

The Comptroller of Public Accounts proposes amendments to §3.586, concerning margin: nexus, in response to the United States Supreme Court decision in *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018).

The comptroller adds titles to subsections and improves readability throughout the section.

The comptroller amends subsection (a) to allow effective dates in this section other than the effective date of January 1, 2008. Specifically, the amendment is in response to the decision in *Wayfair* affecting franchise tax reports due on or after January 1, 2020.

The comptroller amends subsection (b) to add the word "Texas" in front of "franchise tax" to maintain consistency within this section.

The comptroller amends subsection (d) to provide that a foreign taxable entity with a Texas use tax permit is presumed to have nexus and is subject to Texas franchise tax. This presumption codifies existing practice. Information formerly in subsection (d) concerning exemptions for trade show participants is now in new subsection (g).

The Court in *Wayfair* held that substantial nexus may result from substantial sales into a state without physical presence in that state. Tax Code, §171.001(b) provides that the franchise tax extends to the limits of the United States Constitution and the federal law adopted under the United States Constitution. The comptroller is proposing a safe harbor to simplify tax administration for both the agency and taxpayers by eliminating the need to litigate on a case-by-case basis whether activities constitute substantial nexus based on avilment of the substantial privilege of doing business in Texas. The comptroller amends subsection (e) to provide that a foreign taxable entity with annual gross receipts from business done in Texas of \$500,000 or more has nexus, even if the entity has no physical presence in Texas. The comptroller's office will apply this economic nexus

provision beginning with reports due on or after January 1, 2020. Information formerly in subsection (e) concerning Public Law 86-272 is now in new subsection (h).

The comptroller adds new subsection (f) to identify the criteria for determining the beginning date when a foreign taxable entity begins doing business in this state.

Public Benefit/Cost; Fiscal Implications for state or local government, small businesses, and individuals.

Comments on the proposal may be submitted to Teresa G. Bostick, Director, Tax Policy Division, P.O. Box 13528, Austin, Texas 78711-3528. Comments must be received no later than 30 days from the date of publication of the proposal in the Texas Register.

This amendment is proposed under Tax Code, §111.002 (Comptroller's Rules; Compliance; Forfeiture), which provides the comptroller with the authority to prescribe, adopt, and enforce rules relating to the administration and enforcement of the provisions of Tax Code, Title 2.

This amendment is in response to the United States Supreme Court decision in *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018).

<rule>

§3.586. Margin: Nexus.

(a) Effective date. The provisions of this section apply to franchise tax reports originally due on or after January 1, 2008, unless otherwise noted.

(b) Nexus. A taxable entity is subject to Texas franchise tax [in this state]when it has sufficient contact with this state to be taxed without violating the United States Constitution.

(c) Physical presence. Some specific activities that[which] subject a taxable entity to Texas franchise tax include, but are not limited to, the following:

(1) advertising: entering Texas to purchase, place, or display advertising when the advertising is for the benefit of another and in the ordinary course of business (e.g., the foreign taxable entity makes signs and brings them into Texas, sets them up, and maintains them);

(2) consignments: having consigned goods in Texas;

(3) contracting: performance of a contract in Texas regardless of whether the taxable entity brings its own employees into the state, hires local labor, or subcontracts with another;

(4) delivering: delivering into Texas items it has sold;

(5) employees or representatives: having employees or representatives in Texas doing the business of the taxable entity;

(6) federal enclaves: doing business in any area within Texas, even if the area is leased by, owned by, ceded to, or under the control of the federal government;

(7) franchisors: entering into one or more contracts with persons, corporations, or other business entities located in Texas, by which:

(A) the franchisee is granted the right to engage in the business of offering, selling, or distributing goods or services under a marketing plan or system prescribed in substantial part by the franchisor; and

(B) the operation of a franchisee's business pursuant to such plan is substantially associated with the franchisor's trademark, service mark, trade name, logotype, advertising, or other commercial symbol designating the franchisor or its affiliate.

(8) holding companies: maintaining a place of business in Texas or managing, directing, and/or performing services in Texas for subsidiaries or investee entities;

(9) inventory: having an inventory in Texas or having spot inventory for the convenient delivery to customers, even if the bulk of orders are filled from out of state;

(10) leasing: leasing tangible personal property which is used in Texas;

(11) loan production activities: soliciting sales contracts or loans, gathering financial data, making credit checks, collecting accounts, repossessing property or performing other financial activities in Texas through employees, independent contractors, or agents, regardless of whether they reside in Texas;

(12) partners:

(A) acting as a general partner in a general partnership which is doing business in Texas;

(B) acting as a general partner in a limited partnership which is doing business in Texas (a foreign taxable entity which is a limited partner in a limited partnership is not doing business in Texas, if that is the limited partner's only connection with Texas);

(13) place of business: maintaining a place of business in Texas;

(14) processing: assembling, processing, manufacturing, or storing goods in Texas;

(15) real estate: holding, acquiring, leasing, or disposing of any property located in Texas;

(16) services, including, but not limited to the following:

(A) providing any service in Texas, regardless of whether the employees, independent contractors, agents, or other representatives performing the services reside in Texas;

(B) maintaining or repairing property located in Texas whether under warranty or by separate contract;

(C) installing, erecting, or modifying property in Texas;

(D) conducting training classes, seminars or lectures in Texas;

(E) providing any kind of technical assistance in Texas, including, but not limited to, engineering services; or

(F) investigating, handling or otherwise assisting in resolving customer complaints in Texas.

(17) shipment: sending materials to Texas to be stored awaiting orders for their shipment;

(18) shows and performances: the staging of or participating in shows, theatrical performances, sporting events, or other events within Texas;

(19) solicitation: having employees, independent contractors, agents, or other representatives in Texas, regardless of whether they reside in Texas, to promote or induce sales of the foreign taxable entity's goods or services;

(20) telephone listing: having a telephone number that is answered in Texas; or

(21) transportation:

(A) carrying passengers or freight (any personal property including oil and gas transmitted by pipeline) from one point in Texas to another point within the state, if pickup and delivery, regardless of origination or ultimate destination, occurs within Texas; or

(B) having facilities and/or employees, independent contractors, agents, or other representatives in Texas, regardless of whether they reside in Texas:

(i) for storage, delivery, or shipment of goods;

(ii) for servicing, maintaining, or repair of vehicles, trailers, containers, and other equipment;

(iii) for coordinating and directing the transportation of passengers or freight; or

(iv) for doing any other business of the taxable entity.

(d) Texas use tax permit. A foreign taxable entity with a Texas use tax permit is presumed to have nexus in Texas and is subject to Texas franchise tax.

(e) Economic nexus. For federal income tax accounting periods ending in 2019 or later, a foreign taxable entity has nexus in Texas and is subject to Texas franchise tax, even if it has no physical presence in Texas, if during its federal income tax accounting period, it had gross receipts from business done in Texas of \$500,000 or more, as determined under §3.591 of this title (relating to Margin: Apportionment).

(f) Beginning date. A foreign taxable entity begins doing business in the state on the earliest of:

(1) the date the entity has physical nexus as described in subsection (c) of this section;

(2) the date the entity obtains a Texas use tax permit; or

(3) the first day of the federal income tax accounting period in which the entity had gross receipts from business done in Texas in excess of \$500,000.

(g)[(d)] Trade shows. See §3.583 of this title (relating to Margin: Exemptions) for information concerning exemption for certain trade show participants under Tax Code, §171.084.

(h)[(e)] Public Law 86-272. Public Law 86-272 (15 United States Code §§381 - 384) does not apply to the franchise tax.

This agency hereby certifies that the proposal has been reviewed by legal counsel and found to be within the agency's authority to adopt.

Issued in Austin, Texas, on

WILLIAM HAMNER
Special Counsel for Tax Administration
Comptroller of Public Accounts