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March 16, 2016

VIA FACSIMILE 775-684-2020

Deonne E. Contine
Executive Director
State of Nevada
Department of Taxation
1550 E. College Parkway, Suite 115
Carson City, NV 89706

Re: Comments on Proposed Regulation of the Nevada Tax
Commission; LCB file no. R123-15 -- March 11, 2016 draft.
Comments on draft Instructions for Commerce Tax Return -
Draft 4

Dear Director Contine,

The purpose of this correspondence is to provide additional comments with respect to the March 11, 2016 draft of the Proposed Regulation of the Nevada Tax Commission, LCB file no. R123-15 (the "Proposed Regulation") and to provide comments on the draft Instructions to the Commerce Tax return, Draft 4.

1. Inconsistency with respect to limited-liability companies verses S Corporations. Section 4 of Senate Bill 483 enacting the Commerce Tax defines "business entity" in an all-encompassing manner listing the various types of business organizations that can be formed under Nevada law. Subsection 4(2) then provides exceptions to those persons and entities that are not considered a "business entity" for purposes of the Commerce Tax. Subpart (l) thereof then excepts a "passive entity."

Section 14 of Senate Bill 483 defines "passive entity" as follows:

"1. For the purposes of this chapter, a business is a 'passive entity' only if:

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- a. The business is a limited-liability company, general partnership, limited-liability partnership, limited partnership or limited-liability limited partnership, or a trust, other than a business trust;
- b. During the period for which the gross revenue of the business entity is reported pursuant to section 20 of this act, at least 90% of the business entity's federal gross income consists of the following income:
 - (1) Dividends, interest . . . and income from a limited-liability company;
 - (2) Capital gains . . ."

Page 1 of the Instructions for Commerce Tax return provides that each business entity engaged in business in Nevada, unless specifically excluded by law, is required to file the Commerce Tax return. There are certain exclusions contained in these instructions, including passive entities with the reference to Section 14 of SB.483 quoted above.

Page 2 of the Instructions under the subheading "Revenue" provides in pertinent part as follows:

"Revenue

Do not include in revenue:

- . . . Distributions from corporations, including S-corporations, and distributive or proportionate share of receipts and income from partnerships or LLCs"

First, as a tax lawyer, Section 14's definition of "passive entity" is intended to cover those business entities that are "flow-through" entities whose income, deduction, and credit are reported by the owners of the entity and taxed at their level. This would include most limited-liability companies, general partnerships, limited-liability partnerships, limited partnerships, limited-liability limited partnerships, and most trusts.

Missing from this list of "flow-through" entities is a "S corporation." For all intents and purposes a S corporation is taxed very much like a partnership. The shareholders of a S corporation receive a Form K-1 just as do partners of a partnership and members of a LLC. Those Forms K-1 report the distributive share of income and other items to be reported on that shareholder's, partner's or member's income tax return. Accordingly, not including S corporations in this category seems to be an oversight.

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Not to further complicate the matter, but something I need to call to the attention of the Department and members of the Tax Commission is the fact that the default taxation of limited-liability companies is as a partnership. However, it is fairly common practice today for an entity to be formed under state law as a limited-liability company, but the members elect instead to be taxed as a S corporation for income tax purposes. This trend may accelerate in Nevada for the simple reason that if one wants to be taxed as a S corporation, but not to form a corporation so as to avoid the now \$500 annual business license fee, a limited-liability company could be formed instead and then elect to be taxed as a S corporation. Following the 2015 Nevada Legislature, LLCs only pay \$200 per year for the Nevada business license, rather than \$500 as a corporation. That cost deferential can be meaningful over time.

In addition to the foregoing, page 2 of the Instructions for the Commerce Tax return with respect to S corporations should be changed so that S corporations would be treated in a like manner as partnerships or LLCs. Doing so, would not limit the revenue exclusion to "distributions" only but should include the "distributive or proportionate share of receipts and income" from the S corporation.

I submit that the Department has the authority to adopt by regulation the inclusion of S corporations within the definition of a permissible "passive entity." This authority is found in several sections of SB 483. For example, Section 16 of SB 483 provides that the Department shall "administer and enforce the provisions of this chapter, and may adopt such regulations as it deems appropriate for that purpose."

Please note that these changes would merely include S corporations as potentially being classified as passive entities. They must still pass the gross revenue test such that at least 90% of the entity's gross income would come from passive sources as defined in Section 14 of SB 483.

One of the items specifically mentioned as being included in the definition of passive income at Subsection 14(b)(1) is "income from a limited-liability company". Strong consideration should be given to expanding this to also include income from a partnership. As noted above, by default, LLCs are taxed as partnerships. But they are a separate entity formed under a separate Chapter under the Nevada Revised Statutes. Accordingly, (and I note that the Instructions to the Commerce Tax return already so provide, the Proposed Regulation should likewise be amended to conform to the spirit and intent of SB 483 that income from partnerships be considered passive. There is no logical reason as to why it should be limited to "income from a limited-liability company."

2. Section 17 definition of Gross Revenue for Nevada Commerce Tax purposes. First, I applaud and support the revision made in Section 17(2) to include the modifier of "**Nevada** gross revenue" for those entities to simply check the box at the top

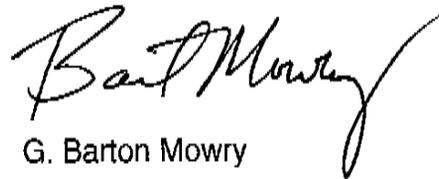
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of the Commerce Tax return with the declaration. I suggest, however, that a conforming change be made to Section 17(2)(e) of the Proposed Regulation such that the affirmation signed under penalty of perjury is that the "**Nevada** gross revenue" of the entity was less than \$4,000,000.

We appreciate your consideration of the comments and suggestions above. Please do not hesitate to contact me if I can be of any further assistance to the Department. Thank you for your continued cooperation and assistance.

Respectfully submitted,



G. Barton Mowry

GBM/km
c: (via fax) George Hritz, Management Analyst