexico; and Arizona.

Day 7: carrier unloads airplane, loads package onto carrier's truck, and drives the package to the customer in San Diego.

Ground transportation: ~10 miles in California

D. Federal Preemption

There are several different federal preemption laws that should guide and inform the Work Group's discussions. Relevant here is the Anti-Head Tax Act (AHTA) that prohibits states from levying or collecting a tax, fee, head charge, or other charge on the gross receipts from air commerce or transportation. 49 U.S.C. § 40116. "Air commerce" includes package delivery. 49 U.S.C. § 40102(a)(3). The AHTA makes uniformity impossible in states that impose gross receipts taxes (e.g., in lieu of corporation net income taxes) because the mode of transportation determines taxability. It may also impact uniformity and horizontal equity concerns for companies with intermodal transportation.

Other federal preemption laws relevant here include the Airline Deregulation Act (ADA), which prohibits states from enacting laws "relating to a price, route, or service of an air carrier," and the Uniformity Carrier Registration Act (UCR), which prohibits states from imposing a tax on interstate licensing and that is not equally applicable on intrastate licensing. 49 U.S.C. §§ 41713(b)(1), -14504a. Both provisions may impact uniformity because the ADA preempts state laws and regulations that have a connection or reference to an air carrier's prices, routes, or services and the UCR prohibits states from in treating interstate and intrastate carriers differently. Thus, creating a uniform sourcing regulation for all "package delivery companies," or impacting whether an entity is a "package delivery company," may result in disparate impact among taxpayers.

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We appreciate the Work Group's efforts thus far to understand the transportation industry. We ask that the Work Group take the above into consideration such that any work product not pick winners and losers among the stakeholders, including industry members and the states in which they do business.

Respectfully,

Eric Tresh
Eversheds Sutherland (US) LLP
999 Peachtree St NE
Atlanta, GA 30309

Charlie Kearns
Eversheds Sutherland (US) LLP
700 6th Street, NW
Washington, DC 20001

Chelsea Marmor
Eversheds Sutherland (US) LLP
1114 Avenue of the Americas, 40th FL
New York, NY 10036

Catalina Baron
Eversheds Sutherland (US) LLP
1001 Fannin Street #3700
New York, NY 77002