SUTHERLAND

SALT SCOREBOARD

Q2 2016

This is the second edition of the Sutherland SALT Scoreboard. Each quarter, we tally the results of what we deem to be significant taxpayer wins and losses and analyze those results. This issue of the SALT Scoreboard includes Sutherland's observations on states' conformity to insurance tax law, states' manufacturing exemptions for sales taxes, and states' treatment of the Multistate Tax Compact.

SECOND QUARTER 2016

Overall, the second quarter of 2016 was tough on taxpayers, as states and localities prevailed in 39 out of 60 significant cases.[1] 28 sales and use tax cases and 20 corporate income tax cases made our cut of significant cases. In our Second Quarter Spotlight (see page 2), 10 manufacturing and processing exemption cases factored into our year-to-date tallies.

1 Some items may have been decided in a prior quarter but included in the quarter in which we summarized them.

SIGNIFICANT TAXPAYER WINS AND LOSSES

45 WINS

2016 OVERALL RESULTS

63 LOSSES

QUARTER 1		QUARTER 2		QUARTER 3		QUARTER 4	
24	24	21	39				
W	L	W	L	W	L	W	L

YEAR-TO-DATE

Taxpayers prevailed in 14 OUT OF 34 significant corporate income tax cases across the country

Taxpayers prevailed in 20 OUT OF 50 significant sales and use tax cases across the country

SIGNIFICANT MULTISTATE DEVELOPMENTS

Due Process

CASE: *Corrigan v. Testa*, Slip Op. No. 2016-Ohio-2805 (Ohio May 4, 2016).

SUMMARY: The Ohio Supreme Court held that the Due Process Clause of the U.S. Constitution precluded Ohio from taxing a nonresident individual on an apportioned share of his gain from the sale of a limited liability company that conducted business in the state. The court explained that the seller was not part of the entity's unitary business because the seller merely provided "stewardship" services, rather than actively managing the business. View more information.

Insurance

CASE: *In re Aetna, Inc.*, Nos. TAT(E)12-3(GC), TAT(E)12-4(GC) (N.Y.C. Tax App. Trib. June 3, 2016).

SUMMARY: The New York City Tax Appeals Tribunal determined that a health maintenance organization was subject to the New York City general corporation tax. Notably, the Tribunal determined that HMOs were regulated almost entirely under the Public Health Law, not the Insurance Law, and therefore were not engaged in an insurance business in the state. View more information.

SUTHERLAND OBSERVATION: Many states look to federal tax law to determine if a corporation's status is an insurance company for state tax purposes. This case is notable because the Tribunal distinguished the federal case law on the issue instead of relying on it.

Remote Sellers

CASE: *Scholastic Book Clubs, Inc. v. Ala. Dep't of Revenue*, No. S. 14-374 (Ala. Tax Trib. Mar. 25, 2016).

SUMMARY: The Alabama Tax Tribunal concluded that an out-of-state retailer had nexus with Alabama for use tax collection purposes because of the activities of unrelated, uncompensated teachers in the state. View more information.

SUTHERLAND OBSERVATION: The Scholastic Book cases have been litigated in several states since the 1990s with mixed results. However, in light of the changing nexus landscape in the states in recent years, it is not surprising that the Alabama Tax Tribunal concluded that the teachers' distribution of catalogs and order forms to students, collection of money for orders and mailing of the orders and money to Scholastic Books resulted in a sales and use tax collection obligation for Scholastic Books in Alabama.

SIGNIFICANT MULTISTATE DEVELOPMENTS *CONT'D*

Retailers

CASE: *Office Depot, Inc. v. Dir. of Revenue*, 484 S.W.3d 793 (Mo. 2016) (en banc).

SUMMARY: The Missouri Supreme Court held that a taxpayer was not subject to Missouri's use tax on catalogues shipped to Missouri residents when the printing and mailing of the catalogues occurred outside of Missouri and the taxpayer did not exercise any right or power incident to ownership or control over the catalogues in Missouri.

Multistate Tax Compact

CASE: *Kimberly-Clark Corp. v. Commissioner of Revenue*, No. A15-1322 (Minn. June 22, 2016).

SUMMARY: The Minnesota Supreme Court held that Minnesota's adoption of the Multistate Tax Compact did not create a binding contractual obligation and, as a result, the state's subsequent repeal of the Compact's alternative apportionment election provision was not prohibited as unconstitutionally impairing contractual obligations. View more information.

Data Processing Services

CASE: *Hegar v. CheckFree Servs. Corp.*, No. 14-15-00027-CV (Tex. App. 14th Dist., Apr. 19, 2016).

SUMMARY: The Texas Court of Appeals held that the taxpayer's online bill pay service was not a taxable data processing service for Texas sales tax purposes because any activities the Comptroller labeled as data processing services were incidental to the professional services provided by the taxpayer. View more information.

SUTHERLAND OBSERVATION: While the Texas Comptroller of Public Accounts has generally taken a broad interpretation of what constitutes taxable data processing services, this decision highlights an important exclusion from the definition of "data processing." Specifically, the definition excludes providers of other professional services who use a computer to facilitate the performance of their services. The services provided by CheckFree Services Corporation fell within this exclusion.

SIGNIFICANT DEVELOPMENTS

CASE: *Sw. Royalties, Inc. v. Hegar*, No. 14-0743 (Tex. June 17, 2016).

SUMMARY: The Supreme Court of Texas held that an oil and gas exploration and production company's purchases of equipment were not exempt from sales tax under various processing exemptions because the hydrocarbon changes were caused by natural pressure and temperature changes and not by the equipment. View more information.

CASE: *Bridges v. Nelson Indus. Steam Co.*, 190 So.3d 276 (La. 2016).

SUMMARY: The Louisiana Supreme Court concluded that limestone purchased for the dual purposes of absorbing sulfur during the generation of electricity and producing ash for sale to third parties was exempt from Louisiana sales tax under the "further processing exclusion" because it was sufficient that the inclusion of the raw material into a sold by-product was a purpose for which the taxpayer purchased the material. View more information.

CASE: *Graphic Packaging Int'l, Inc. v. Lewis*, 187 So.3d 499 (La. Ct. App. 2016).

SUMMARY: The Louisiana Court of Appeals held that a paperboard products manufacturer was entitled to sales tax refunds for purchases of chemicals used in the manufacturing process under the "further processing" exclusion because they were identifiable components of the end product, benefited the end product, and purchased with the purpose of being included in the end product. View more information.

CASE: *In re Gray Oil Co.*, No. 2014-05 (Wyo. State Bd. of Equalization Apr. 8, 2016).

SUMMARY: The Wyoming State Board of Equalization determined that sales of oil and lubricants used to lubricate machinery at a crude oil refinery did not qualify for an ingredient/component sales tax exemption because they were not used directly in the manufacturing process or consumed or destroyed during the process.

CASE: *Walther v. Carrothers Constr. Co. of Ark., LLC*, 2016 Ark. 209 (Ark. 2016).

SUMMARY: The Supreme Court of Arkansas held that equipment used in a water treatment facility expansion was not exempt from use tax under a manufacturing exemption because the facility's water treatment process did not transform the water into a different article. View more information.

OVERALL SUTHERLAND OBSERVATION: While state economic development authorities often advertise their favorable environment for manufacturing businesses, recent cases emphasize how state revenue departments narrowly construe their manufacturing and processing exemptions and that taxpayers bear a considerable burden to meet each element of the exemptions.

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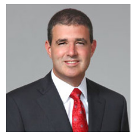
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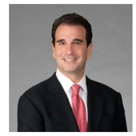
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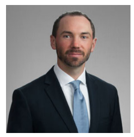
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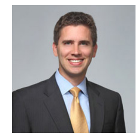
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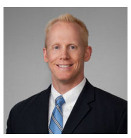
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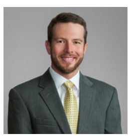
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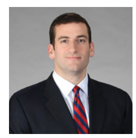
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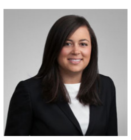
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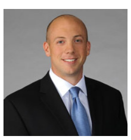
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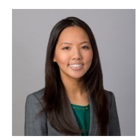
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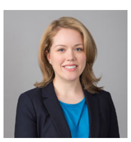
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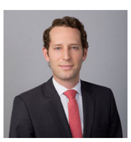
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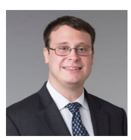
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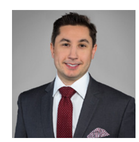
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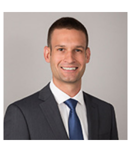
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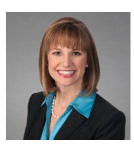
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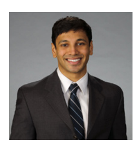
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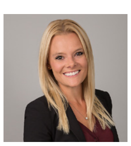
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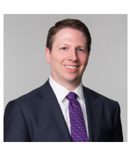
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