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DATE: October 8, 2015

TO: Deonne Contine, Executive Director
Nevada Department of Taxation

Submitted via email

Pauline Oliver, Deputy Director
Nevada Department of Taxation

FROM: Carole Vilardo, President

SUBJECT: Suggested Changes to the proposed Commerce Tax regulations dated September 9 and 25.

The following three pages contain suggested changes to the proposed commerce tax regulations which were the subject of workshops held on September 9 and September 25.

For the “general” regulation which was the subject of the workshop held on September 9, regulation, suggested changes (additions and deletions) are provided for four of the sections.

For the proposed regulation on “situs” I have identified three issues of concern with corresponding suggestions as to how those concerns might be addressed.

I know that you have received a number of suggestions for changes to the regulations and am looking forward to the next workshop when we can see how all of the changes have been “packaged” into one regulation. Also, is there any word yet on when the reporting form will be available to circulate to our members and ask for their feedback?

Thank you for your consideration to the attached changes. Please call me if you would like to discuss the proposed changes further.

Suggested changes to the Proposed Commerce Tax Regulation discussed at the September 9, 2015 Workshop

(Proposed changes are shown in ***blue italics*** and language suggested for deletion is **[bracketed]**.)

TAXABLE ENTITY V. BUSINESS ENTITY

NTA A number of questions have been raised as to why this section is necessary, and why the emphasis on a “taxable entity?” The phrase has generated the perception that the base would be potentially broadened. If this provision is to remain in the regulation then I suggest the following changes. However, with the proposed wording change, section 4 could stand-alone and would be a simpler way to convey that a business entity is a taxable entity. Additionally I do not believe that section 5) is needed.

“Clarifying [a taxable business entity and] the requirements of a [taxable] business entity”

1) *The tax imposed by Senate Bill 483 is an entity based tax. Each [taxable] business entity must file the annual return pursuant to Sec. 20 of SB 483 even if the [taxable] business entity has no tax liability pursuant to Secs. 24-49 of SB 483*

2) “*[Taxable] Business entity*” *[means:]*

[a person or entity in this State that is engaging in a business including]

(a) those entities identified] has the meaning ascribed to it in Sec. 4 of SB 483, which includes Subchapter S corporations.

[b) the entity or person who files the Schedule C (Form 1040), Profit or Loss from Business, or its equivalent or successor form, a Schedule E (Form 1040), Supplemental Income and Loss, or its equivalent or successor form, or a Schedule F (Form 1040), Profit or Loss from Farming, or its equivalent or successor form, for that business or any other person or entity.]

3) *Engaging in a business has the meaning ascribed to it in Sec. 6 of SB 483*

4) *The Department will determine that a[n] business entity is commencing, conducting or continuing a business in this State, and therefore a taxable entity, if it conducts certain activities, including without limitation, any of the following:*

Please Note: Sections (a) through (u) are not shown

[5) Taxable entity does not include those entities specifically excluded from the definition of business entity as provided in Sec. 4 of SB 483.]

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NAICS CODE DESIGNATION

NTA There are different reasons a business with more than one NAICS CODE could have a different primary NAICS Code within a year or two of filing their initial return. For example, a business entity could sell property in a quarter that exceeds the revenue for their commonly/publically identified business type that year. As the code is the basis for the revenue generated to the State, it is bound to be an issue raised when the entity has an audit by the Department. Following is suggested language to address that issue, and issues involving the change of the NAICS code and the notification of acceptance of a change in the NAICS Code. In addition, the regulation should indicate that the NAICS code to be used should identify those codes listed in SB 483, to avoid having a business entity using one of the 19,000 plus codes that makes up the NAICS codes list.

“Process for reporting and changing the NAICS Code designation.”

Sec. 1. The [taxpayer] business entity will designate its NAICS code as provided in SB 483 sections 24-49 and corresponding tax rate on its initial Commerce Tax return and will use such NAICS code designated on its initial return on all subsequent Commerce Tax returns filings with the Department. Unless the Department discovers that the taxpayer has submitted an erroneous or inaccurate NAICS code, the [taxpayer] business entity Department will record the designation on the initial return as the NAICS code for the [taxpayer] business entity. If the Department determines that the taxpayer has submitted an erroneous or inaccurate NAICS code, Department will notify the [taxpayer] business entity requesting additional documentation or clarification regarding the NAICS code designation.

Sec. 2.1 A business entity will identify their primary NAICS code based on the code which has the greatest Nevada gross revenue averaged over the prior three years.

- a. A business entity that has been operating in Nevada for only two years it will use the NAICS code in which the greatest Nevada gross revenue has been averaged over the prior two years.*
- b. For a new business entity the NAICS code shall be determined by the greatest amount of Nevada gross revenue to be projected.*

The average revenue will be calculated based on the annual federal income tax filing of the business entity.

Sec. [2] 3. If the taxpayer intends to use a NAICS code designation different from the NAICS code initially designated by the taxpayer, the taxpayer must notify the Department in writing on a form designated by the Department at the same time it files its Commerce Tax Return. The request should include the prior category, the new category, the reason for the change and all documentation supporting its change in NAICS category.

Sec. [3] 4.1 The Department will review the NAICS designation change request and make a determination regarding the change in NAICS designation and tax rate within 60 days of receipt of the request and documentation required herein.

4.2 The Department shall not consider a taxpayer’s use the use of a NAICS code any other federal, state or local government agency.

Sec.5 . If the Department does not respond within 60 days, the change will be considered granted.

Sec. 6. A request by the business entity for a change in the NAICS code made during the period the filing and payment are due shall allow the business entity to delay the filing and payment of the commerce tax pending a response by the department. The penalty and interest will be waived if the filing and payment are remitted within 10 business days following the determination.

Sec. 7. If the Department later determines that a NAICS code change was submitted based on fraudulent or erroneous information, and the change resulted in underreporting of tax liability by the taxpayer, the Department shall not be estopped from assessing liability.

RECOVERY CHARGE

NTA This section is confusing as written; the language of Section 1 and Section 2 appear to be contradictory to one another. Following are suggested changes.

“Commerce Tax Recovery Charge”

Sec. ____ 1. The Commerce Tax is a tax imposed on the gross revenue of a business. It is not a tax on the customer. [~~and the business entity is prohibited from assessing it directly against the customer.~~]

2. *The business entity may itemize a “Commerce Tax recovery charge” on an invoice or receipt if:*
 - a. *The business entity explains to its customers that the charge is made in order to recover money paid by the business for taxes imposed upon it pursuant to NRS _ [Commerce Tax].*
 - b. *The invoice clearly indicates that the **itemized** recovery charge is ~~is included in~~ part of the total price collected from the customer and is not an additional charge assessed (such as a tax or fee) on the customer’s total.*
 3. *The total amount collected from the customer is the measure of Commerce Tax, less allowed deductions.*
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AFFILIATED GROUP: COMMERCE TAX CREDIT

NTA Subsection (b) of Section 6 was identified by some of our members as “... creating a new definition for what constitutes being *engaged in the same business or similar businesses* and seems to conflict with the definition of an *affiliated group*, a term that is already clearly defined, well understood, and conforms to a federal standard.” Furthermore, separating out corporate entities that would otherwise be considered as part of the same affiliated group would probably create further administrative challenges for the state.

“Amend NAC 363A and B as follows: (to allow for payroll provider to take Commerce Tax Credit toward affiliated group (MBT Liability)”

Sec. 6.

1. *An employer may apply to the Department to be recognized as a payroll provider by submitting to the Department such forms, application materials and supporting documents as the Department may require. To be recognized as a payroll provider, the employer must demonstrate to the satisfaction of the Department that:*

- (a) *The employer meets each of the conditions described in section 5; and,*
~~(b) *The members of the affiliated group are engaged in the same business or similar businesses;*~~
(c) *Each member of the affiliated group would have a recurring liability for the modified business tax if the persons providing services exclusively for that member were treated as that member’s own employee and not those of the payroll provider.*
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Proposed Regulation on the Commerce Tax Regarding Situs discussed at the September 25 Workshop
Proposed changes are shown in ***blue italics***.

GUIDELINES FOR SITUSING SERVICES UNDER THE COMMERCE TAX

NTA The guidelines in this regulation are helpful however, there is a total of 54 examples, while the NAICS codes listed in SB 483 number 25 with a 26th code as “The unclassified business category. . . .” For many of the examples in this regulation there is either no obvious NAICS code to associate with the example, or there are multiple NAICS codes that could apply to the example. For instance, in Section “(4) Agency - - Other” the NAICS code is not obvious, but Section “(44) Repair/maintenance/installations services,” is an example of a guideline that can apply to multiple NAICS codes. Without listing these examples under a corresponding NAICS code, it is difficult for a business entity to read these examples in context.

Following is a suggestion to change the format of the regulation.

Group the “example” or “examples” under the appropriate NAICS code in the sequence identified in sections 24-49 of SB 483. That will allow the business entity to review the example in context with the NAICS code, and the way they do business.

ADDITIONAL “EXAMPLE” NEEDED FOR GUIDELINES

NTA A number of our members ship the goods they supply. If the origin of the shipment is a location in Nevada and it is delivered to another location in Nevada, the revenue is sitused to Nevada. (See example “51) - Transportation” in proposed situs regulation.)

In a number of instances various methods of shipping may be utilized by a supplier. The supplier can use their own vehicles, or contact with a third party, or allow the purchaser to pick up the goods using the purchaser’s vehicle, or any combination of these methods.

I suggest that the following language as an example of situs for a supplier.

A supplier that provides for the delivery of goods and products they sell from a location in Nevada to a destination outside of Nevada shall not situs the revenue to Nevada if the following applies:

- (a) There is a valid contract agreement between the supplier and purchaser identifying how the delivery/deliveries will be made; and***
 - (b) A bill of lading for the shipment shows the destination state.***
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SB 483 – Commerce Tax – Sections 2 thru 61

Issues to consider for clarification and/or regulation development

October 1, 2015

Section 8:

Issue: Definition of "Gross Revenue" – "amounts realized" is unclear as it applies to hospitals as we bill in a uniform manner but collect different amounts for these services based on who is paying for the service and the patient's ability to pay.

Recommendation: Clarify that this means amounts collected (not billed) for services provided. For health care providers, gross revenue means revenue less contractual allowances /discounts. (line 1C IRS Form 1120)

Section 12:

Issue: Tax year is the State fiscal ending June 30 of each year and most Commerce Tax payers will be operating on a calendar year.

Recommendation: We ask that the State make a **technical correction** to modify its process and allow the tax payer to elect their taxable year to match their federal tax year including the following:

- If the tax payer elects tax year other than SFY – allow for a stub period filing in the first year to bridge to the tax payers elected tax period.
- Consider matching filing due date to the federal filing date – 75 days after the end of the fiscal period which will allow information that is common between both returns to be known prior to filing.
- If an organization is sold mid-year, each owner is responsible for filing a commerce tax return for the portion of the year they owned the business.
 - o Any tax credit earned by the seller of a business entity can be transferred to the buyer of that business.

Section 20:

Issue: Uncertain as to whether business entities that don't exceed \$4 million of NV gross revenues are required to file.

Recommendation: Need confirmation all taxable business entities are required to file.

Section 21 - Deductions:

Subsection (i)

Issue: This subsection allows health care providers to deduct payments received from Medicaid, Medicare, SCHIP, Hospital care for Indigent Persons, or Tricare/ Workers Comp/ actual uncompensated costs. The Department has proposed language (see attached) to calculate uncompensated costs that will be quite burdensome to maintain in addition to current reporting and does not adequately address the inherent delays in being able to determine uncompensated cost.

Recommendation: Ask the Department to clarify in the regulations:

1. Payments from Government-funded programs including those administered by private managed care organizations (i.e. Medicaid, Medicare, Workers Comp. MCO's, etc.) are included in the deduction.

2. Utilize the Uncompensated Cost Report (which is part of the annually required Community Benefit reporting for hospitals in Nevada -see example attached) to establish the uncompensated cost ratio from the most recent reported year – which is generally 8 – 12 months after the close of the fiscal year. The uncompensated cost ratio will be applied to billed charges for payers defined in the uncompensated cost report for the current tax year to estimate current year uncompensated cost. We would like to work with the Department to refine the methodology for the industry that takes into consideration the inherent lag in being able to estimate uncompensated costs.

Subsection (i):

Issue: This subsection only allows health care institutions to deduct 50% of the amount quantified in subsection (i) – institutions may also in certain circumstances employ/bill/collect for physician services and should be treated the same as independent physicians when doing so.

Recommendation: Regulations should clarify that this reduced deduction applies to health care “gross revenue” related to institutional services only. In other words, the limitation applies to the revenue stream(s) and not the entity itself.

Subsection (q):

Issue: References exclusion of receipts from the sale of section 1221 or 1231 property per the federal tax code. Is the amount of the receipt equal to the federal tax basis or equal to GAAP?

Recommendation: Clarify that the receipts are per GAAP or federal tax basis.

Subsection (x):

Issue: Subsection (x) allows for 100% deduction of bad debt reported for federal income tax purposes.

Recommendation: Clarify subsection (x) applies to hospitals the same as all other businesses.

Subsection (z):

Issue: This subsection appears to address factored accounts receivable and allows business entities to deduct amounts realized from factoring to the extent already included in gross receipts

Recommendation: We propose that the business entity selling the accounts receivable be responsible for paying taxes related to the services they provided at the value that were able to collect (in this case from the factoring company) and the factoring company should only pay tax on amount they collect above what they paid for the receivable (should be considered pass thru revenue under subsection (l)).

Section 22:

Subsection (1) (b):

Issue: Gross revenue from the sale of property located in Nevada is subject to the commerce tax. If a business sells a building and buys or builds another building, it appears the entire sales price of the first building is taxed even though the proceeds are invested in a new location.

Recommendation: Confirm with the Department that the proceeds from the sale are considered as deductions similar to the tax basis for securities under section 21 subsection (m).

Other:

1. Given the filing deadline is only 45 days after June 30 each year and several components of the statute refer to methods (section 50) or amounts from federal income taxation (section 21 subsection which will not have occurred yet for most organizations, consider the following:
 - a. Work with the Department to consider allowing businesses to elect a fiscal period that matches their filing time frames for federal income tax purposes and allow a stub period in the first year that will bridge the business entity to their newly elected reporting period (base deductions on estimates).
 - b. Clarify if extensions are allowed section 20 subsection 4.
2. Confirm treatment of Commerce tax credit (50% of commerce tax paid last year) to reduce Modified Business Tax liability can be used within an Affiliated Group.
3. What was the intent of Section 50? The entity's method of accounting for gross revenue for purposes of the commerce tax must be the same as the method used for federal income tax purposes yet there are a number of other references to using GAAP accounting.

Possible Legislative Fixes/Changes to Consider

Sections 8 and 50:

Issue: Conflicts in the sources of information to calculate commerce tax liability: Subsection 3(g) indicates to follow GAAP, but Subsection 3(d) references federal tax codes sections for exceptions to "gross revenue". Also, see Section 50, which references using the same accounting method as federal income tax purposes.

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Section 12:

Issue: Tax year is the State fiscal ending June 30 of each year and most Commerce Tax payers will be operating on a calendar year.

Section 21 subsection (j): This subsection only allows health care institutions to deduct 50% of the deductions listed in section 21 subsection (i). We would like the Department to consider eliminating section 21 subsection (j) so that all health care providers (including institutions) are treated the same and are allowed to deduct 100% of the payments related to government payers and uncompensated costs outlined in section 21 subsection (i).

Sections 68 and 70

Issue: Commerce tax credit should be able to be utilized by other affiliated group members. Not different than the cellular industry, many times business entities in an affiliated group are organized for specific business purposes but in practice operate as one or at least in support of each other. Therefore tax credits earned by one business entity if not usable by that entity should be able to be used by other business entities in affiliated group or "family".

UNCOMPENSATED COST REPORT

HOSPITAL: Example Hospital

Period:

12/31/2014

Line PART I - Calculate Ratio of Cost to Charges (RCC)

1	Total Operating Expenses (A)	\$ 539,918,302	
2	Non - Operating Expense (A)	\$ -	
3	Total Hospital Expenses (sum of oper & non-oper exp)	\$ 539,918,302	0
<u>Less Cost Directly Assigned to Uninsured Patients</u>			
4	Graduate Medical Education Cost (B)	\$ (2,769,257)	FROM COST REPORT
5	Emergency Room Physician Professional Fees (C)	\$ (11,209,964)	
	Other Directly Assigned Cost (list) - (D)		
6	1) Medicaid Eligibility Vendors (PAS)	\$ (3,786,826)	FROM PAS
7	2) Nursing Homes, etc	\$ (41,008)	
8	3)	\$ -	
9	4)	\$ -	
10	5)	\$ -	
<u>Less Cost Prohibited by CMS for DSH Purposes</u>			
11	Offsite Clinic Cost (E)	\$ -	
	Other Excluded Cost (list) - (F)		
12	1)	\$ -	
13	2)	\$ -	
14	Total Expenses Excluded from Cost Pool	\$ (17,807,055)	
15	Adjusted Cost Pool (Total expenses less excluded items)	\$ 522,111,247	
16	Billed Charges (G)	\$ 4,315,318,135	
17	Average Ratio of Cost to Charges (adj cost / charges)	<u>12.1%</u>	

(A) From the Nevada Hospital Quarterly Reports found at:

http://www.unlv.edu/Research_Centers/chia/utilizationandfinancial.htm

(B) Resident /Faculty Salaries and other costs in support of GME from hospital records.

Exclude allied health education programs.

(C) ER / Trauma /Anesthesiology on-call coverage and compensation to physicians for indigent patient care.

From hospital records. Exclude directorship fees and other services not directly related to patient care.

(D) Any identifiable cost that is solely related to uninsured patients from hospital records.

Examples include payments to nursing homes for placement of patients without pay source, and eligibility workers in excess of standard social services staff.

(E) All costs associated with operating clinics not on hospital campus from hospital records.

(F) Any other cost category specifically prohibited for DSH by regulation or policy

(G) From NHQR for your hospital for the reporting period.

Note: Cost reported as AB342 community benefits are included either in pool or directly assigned.