



## Southeast State & Local Tax: Important Developments - June

06.14.2013

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### VIRGINIA

#### TAX INCREASES (EFFECTIVE JULY 1, 2013)

##### State-Wide

- Gasoline tax of \$0.175 per gallon eliminated.
- New 3.5% wholesale tax on gasoline (6% on diesel fuels) implemented.
- Sales and use tax increases from 5% to 5.3% statewide (except exempt food purchases).
- Motor vehicles tax increases from 3.0% to 4.0%.
- License tax on electric motor vehicles increases from \$50 to \$64.

##### Regional Taxes

- Additional sales and use tax of 0.7% applies in Northern Virginia and Hampton Roads.
- Additional grantor's tax of \$0.15 per \$100 applies in Northern Virginia.
- Additional transient occupancy tax of 2% applies in Northern Virginia.
- Additional Sales tax of 2.1% on motor vehicle fuels applies in Hampton Roads.

#### RULINGS OF THE TAX COMMISSIONER

##### *Sales and Use Tax*

- **Guidelines for Accelerated Sales Tax.** Sales and use tax dealers with \$26 million or more in taxable sales and purchases in the previous fiscal year must make an additional payment in June of each year equal to 90% of their sales and use tax liability for the previous year. A "dealer" includes every person required to collect and remit sales tax, as well as every person required to remit use tax to Virginia. In [Va. P.D. 13-61](#), the Department of Taxation issued guidelines for the additional payment required to be made by dealers in June 2013.
- **Property Purchased Under Government Services Contract Subject to Use Tax** The

Department of Taxation held that the taxpayer, a government contractor that provided training courses in firearms, was subject to the sales and use tax on tangible personal property purchased in connection with the service contracts. Under Va. Code § 58.1-609.1(4), the sales and use tax does not apply to tangible personal property for use by governmental agencies. However, the Department held that the provision of services (i.e., training) in this case was the “true object” of the transactions. As such, all tangible personal property purchased under the service contracts was used by the taxpayer and subject to sales and use tax. [Va. P.D. 13-73](#).

#### *Allocation and Apportionment*

- **Single Sale Factor Guidelines Published.** The Department of Taxation clarified the methods that a manufacturer may use to calculate the “average” number of full-time employees for the base year (the taxable year before the single sale factor apportionment election) and in each of the three years after the election. The “average” must be determined by using the mean, median or mode method. Using the number of employees at the end of the year (or any other single day) does not come within the meaning of “average.” The Department also rejected the taxpayer’s method of using total hours worked by all employees divided by 1,680. [Va. P.D. 13-84](#).

#### *Business, Professional and Occupational Tax*

- **Home Renovation Business Subject to BPOL Tax.** The Department of Taxation held that a taxpayer was subject to the BPOL tax as a contractor unless the taxpayer could provide documentation that its activities extended beyond purchasing, renovating and selling real estate. The taxpayer, a limited liability company, hired a contractor to rehabilitate a residential dwelling acquired by the taxpayer in County A. The taxpayer did not have an office in County A, but its owner resided in County A. The Department held that the taxpayer was engaged in business in County A because it purchased the dwelling for sale and was likely looking for other investment opportunities. The Department also ruled that, under Va. Code § 58.1-3700.1, when an individual engaged in a business maintains no definite place of business, his residence is the definite place of business. Therefore, the taxpayer was subject to the BPOL tax in County A. [Va. P.D. 13-76](#).

#### *Individual Income Tax*

- **Itemized Deductions Denied to Part-Year Resident.** The Department of Taxation denied a Virginia part-year resident taxpayer’s request to use a pro-rated standard deduction for Virginia income tax purposes in the same year that he itemized his federal income tax deductions. The taxpayer was able to begin itemizing his federal income tax deductions when he moved to Maryland and purchased a home. Under Va. Code § 58.1-322(D)(1)(B), taxpayers may claim the Virginia standard deduction only if they have not elected to itemize their federal deductions. As the taxpayer elected to itemize his federal income tax deductions and the payments giving rise to such deductions (i.e., interest and property tax) were made while he was a Maryland resident, the taxpayer was not entitled to any deduction against Virginia income taxes. [Va. P.D. 13-72](#); *see also* [Va. P.D. 13-64](#).
- **Tax Credits.** The Department of Taxation issued a notice to provide taxpayers with information on the annual cap for the qualified equity and subordinated debt investments tax credit. For the 2012 tax year, the tax credit cap was \$4 million. The tax credit limit increases to \$4.5 million in 2013 and to \$5 million in 2014. For taxable years after 2014, the credit will remain at the statutory limit of \$5 million unless the General Assembly takes further action. [Va. P.D. 13-75](#).

#### **DISTRICT OF COLUMBIA**

- **Annual Real Property Tax Sale.** The Office of Tax and Revenue will conduct its annual real property tax sale on July 15 through July 17, 2013. Purchasers must come to 1101 4th Street, SW, 2<sup>nd</sup> Floor – Room 250, Washington, DC 20024. Each day, the sale will be conducted from 8:30 a.m. until Noon and from 1 p.m. until 4 p.m., or until all the real properties scheduled for sale for that day are sold. Additional information can be found on the website for the Office of Tax and Revenue at <http://otr.cfo.dc.gov/page/annual-real-property-tax-sale>
- **Energy Efficiency Loan Agreements.** The Sustainable DC Act of 2012 provides that unpaid special assessments levied under energy efficiency loan agreements will be collected under D.C. Code § 47-1336. The special assessments are treated as an additional real property tax. The legislation also provides procedures in which the Chief Financial Officer can sell the real property subject to the special assessment to the lender, loan servicer or third party for \$1 or no consideration. [L. 2013, Act 19-615 \(Law 19-262\) \(Effective April 20, 2013\)](#).
- **Vehicle & Trailer Tax.** The Excise Tax Amendment Act of 2012 clarifies the exemptions and exceptions from payment of the excise tax on the issuance of certificates of title for motor vehicles and trailers. The legislation provides that a bona fide gift of a vehicle already titled in D.C. between spouses, between parent and child or between domestic partners is exempt from the tax. Motor vehicles titled to a non-resident in another jurisdiction also are exempt from the tax. [L. 2013, Act 19-634 \(Law 19-272\)](#).

## NORTH CAROLINA

- **New Developments in North Carolina Tax Reform Initiatives.** For several months, the North Carolina Senate and House have considered competing tax reform proposals. On June 10, the House passed HB 998 on its third reading and sent it to the Senate for consideration. On June 11, the Senate rolled out its version of tax reform in a proposed committee substitute for HB 998. On June 12, the Senate Finance Committee gave a favorable report for the proposed committee substitute. It is expected that the Senate's version will pass the Senate this week and be sent to a Senate/House conference committee.

The Senate's proposed committee substitute signaled a significant departure from SB 677, sponsored by Senators Rucho and Rabon, co-chairs of the Senate Finance Committee. Among other items, they had proposed a sweeping expansion of the sales tax base by expanding the sales tax to approximately 120 services, most of which are not currently subject to sales tax in North Carolina. See recent alert [here](#)

- **Municipal Privilege License Tax Ruled Unconstitutional.** The North Carolina Court of Appeals reversed a trial court's order granting summary judgment to the City of Fayetteville regarding the city's privilege tax. The taxpayers sold blocks of Internet usage to customers in the City of Fayetteville. The city enacted a privilege license tax on "electronic gambling operations" of \$2,000 per business location and \$2,500 per computer terminal with a minimum tax of \$4,500. Before the increase, the privilege license tax was \$50. The court of appeals held that the 8,900% tax increase in the minimum tax violated the Just and Equitable Tax Clause of the North Carolina Constitution. [Smith v. City of Fayetteville, No. COA11-1263-2 \(N.C. Ct. App. 2013\)](#).

## MARYLAND

- **Local Tax Credit for Resident Owners of Pass-through Entities.** The Maryland Court of Appeals denied a motion filed by the Maryland Comptroller of the Treasury to reconsider the court's previous decision that the failure of Maryland law to provide a credit for county taxes paid by Maryland residents with pass-through entity income violated the Dormant Commerce Clause. The

court clarified that its original opinion did not preclude Maryland from imposing different tax treatment of income taxes that are not based on pass-through personal income. The court also clarified that Maryland can provide another method of providing relief against the discrimination, such as apportionment, in addition to a credit. [Wynne v. Comptroller of the Treasury, Md. Ct. App., Dkt. No. 107, Sept. Term 2011 \(2013\)](#).

- **Real Property Recordation and Transfer Tax Exemption Extended to LLCs.** The General Assembly enacted legislation extending the real property recordation and transfer tax exemption to certain transfers between affiliated LLCs. Previously, the exemption applied only to affiliated corporations. The new legislation provides that a “business entity” includes corporations and LLCs, but not partnerships. [H.B. 372, Leg. 2013 \(Md. 2013\)](#).

## SOUTH CAROLINA

- **Sales and Use Tax Exemption – Equipment Used in Manufacturing Facility.** The Department of Revenue issued guidance regarding the sales and use tax exemption for certain material handling systems and equipment used in a manufacturing or distribution facility (e.g., carts, conveyors, forklifts, piping and racks used in the operations of the facility). Manufacturers must satisfy certain investment requirements to claim the exemption. [S.C. Rev. Rul. 13-3](#).

## AROUND THE NATION

- **California – Special Purpose Entities Had Nexus.** The May 1, 2013 decision by the San Diego Superior Court in *Harley Davidson, Inc. & Subs. v. California FTC*, has California focusing on special purpose entities (“SPEs”) again. In *Harley*, SPEs functioned as securitization and financial subs for Harley. The SPEs provided loans to buyers of Harley products and then securitized those loans into notes which it then sold to third parties. Each SPE was restricted to doing business with the related group and was under the control of the parent. The California court found that even though the SPEs had no physical presence in California, their relationship with the other related entities created an agency relationship, and, therefore, the California sourced “sales” were includable in the sales factor of the combined group report. The California court also held that the SPEs were considered “financial institutions” for purposes of California law because of the nature of their activity (i.e., issuing securities, making loans, securitizing loans). [Harley Davidson, Inc. v. California Franchise Tax Board, Cal. Sup. Ct., San Diego \(California\), No. 37-2011-00100846-Cu-MC-CTL \(May 1, 2013\)](#).
- **California – Non-Resident General Partner Found Liable for Minimum Tax.** The California State Board of Equalization held that a Nevada corporation was liable for the California minimum franchise tax as the general partner of a partnership doing business in California. *Sup, Inc., Cal. State Bd. Of Equal*, Dkt. No. 571262 (Nov. 14, 2012) (released for publication March 7, 2013).
- **Massachusetts – Sham Transaction.** The Massachusetts Appellate Tax Board applied the sham transaction doctrine to deny the tax benefits created when a corporate subsidiary (“ADSW”), which was doing business in Massachusetts, transferred its tax, insurance and audit functions to its U.S. parent (“ADNAC”) to create a physical presence and nexus for ADNAC in Massachusetts. ADSW applied an apportioned share of ADNAC’s losses to offset the income of the combined group. The Massachusetts Appellate Tax Board held that centralization of the tax, insurance and audit functions was not a legitimate business purpose of the transfer and denied the tax benefits created by the transfer. [Allied Domecq Spirits and Wines USA, Inc. v. Comm’r of Rev, Mass. App. Tax Bd., Dkt. No. C282807 \(May 22, 2013\)](#).
- **Michigan – Multistate Tax Compact.** The Michigan Court of Claims recently held that the

Multistate Tax Compact is a binding multistate compact that cannot be repealed by a subsequent statute. *Anheuser-Busch, Inc. v. Michigan Dep't of Treasury*, Mich. Ct. of Claims, Case No. 11-85-MT (June 6, 2013). *Anheuser-Busch* marks the first case since the California Court of Appeals' decision in *Gillette* to apply interstate compact law in upholding the MTC's election. See also [\*Gillette Co. v. Franchise Tax Bd.\*, 209 Cal. App. 4th 938 \(2012\), review granted and opinion superseded sub nom., 291 P.3d 327 \(Cal. Jan. 16, 2013\).](#)

- **Tennessee – General Partnership Interest Creates Taxable Nexus.** A Tennessee chancery court held that a British company whose only activity in the United States was a 45% interest in a general partnership had nexus with Tennessee and was doing business in Tennessee. [\*Vodafone Americas Holdings, Inc. v. Roberts\*, Tenn. Chancery Ct. Case No. 07-1860-IV \(March 19, 2013\).](#)
- **Possible Multistate Tax Commission Transfer Pricing Audit Program**– The Multistate Tax Commission (“MTC”) will consider a request from one of its member states to create a transfer pricing audit program. Transfer pricing is sometimes thought of as a multinational issue, but many multistate companies utilize IRC § 482 transfer pricing type studies to justify their intercompany charges. One of the issues in state tax departments is that, while taxpayers may have the resources to fund a transfer pricing study, the states have limited budgets and cannot afford to develop internal transfer pricing expertise. A joint effort by the MTC to develop transfer pricing expertise would assist states in challenging taxpayer IRC § 482 studies.

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