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Business activity tax federal bill re-introduced, including Joyce rule; hearing scheduled

April 8, 2011

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On Friday, April 8, 2011, US Representatives Bob Goodlatte (R-VA) and Bobby Scott (D-VA) introduced H.R. 1439, the Business Activity Tax Simplification Act of 2011. While the legislation is substantially similar to legislation introduced in prior sessions -- including expansions of Public Law 86-272, a codified physical presence nexus standard, a 15-day de minimis period for the imposition of a business activity tax, and other changes -- it also includes a "Joyce" standard for including in the numerator of the apportionment factors only those entities "that are themselves subject to taxation by the State" pursuant to the Act's revised nexus standard. The legislation would apply to taxable periods beginning on or after January 1, 2012. A hearing in the House Judiciary Subcommittee on Courts, Commercial and Administrative Law has been scheduled for Wednesday, April 13, 2011.

"Modernization" of Public Law 86-272

Similar to previous versions of the legislation, H.R. 1439 would "modernize" P.L. 86-272 by applying the restrictions of the Public Law to all "business activity taxes," rather than limiting its application to net income taxes. Business activity taxes are defined as "any tax in the nature of a net income tax or tax measured by the amount of, or economic results of, business or related activity conducted in the State." Transaction taxes (e.g., sales and use taxes) are excluded from the definition. The legislation would also remove the limitation of the Public Law to "sales" of "tangible personal property," instead applying the Public Law to the solicitation of orders (sent outside the state for approval or rejection) or of *customers* in the state "for sales or transactions." Conforming changes would be made throughout the Public Law.

Public Law 86-272 would also be amended to protect certain other "business activities" from the imposition of state and local business activity taxes, including the "furnishing of information to customers or affiliates" in the state, coverage of events or other gathering of information in the state, where the information is used or disseminated from a point outside the state, and business activities directly related to the taxpayer's potential or actual purchase of goods or services within the state, where the final decision to purchase is made outside the state.

"Physical presence" standard codified

Further, the legislation provides that no state would have the power to impose, assess, or collect a business activity tax on any person relating to such person's activities in interstate commerce unless the person has a physical presence in the state during the taxable period. H.R. 1439 provides that the term "physical presence" does not include presence "for less than 15 days in a taxable year" (i.e., two weeks). Further, the legislation provides that the term "physical presence" would not include presence in a state "to conduct limited or transient business activity." No definition is given with respect to "limited" or "transient" for purposes of this exclusion.

A person is deemed to have a physical presence only if such person's business activities in the state include (1) being an individual physically in the state, or assigning one or more employees to be in the state; (2) using the services of an agent (excluding an employee) to establish or maintain the market in the state, but only if the agent does not perform business services in the state for any other person during the taxable year; or (3) leasing or owning tangible personal property or real property in the state (excluding the leasing or licensing of computer software). Engaging in any of these activities counts against the 15-day threshold noted above.

Joyce over Finnigan

The legislation would enact a new section, not contained in prior proposals, entitled "Group Returns." Under this section, where the net income or other economic results (e.g., gross

receipts) of affiliated persons are taken into account in determining a net income or other business activity tax liability of a person for a taxable year (e.g., in a mandatory state combined return), (1) the amount of combined or consolidated net income (or other economic results) subject to tax in a state "shall be computed using the methodology that is generally applicable to businesses conducting similar business activities"; and (2) if this methodology employs an apportionment formula, the denominator(s) shall include the aggregate factors of all persons whose net income or other economic results are included in such combined or consolidated net income (or other economic results), and the numerator(s) shall include the factors attributable to the state "of only those persons that are themselves subject to taxation by the State pursuant to the provisions of this Act and subject to all other legal constraints on State taxation of interstate or foreign commerce."

PwC observes

"The Business Activity Tax Simplification Act would address a number of concerns for multistate businesses," observes Ferdinand Hogroian, Washington National Tax Services Director with PwC in Washington, D.C. "As seen by the fact that this legislation delves into areas of apportionment for combined groups, merely addressing nexus standards, as in the past, may not be enough. Clearly, state advances in the area of economic nexus over the years, along with creative ways to tax the income of affiliates, have made this proposal timelier than ever. The question will be whether this legislation can progress to enactment. In the past, with a Republican House, similar legislation has advanced to a scheduled House floor vote, although the vote itself never occurred. The hearing scheduled for April 13 is an encouraging sign that early movement on this legislation may be possible in the 112th Congress."

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