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Via email: vashekon@tax.state.nv.us

Nadia Vasheko
Commerce Tax Manager
State of Nevada
Department of Taxation
Grant Sawyer Office Building
555 E. Washington Ave, Suite 1300
Las Vegas, NV 89101

**Re: Comments on Proposed Regulation of the Nevada Tax Commission; LCB
File No. R123-15**

Dear Ms. Vasheko,

We believe that the following comments and recommendations on the Proposed Regulation of the Nevada Tax Commission, LCB File No. R123-15 (the “Proposed Regulation”) are consistent with the statutory language of SB 483 (the “Bill”) and would aid in tax administration for the Department and for taxpayers. We also request further consideration of the comments we made on November 3, 2015 with respect to the September 8th proposed draft especially our comments at Paragraph 6 of our letter concerning “engaging in business in Nevada and jurisdiction to tax”.

Comments and Recommendations

1. Definition of “Business Entity”. Paragraph 1 of the Definitions section of the Proposed Regulation defining the term “business entity” is comprised of two parts. We believe that a minor clarification should be made to that paragraph to indicate that part “a” applies to entities governed, organized or incorporated pursuant to Title 7 of Nevada Revised Statutes or similar statutes of other states, and that part “b” applies to trusts, natural persons and entities not described in part “a.” Below are recommended modifications to the language of the Proposed Regulation marked to show our suggested clarifications to the definition of business entity:

1. “Business entity” means:
 - a. an entity identified in subsection 1 of Section 4 of SB 483, which is organized or incorporated pursuant to Title 7 of Nevada Revised statutes or similar statutes of other states, or



- b. ~~an entity, a trust,~~ natural person, ~~or other entity not described in a., above,~~ who reports ~~their~~ its Nevada gross income for its business on any of the following Internal Revenue Schedules to Form 1040:
- i. Schedule C (Form 1040), Profit or Loss from Business, or
 - ii. Schedule E (Form 1040), Supplemental Income and Loss, - Part I or Part V, or
 - iii. Schedule F (Form 1040), Profit or Loss from Farming, or
 - iv. equivalent or successor schedules to Form 1040 referenced above,
- ~~for their business or any other person or entity.~~

2. Treatment of Entities Disregarded for Federal Income Tax Purposes. While it appears that the intent of the Bill is to recognize all entities as separate entities regardless of their federal tax classification, that intent is not explicit in the language of the Bill. We therefore suggest that an additional item be added to the Definitions section of the Proposed Regulation indicating that all entities, including entities disregarded for federal income tax purposes, are treated separately for purposes of the commerce tax without regard to their federal income tax classification.

3. Filing Requirements of Businesses not Classified as “Business Entities”. We believe clarifying that businesses not classified as “business entities” under the Bill are not required to file an annual return would be helpful to the Department and taxpayers. We recommend that language to that effect be added to Section 1(1) of the proposed regulation as follows:

- 1. The tax imposed by Senate Bill 483 is an entity based tax. Each business entity must file the annual return pursuant to Sec. 20 of SB 483 with the Department, even if the business entity has no tax liability pursuant to Secs. 24-49 of SB 483. Businesses not classified as business entities pursuant to Sec. 4 of SB 483 and these regulations need not file the annual return.

4. Engaging in Business in Nevada and Jurisdiction to Tax. Section 2 of the Proposed Regulation describes the circumstances in which a business entity will be determined to be engaged in business in Nevada. A business entity will be subject to the Commerce Tax only if it is engaged in business in Nevada and if Nevada has jurisdiction to tax the entity (or nexus). The taxing jurisdiction of Nevada for purposes of the Commerce Tax shall be exercised to the full extent permitted by the Constitution of the United States, subject to the following:

- a. The Commerce Tax is not an income tax, and Public Law 86-272, 15 U.S.C. 381, shall not apply to limit the exercise of Nevada’s taxing jurisdiction.

b. As illustrated by the activities listed in Section 2, some physical presence within Nevada of the taxpayer, the taxpayer's employees, independent contractors or other representatives acting on behalf of the taxpayer is required to establish taxing jurisdiction. The presence of customers in Nevada, without such physical presence of the taxpayer, the taxpayer's employees, independent contractors or other representatives acting on behalf of the taxpayer, is not sufficient to establish nexus. With respect to business entities located outside of Nevada that sell to customers within Nevada who place orders via internet websites, the taxpayer's payment of remuneration to persons located in Nevada that provide internet-based referrals to the taxpayer shall not, without more, constitute nexus or support jurisdiction to tax.

5. Persons Whose Activities are Confined to Owning, Maintenance and Management of Intangible Investments. We believe minor adjustments to the language of Section 5 of the Proposed Regulation are appropriate for purposes of consistency and clarification. Recommended modifications to the language of Section 5 of the Proposed Regulation is included below, marked indicating our suggested modifications.

1. For purposes of subparagraph (m) of subsection (2) of section 4 of S.B. 483, the phrase "person whose activities within this State are confined to owning, maintenance and management of the person's intangible assets" means any legal entity, including a trust, whose activities within Nevada are confined to owning, maintenance and management of intangible assets of which such legal entity or ~~the~~ trust is the legal owner.
2. For purposes of subparagraph (m) of subsection (2) of section 4 of S.B. 483, the types of intangible assets similar to the investments in stocks should include an interest in other legal entities, organized or incorporated pursuant to Title 7 of Nevada Revised statutes or similar statutes of other states, without regard to whether the person, or the beneficiary, or the fiduciary controls or participates in the management of such entities.

6. "Passive Entity" Definition. Because application of the definition for "passive entities" in Section 14 of the Bill is complex and potentially inconsistent with the application of other portions of the Bill and the Proposed Regulation, we believe that several clarifications would be helpful to both the Department and to taxpayers. Our recommendations for defining the term "Passive Entity" for regulatory purposes appears below:

"Passive entity" defined.

- (1) A "passive entity" is excluded from the definition of business entity by Section 4(2)(1) of SB 483. For the purposes of this chapter, a business is a "passive entity" only if the entity satisfies an organizational test, a passive income test that requires at least 90 percent of the entity's gross income to consist of specified categories of passive investment income, and an active trade or business income test that requires no more than 10 percent of the entity's gross income to be received from conducting an active trade or business. These tests are applied for each taxable year of the entity.

- (2) **Organizational Test.** An entity satisfies the organizational test for “passive entity” status if the entity 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. Accordingly, entities that are in the form of a corporation, an unincorporated association or a business trust may not satisfy the organizational test for “passive entity” status. However, a partnership or limited liability company satisfies the organization test for “passive entity” status without regard to its classification for federal income tax purposes as a partnership, disregarded entity or corporate entity.
- (3) **Passive Income Test.** An entity satisfies the passive income test for “passive entity” status if, during the period for which the gross revenue of the business entity is reported pursuant to section 20 of this act, at least 90 percent of the business entity’s federal gross income consists of the following income:
 - (a) Dividends, interest, foreign currency exchange gains, periodic and nonperiodic payments with respect to notional principal contracts, option premiums, cash settlements or termination payments with respect to a financial instrument, and income from a limited-liability company;
 - (b) Capital gains from the sale of real property, gains from the sale of commodities traded on a commodities exchange and gains from the sale of securities; and
 - (c) Royalties, bonuses or delay rental income from mineral properties and income from other nonoperating mineral interests.

For purposes of this passive income test, “income” does not include any (i) rent, or (ii) income received by a nonoperator from mineral properties under a joint operating agreement if the nonoperator is a member of an affiliated group and another member of that group is the operator under that joint operating agreement. The passive income test is applied only to the income received directly by the entity and not to the entity’s share of income received by any pass-through entity in which it has an interest (without regard to whether the entity has management rights or control of such other entity).

- (4) **Active Trade or Business Test.** An entity satisfies the active trade or business income test for “passive entity” status if the business entity does not receive more than 10 percent of its federal gross income from conducting an active trade or business. A business entity is “conducting an active trade or business” for purposes of this test if:
 - (a) The activities being carried on by the business entity include one or more active operations that form a part of the process of earning income or

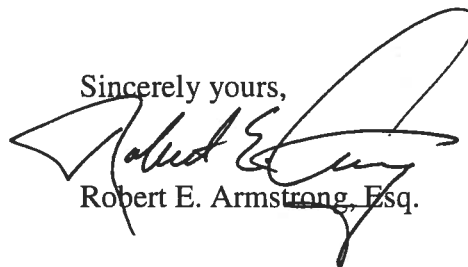
profit, and the business entity performs active management and operating functions; or

- (b) Any assets, including, without limitation, royalties, patents, trademarks and other intangible assets, held by the business entity are used in the active trade or business of one or more related business entities.

For purposes of determining whether an entity is engaged in an active trade or business, (i) the ownership of a royalty interest or a nonoperating working interest in mineral rights does not constitute the conduct of an active trade or business; (ii) the payment of compensation to employees or independent contractors for financial or legal services reasonably necessary for the operation of a business does not constitute the conduct of an active trade or business, and (iii) holding a seat on the board of directors of a business entity does not by itself constitute the conduct of an active trade or business. In general, the active trade or business income test is applied only to the income received directly by the entity from the conduct of a trade or business and not to the entity's share of income received by any pass-through entity in which it has an interest (without regard to whether the entity has management rights or control of such other entity), and the business activity of any pass-through entity is not attributed to the entity owning an interest in the pass-through entity. However, for purposes of determining whether an entity is engaged in an active trade or business, activities performed by a business entity include activities performed by persons outside the business entity, including independent contractors, to the extent that those persons perform services on behalf of the business entity and those services constitute all or any part of the business entity's trade or business.

We appreciate the Department of Taxation and the Nevada Tax Commission consideration of our comments and please do not hesitate to contact us. Thank you for your attention in this matter.

Sincerely yours,



Robert E. Armstrong, Esq.

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cc: Deonne Contine, Executive Director, Department of Taxation (via email: contine@tax.state.nv.us) Gregory L. Zunino, Bureau Chief, Bureau of Business and State Services, Office of the Attorney General (via email: gzunino@ag.nv.gov) Bryan Fernley, Principal Deputy Legislative Counsel, Legal Division (via email: bryan.fernley@lcb.state.nv.us) George Hritz, Management Analyst III, Nevada Department of Taxation (via email: ghritz@tax.state.nv.us)