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A first-year review of the
Nevada commerce tax

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A First-Year Review of the Nevada Commerce Tax

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This article reviews issues, considerations, and some open questions associated with the Nevada commerce tax, for which the first filings were due August 15 for the period from July 1, 2015, to June 30, 2016. The commerce tax is based on a business entity's gross revenue sourced to Nevada and is assessed at varying tax rates depending on the business entity's primary industry classification.

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I. Introduction

In June 2015 Nevada enacted its largest tax increase ever, the commerce tax, to bolster K-12 education funding.¹ The commerce tax, which became effective July 1, 2015, is imposed on the Nevada gross revenue of each business entity exceeding \$4 million in a taxable year at various rates that depend on the industry in which the business entity is primarily engaged.

For purposes of the commerce tax, the taxable year is defined as the 12 months beginning July 1 and ending June 30 of the following year, which coincides with the Nevada fiscal year.² The first taxable year for the new commerce tax began July 1, 2015, and ended June 30, 2016, and the first commerce tax return was due August 15, with a 30-day extension available. Questions, issues, and taxpayer considerations have arisen during that initial commerce tax taxable year and filing period.

II. Background

In his January 2015 State of the State address, Nevada Gov. Brian Sandoval (R) sought legislative approval of a new tax structure to provide additional funding for public education. Despite expected resistance from small business taxpayers and a history of failed business tax proposals (such as a margins tax proposed in 2014³), the commerce tax received bipartisan support from the congressional delegation. Introduced by Sandoval on March 23, 2015, the commerce tax legislation (SB 483) moved quickly, clearing the Assembly on May 31 and the Senate on June 1 before the governor signed an amended version on June 10. As a result of

that fairly rapid enactment, the Department of Taxation was challenged with promulgating regulations and developing tax forms in rather short order.

III. Overview of the Nevada Commerce Tax

A. Introduction

The commerce tax is imposed "for the privilege of engaging in a business" in Nevada on the gross revenue of each business entity sourced to the state.⁴ Consolidated returns are prohibited,⁵ and it is levied on an entity-by-entity basis on the Nevada source gross revenue of each business entity in excess of \$4 million. Business entities not meeting the \$4 million gross revenue threshold yet conducting business within the state are required to file the commerce tax return. However, the Department of Taxation has provided a simplified filing process for entities that affirm that the revenue threshold was not met and is not required to complete the portion of the form in which items of revenue and deduction are reported.⁶

B. Taxable Year

The taxable year for commerce tax purposes is applicable to all business entities subject to the tax and does not take into account a business entity's federal income taxable year.⁷ The statute also provides that "a business entity's method of accounting for gross revenue for a taxable year for the purposes of determining the amount of the commerce tax owed by the business entity must be the same as the business's method of accounting for federal income tax purposes for the business's federal taxable year which includes that calendar quarter."⁸ That might create issues for taxpayers that do not have a June 30 federal income taxable year-end, and consideration should be given to internal accounting processes necessary to comply. A related complication could arise if a taxpayer without a June 30 taxable year-end makes a method change for a federal taxable year that potentially results in two different methods within the July 1 to June 30 taxable year for commerce tax purposes.

Perhaps realizing the difficulties associated with reporting Nevada gross revenue on a June 30 taxable year-end, the Department of Taxation promulgated a regulation providing potential relief from penalties and interest for business entities that have timely filed the commerce tax return and relied on either prior-year commerce tax calculations or federal income tax calculations.⁹ The regulation states:

The Department may waive or reduce a penalty or interest, or both, for a late payment of the commerce tax if the Nevada commerce tax return was timely filed . . . and the Department determines that the late payment was made because, in calculating the Nevada gross revenue of the taxpayer, the taxpayer or the taxpayer's agent relied on:

- (a) The commerce tax calculations of the taxpayer for the taxable year immediately preceding the taxable year for which the commerce tax was paid; or
- (b) Federal income tax calculations of the taxpayer for the most recent federal taxable year of the taxpayer.¹⁰

The grant of relief from penalties and interest under that provision is only available if the taxpayer timely filed the commerce tax return, and is at the discretion of the Department of Taxation. It is unclear how the department will administer that waiver provision.

Another issue with the commerce tax's "tax year" is the apparent lack of a short-year method. Because taxable year for commerce tax purposes is not defined with reference to the business entity's taxable year for federal income tax purposes, it does not appear that events that trigger a short-period return for federal income tax purposes (for example, a change of ownership) also trigger a short-period return for commerce tax purposes. That might present problems in some instances, such as a reorganization or an acquisition in which financial information is not readily available or responsibility for filing and payment of the commerce tax is uncertain.

C. Due Date and Extension

The commerce tax return is due 45 days after the end of the taxable year. Based on Department of Taxation guidance, the first return was due August 15, 2016, and future returns will generally be due on August 15 in each succeeding year.¹¹ A business entity can apply for good cause for a 30-day extension to pay the commerce tax. Although no penalty will be charged, interest will accrue from the August 15 due date until the date of payment.¹² Interestingly, there are no estimated tax payment requirements regarding the commerce tax. The full amount of computed commerce tax is paid annually with the filing of the return.

In addition to the extension, the legislation provides for a grace period for the initial commerce tax return filing for the July 1, 2015, through June 30, 2016, taxable year. Specifically, SB 483 provides that the department "shall waive payment of any penalty or interest for a person's failure to timely file a report or pay the commerce tax . . . which occurs before February 15, 2017 . . . if the failure: (1) Occurred despite the person's exercise of ordinary care; and (2) Was not intentional or the result of willful neglect."¹³ In the final version of the instructions to the initial commerce tax return, that provision is referenced in the "extension to file" section, leading some taxpayers to inadvertently interpret the grace period as an available second extension.

It appears that the department will administer that penalty relief provision using the same administrative procedures it applies to other provisions for penalty relief (such as the modified business tax, discussed further below), and that taxpayers will be required to file and pay the underlying tax before any requests for waiver will be considered. The FAQs on the department's website provide that waiver requests filed under the grace period provision will be reviewed case by case.¹⁴

D. Whether a Business Entity Is 'Engaging in a Business' in Nevada

To determine whether it is subject to the commerce tax, a business entity must first determine: (1) whether it is the type of business entity within the scope of the tax; and (2) whether it meets the applicable nexus standard that would subject it to the levy of the commerce tax -- that is, whether it is considered to be "engaging in a business" in Nevada.

1. Business Entity

The term "business entity" is quite broad, and includes corporations, partnerships, sole proprietorships, limited liability companies and limited liability partnerships, business associations, joint ventures, business trusts, professional associations, joint stock companies, holding companies, and "any other person engaged in a business."¹⁵ Since the commerce tax is imposed on each business entity doing business in Nevada (that is, on an entity-by-entity basis)¹⁶ and because the definition of business entity for commerce tax purposes includes entities such as partnerships and LLCs, the commerce tax is imposed on entities typically not subject to federal income tax, such as flow-through entities and entities that are disregarded.

Although the business entity definition is broad, it excludes several types of entities. A business entity does not include, among other things, federally tax-exempt organizations, estates or trusts other than business trusts, and real estate investment trusts meeting certain criteria.¹⁷ The definition also excludes:

A person whose activities within this State are confined to the owning, maintenance and management of the person's intangible investments or of the intangible investments of persons or statutory trusts or business trusts registered as [a regulated investment company] and the collection and distribution of the income from such investments or from tangible property physically located outside this State. For the purposes of this paragraph, "intangible investments" includes, without limitation, investments in stocks, bonds, notes and other debt obligations, including, without limitation, debt obligations of affiliated corporations, real estate investment trusts, patents, patent applications, trademarks, trade names and similar types of intangible assets or an entity that is registered as an [RIC].¹⁸

Thus, a broad exclusion appears to exist for a person engaged solely in the maintenance and management of his or her own intangible investments. While the term "person" is undefined in the legislation or the regulations, it does not appear to be limited to a natural person, since the term "natural person" is frequently used elsewhere in the legislation and regulations when such a limitation appears to be intended.¹⁹ In that context, person seems to include entities organized as corporations, partnerships, LLCs, or in any other manner. Those entities would not be subject to the commerce tax to the extent their activities are limited to the owning, maintenance, and management of their own "intangible investments."

The regulations further provide that in addition to the intangible investments described in the statute, the term includes "an interest in any entity, including without limitation, a trust, S corporation, partnership, limited-liability company or other entity in which a person owns an interest, regardless of whether that person controls or participates in the management of the entity in which the person owns an interest."²⁰

Also, the regulations provide that that exclusion would apply even if the intangible investment is in a lower-tier operating entity and the upper-tier entity "controls or participates in the management" of the lower-tier entity. There is, however, a potential inconsistency between that exclusion and the fact that the term "business entity" is defined to include a holding company, defined as "an entity that confines its activities to owning stock in, and supervising management of, other companies."²¹ It appears that an entity that meets the definition of a holding company could potentially also meet the requirements of the exclusion. It is unclear how the department

will attempt to reconcile those two apparently contradictory provisions.

In addition to applying to a person whose activities are confined to the owning, maintenance, and management of its own intangible investments, the exclusion also applies to a person whose activities are confined to the maintenance and management of the intangible investments "of persons or statutory trusts or business trusts registered as [a RIC]." ²² Because only business trusts can qualify as a RIC, the phrase "registered as [a RIC]" in the context of the sentence appears to refer only to business trusts and does not apply to persons or statutory trusts. ²³

The statute also excludes a "passive entity" from the definition of a business entity, and defines a passive entity as an LLC, partnership, or (nonbusiness) trust that has at least 90 percent passive income. ²⁴ Passive income includes income such as dividends and interest from financial instruments, and capital gains on the sale of real property, securities, and commodities traded on a commodities exchange, but excludes rental income. ²⁵

The 90 percent passive income threshold is calculated with regard to a taxpayer's federal gross income of the above items. ²⁶ If a taxpayer's year-end differs from the commerce tax taxable year ending June 30, taxpayers at or near that threshold will need to consider potential book-to-tax timing differences to determine whether the passive entity definition may apply. ²⁷

2. Doing Business

As noted, the commerce tax is imposed on an entity-by-entity basis. Accordingly, businesses with multiple affiliates in their organizational structure will need to consider on an entity-by-entity basis which affiliates are subject to the tax. To make that determination, the regulations provide that "to determine whether a business entity is engaging in a business in that State, the Department must consider the activities of the business entity, and not the activities of other entities in which the business entity owns an interest." ²⁸

The commerce tax is imposed on any business entity incorporated or organized in Nevada. ²⁹ Also, the commerce tax applies to non-Nevada domiciled business entities engaged in business in the state. The statute defines business as "any activity engaged in or caused to be engaged in with the object of gain, benefit or advantage, either direct or indirect, to any person or governmental entity." ³⁰ The statute further provides that "engaging in a business" (which represents the basis on which a taxpayer may be subject to the tax) means conducting a business (as defined above) or otherwise exercising corporate powers of a business in Nevada. ³¹

The regulations provide 22 examples of what it means to engage in a business in Nevada, with applications across many categories of business activity. Aside from a broad catchall provision for engaging "in any other activity that constitutes sufficient nexus to subject the business entity to the commerce tax in a manner consistent with the United States Constitution," all of the examples involve a physical presence in Nevada. ³² The examples include holding consigned goods or inventory, performing services (including through employees or independent contractors), maintaining a place of business, lease or sale of real or tangible personal property, or delivering goods on business entity-owned vehicles in Nevada. ³³ Unlike states such as Ohio or California, the commerce tax statute does not include a bright-line factor-based economic presence nexus provision, whereby a company would be considered to be "doing business" in a

state and subject to tax if it meets some levels of sales to customers within the state.

The Department of Taxation has developed a nexus questionnaire available for businesses incorporated outside Nevada that do not have a Nevada secretary of state business license. The questionnaire summarizes the examples of "engaging in a business" as stated in the adopted regulations.³⁴ Business entities that answer no to each question are not required to register for the commerce tax. Those that answer yes to any question must submit the form to the department, which will then reply with a welcome letter that includes a unique tax ID number for commerce tax return filing purposes.

Based on the statute, regulations, and the nexus questionnaire, it appears reasonably clear that a business entity must have physical presence in the state to be subject to a filing requirement. Also, since the regulations require the department to consider only "the activities of the business entity, and not the activities of other entities in which the business entity owns an interest" for purposes of determining "whether a business entity is engaging in business" in Nevada, it appears the department will not be asserting nexus based on the activities of an affiliate doing business in Nevada.³⁵

E. Taxable Base

The commerce tax is imposed on Nevada gross revenue, which is derived from activities in Nevada considered to be "engaging in a business."³⁶ That amount is then subject to numerous exclusions and deductions. The resulting gross revenue is situated or sourced to Nevada under the statute's applicable rules discussed below, resulting in Nevada gross revenue.

1. Gross Revenue

Gross revenue is defined broadly as "the total amount realized by a business entity from engaging in business . . . without deduction for the cost of goods sold, that contributes to the production of gross income."³⁷ More specifically, gross revenue includes receipts from the sale of property, from services performed, from the use of property or capital, and any combination of the above.³⁸ The commerce tax requires an accounting method for determining gross revenue for the commerce taxable year to be the same accounting method used for federal income tax purposes.³⁹

2. Exclusions From Gross Revenue

The value of cash discounts, complimentary goods or services, or charitable donations is generally excluded from the commerce tax definition of gross revenue.⁴⁰ Also excluded are amounts realized "from the sale, exchange, disposition or other grant of the right to use trademarks, trade names, patents, copyrights and similar intellectual property."⁴¹ As such, while an intangible property holding company domiciled in Nevada would generally be required to file, the royalties and other income it earns regarding its IP would generally not constitute gross revenue for purposes of the tax.

Excluded from the definition of gross revenue are amounts realized from a transaction "described in, or equivalent to, section 118, 331, 332, 336, 337, 338, 351, 355, 368, 721, 731, 1031 or 1033 of the Internal Revenue Code . . . regardless of the federal tax classification of the

business entity."⁴² Also excluded are amounts "indirectly realized from a reduction of an expense or deduction," and "amounts that are not considered revenue under generally accepted accounting principles."⁴³

The exclusion for amounts that do not constitute revenue under GAAP lends clarity in situations in which it may be unclear whether some transactions should be included on a gross or a net basis. For example, GAAP provides guidance regarding whether "a company should report revenue based on (a) the gross amount billed to a customer because it has earned revenue from the sale of the goods or services, or (b) the net amount regained (that is, the amount billed to the customer less the amount paid to a supplier) because it has earned a commission or fee."⁴⁴

However, the exclusion for amounts that do not constitute revenue under GAAP may lead to uncertainties in some situations when read in combination with the aforementioned requirement that taxpayers follow their federal method of accounting to compute gross revenue for commerce tax purposes.⁴⁵ There are some situations in which an item is excluded from revenue under GAAP, but it is reported as income for federal income tax purposes. For example, under GAAP, liquidated damages received during a construction project for missed milestones or project completion delays are not recognized as revenue, but are instead recorded as a reduction to basis in property.⁴⁶ However, the receipt of liquidated damages may be treated as income from a federal income tax perspective in some situations.⁴⁷

It is unclear which provision would control in that instance. Would the liquidated damages be excluded from gross revenue because they do not constitute revenue under GAAP and are instead treated as the reduction of basis? Or would the business entity be required to include them consistent with how they are treated for federal income tax purposes? Does the requirement that a taxpayer follow its federal method of accounting simply require that an accrual basis taxpayer also compute gross revenue for commerce tax on an accrual basis? Or does it require that other book-to-tax adjustments be made?

Another situation in which the interaction between GAAP and the federal income tax treatment of an item may vary occurs when a business entity sells an interest in a lower-tier entity treated as a disregarded entity for federal income tax purposes. As noted, a federally disregarded entity -- such as an LLC that has not checked the box to be treated as corporation -- is nonetheless a recognized and taxable entity for commerce tax purposes.⁴⁸ Whether the transaction adopts the nontax characterization as a sale of an intangible asset, or adopts the federal income tax characterization as a sale of the underlying assets, could have different results for commerce tax purposes regarding the potentially available deductions and the applicable situsing method that applies. The legislation and the regulations are unclear regarding which treatment is appropriate.

3. Deductions From Gross Revenue

In addition to the exclusions from gross revenue, there are 27 deductions from gross revenue.⁴⁹ Those include a deduction for interest on government securities, returns, refunds, and bad debt expense, as well as industry-specific deductions for healthcare providers, insurance companies, employee leasing, and business entities required to pay the liquor excise tax.⁵⁰ Several more broad-based deductions are outlined below.

a. Income From a Passthrough Entity

Consistent with the commerce tax's entity-by-entity imposition, a deduction is allowed for "distributive or proportionate shares of receipts and income from a pass-through entity."⁵¹ A passthrough entity is "an entity that is disregarded as an entity for the purposes of federal income taxation or is treated as a partnership for the purposes of federal income taxation."⁵² The deduction seeks to avoid double taxation, since disregarded entities and partnerships are taxed on their own gross revenue under the commerce tax.

b. Passthrough Revenue

The commerce tax allows for a deduction of "any pass-through revenue of the business entity."⁵³ The deduction has a broad range of statutorily enumerated applications. Passthrough revenue includes any amounts required by law or fiduciary duty to be passed through to another business entity or the government. Similarly, it extends to taxes collected from a third party and remitted to the state, such as sales tax collected from a customer. (This deduction does not extend to any taxes imposed directly on the business entity.)⁵⁴ Some reimbursements for advances made for a customer or client, as well as amounts required by contract or subcontract to be passed on to a third party, are also considered passthrough revenue.⁵⁵

Significantly, passthrough revenue includes "revenue received by a business entity that is part of an affiliated group from another member of the affiliated group."⁵⁶ For that purpose, the term "affiliated group" is defined as "a group of two or more business entities, including, without limitation, a business entity [exempt from the commerce tax], each of which is controlled by one or more common owners or by one or more members of the group" when "controlled by" means "the direct or indirect ownership, control or possession of 50 percent or more of a business entity."⁵⁷

c. Interest Income

A deduction for interest income "other than interest on credit sales" is allowed.⁵⁸ A credit sale is defined as "a sale of goods by a seller who accepts payment for the goods at a later time."⁵⁹ Based on the statute's language, some uncertainty exists whether the deduction from gross revenue would be available to a lender providing financing for the sale of goods by a third party. However, because the lender would not be a seller of the goods, it would appear that such a lender would be entitled to a deduction regarding its interest income. The regulations do not provide any additional guidance regarding that deduction, though the final instructions to the commerce tax return state that gross revenue should include "interest income from credit sales *and loans*."⁶⁰ The instructions provide the following example:

Best rates, LLC is located in Long Beach, CA. It makes car loans to customers in California and Nevada. During the year the total interest revenue on the loans equaled to \$10 million, including \$5 million from Nevada customers. Hence, \$5 million is situated to Nevada.⁶¹

It is unclear in that example whether Best Rates LLC is providing financing for sales of automobiles by a third party, or whether it is providing financing for sales of its own inventory. To the extent that the example extends to the former scenario (that is, interest arising purely

from a loan transaction), the example is arguably inconsistent with the statute.

d. Revenue From IRC 1221 or 1231 Assets

A deduction is allowed for revenue derived "from the sale, exchange or other disposition of an asset described under section 1221 or 1231 of the Internal Revenue Code."⁶² IRC section 1231 governs gains and losses regarding the sale, disposition, or involuntary conversion of property used in a trade or business or "capital assets," which is either depreciable property or real estate used in a trade or business held longer than one year.⁶³ Section 1221 defines a "capital asset" such that its sale would be treated as capital gain (instead of ordinary income); generally, assets held for resale are not capital assets (either section 1221 or 1231 assets).⁶⁴ Taxpayers should closely monitor for transactions outside the normal scope of their business activities, such as the disposition of equipment, other depreciable property or real estate potentially qualifying under IRC sections 1221 or 1231, because any revenue (or gain) resulting from those transactions would not be in gross revenue.

e. Gaming License Fee Deduction

A deduction from gross revenue is permitted for the amount of gross receipts used to determine the gaming license fee imposed by the state and collected by the Nevada Gaming Commission.⁶⁵ Specifically, the deduction is for "the amount of . . . gross receipts used to determine the amount of [the gaming license] fee."⁶⁶ The monthly gaming license tax fee is based on gross revenue from table games, slots, and revenue "from any game or gaming device" used by the business entity and is reported and collected on a cash basis.⁶⁷

Because the gaming license fee is determined on a cash basis, while the commerce tax requires the use of the same accounting method used by taxpayers for federal income tax purposes, there could be a potential mismatch for business entities in the gambling industry that record gambling revenue on an accrual basis (that is, timing difference in recognition of gross revenue versus gaming license fee deduction).⁶⁸ The mismatch may be significant for gambling industry entities that offer customers markers, or gambling credit, which may collectively result in significant revenue accrued for federal income tax purposes, but for which cash has not been received and thus not yet subject to the gaming license fee. Although businesses subject to the gaming license fee will eventually take advantage of the deduction once the cash is received, taxpayers who find themselves in that situation should closely consider the potential impact.

4. Gross Revenue, Exclusions, and Deductions on the Commerce Tax Return

The commerce tax form itself provides eight categories of gross revenue (including "other revenue") and allows for general and industry-specific deductions.⁶⁹ However, there is no reference to the exclusions from gross revenue. The commerce tax return filing instructions list both the exclusions and deductions together as amounts not to be in revenue, but says that deductions (described in detail with examples) are "allowed to the extent they are included in gross revenue."⁷⁰ Taxpayers should therefore be familiar with the applicable exclusions and determine whether potential deductions are available in computing gross revenue.

F. Sourcing Rules

After calculating gross revenue with applicable exclusions and subtracting available deductions,

total gross revenue must be sourced to Nevada to determine Nevada gross revenue.⁷¹

Regarding sales of tangible personal property, Nevada generally follows the sourcing language in the Uniform Division of Income for Tax Purposes Act, except that no throwback rule is used. The statute provides that "gross revenue from the sale of tangible personal property is situated to [Nevada] if the property is delivered or shipped to a buyer in [Nevada], regardless of the F.O.B. point or any other condition of sale." Consistent with that rule, sales of tangible personal property are situated to the destination state, regardless of where title transfers or other conditions of sale.

Rents and royalties from tangible personal property are sourced to Nevada to the extent that the property is located or used in Nevada.⁷² Similar rules apply to rents, royalties, or gross revenue from the sale of real property, which are situated to Nevada to the extent that the property is located in Nevada.⁷³

Services are sourced to Nevada based on market sourcing principles -- that is, service revenue is sourced to Nevada "in the proportion that the purchaser's benefit in [Nevada] . . . bears to the purchaser's benefit everywhere."⁷⁴ The statute further specifies that the physical location where the purchaser receives the benefit of the service is "paramount" in determining the applicable portion of the revenue that should be sourced to Nevada. If a taxpayer's records cannot accurately establish a physical location for sourcing, the business entity may use a reasonable alternative sourcing method.⁷⁵ Under an additional rule regarding transportation services, those services are sourced to Nevada only if both the travel origin and destination locations are within the state.⁷⁶

The statute also includes a catchall sourcing rule requiring a taxpayer to source to Nevada any gross revenue not captured by the sourcing categories if the revenue is the result of "business conducted" in the state.⁷⁷ The primary determinant, as in the rule for sourcing services, is the purchaser's physical location. If a taxpayer's records cannot establish the purchaser's location, the statute provides that the gross revenue is excluded from Nevada.⁷⁸ Finally, if the sourcing rules do not "fairly represent" the taxpayer's business activities in Nevada, the department may authorize an alternative sourcing method.⁷⁹

The regulations promulgated by the Department of Taxation contain 53 sourcing examples relative to services performed across various business types -- including accounting, computer programming, finance, marketing, and waste management.⁸⁰ Each example defines the activity being performed and the rule by which the revenue generated from that activity is sourced to Nevada. The regulations also instruct taxpayers performing services not described in the regulations to rely on the statute's general market sourcing rule and, if still unclear about the application, look to the physical location of the purchaser receiving the benefit of the service provided.⁸¹ Taxpayers may also review the commerce tax return filing instructions, which offer hypothetical examples for various revenue types and sourcing rules. For example, interest from credit sales and loans -- discussed previously as income includable in gross revenue -- should be sourced "based on the location of the purchaser's use or benefit from service, or an alternative method can be used."⁸²

G. Industry Classification Tax Rates

After a business entity's revenue has been properly sourced, Nevada gross revenue is reduced

by \$4 million to calculate taxable revenue.⁸³ Instead of a flat tax rate on all business conducted in the state, the commerce tax imposes 26 different rates based on each business entity's industry classification.⁸⁴ The rate is determined by reference to the North American Industry Classification System (NAICS) used by federal agencies to classify businesses for statistical data.⁸⁵ Tax rates range from a low of 0.051 percent (applicable to mining, quarrying, and oil and gas extraction) to a maximum of 0.331 percent (applicable to rail transportation) of Nevada gross revenue over \$4 million.⁸⁶

A taxpayer's applicable tax rate is based on the business category (as described by its NAICS code) in which it is "primarily engaged."⁸⁷ Business entities having multiple revenue streams qualifying under differing industry classifications should use the NAICS code and tax rate of the revenue stream "with the greatest percentage of the business entity's Nevada gross revenue for the taxable year for which the return is filed."⁸⁸ In determining the applicable NAICS code and tax rate, taxpayers should consider the percentage of revenue streams sourced to Nevada, and not the percentage of total revenue streams from multistate operations. If a taxpayer's primary Nevada gross revenue stream is not described by a NAICS code in the statute, the business entity falls into an unclassified business category, which is taxed at a rate of 0.128 percent.

A taxpayer's initial commerce tax return filing designates the business entity's NAICS code and applicable tax rate.⁸⁹ If a taxpayer wishes to change its NAICS code and applicable tax rate, it must do so through written application to the Department of Taxation. The department has 60 days to accept or reject the request, and if no response is received, the request is deemed granted.⁹⁰

H. Modified Business Tax Credit

Before the commerce tax, substantial state revenue was generated by the modified business tax (MBT), a quarterly payroll-based tax on businesses paying wages to employees in Nevada. Before July 1, 2015, the tax was imposed on wages paid exceeding \$85,000 in each calendar quarter at a rate of 1.17 percent.⁹¹ SB 483, which implemented the commerce tax, also amended the MBT to increase the rate to 1.475 percent on wages paid exceeding \$50,000 per quarter.⁹² However, business entities subject to the commerce tax are permitted a credit against their MBT liability of up to 50 percent of the total commerce tax liability paid by an employer in the preceding taxable year.⁹³ The credit is available for use in the four calendar quarters following payment of the commerce tax, but it cannot exceed the amount of MBT liability.⁹⁴ No refund of unused MBT credit is allowed, and the credit cannot be carried forward past the four calendar quarters following payment of the commerce tax.⁹⁵

Many affiliated businesses use a common paymaster, rather than processing payroll separately for each affiliated entity. In these situations, the business entities in the affiliated group that generate Nevada gross revenue subject to the commerce tax may not be the same business entities filing and paying the MBT. Recognizing that, the regulations provide that an employer may apply and be designated by the department as a "payroll provider" if it is a member of an affiliated group for which it provides payroll services for employees providing services for one or more affiliated members.⁹⁶ Once it is designated as the payroll provider, that business entity is permitted to claim the MBT credit based on the amount of commerce tax paid by any affiliated business entity for which it provides payroll services.⁹⁷ Thus, for MBT purposes, the payroll provider is treated as having earned the commerce tax credit for all of its affiliated members and

may apply up to 50 percent of the total commerce tax credit paid against its subsequent MBT liability. Businesses employing a common paymaster should seek to have it designated as a payroll provider for MBT purposes.

IV. Conclusion

It has been an eventful several years in Nevada with the passage of a new tax regime and the issuance of final regulations, forms, instructions, and other guidance from the Department of Taxation. But with numerous areas of uncertainty regarding the commerce tax, one hopes further department guidance will be forthcoming to provide additional clarity.

FOOTNOTES

Nev. Rev. Stat. section 363C.200 (2016); and Associated Press, "Nevada Assembly Passes the State's Largest One-Time Tax Increase," *The Wall Street Journal*, June 1, 2015.

Nev. Rev. Stat. section 363C.080 (2016).

Nevada Margin Tax for Public Schools Initiative, Question 3, State of Nevada Statutory Ballot Measure (Nov. 4, 2014).

Nev. Rev. Stat. section 363C.200(1) (2016).

See Filing Requirement FAQs, Nevada Department of Taxation Website, *available at* <http://bit.ly/2f0laxG>. See *also*, Nevada Tax Commission Adopted Regs. R123-15, section 14 (2016).

Id.; Nevada Tax Commission Adopted Regs. R123-15, section 17(1)-(2) (2016).

Nev. Rev. Stat. section 363C.080 (2016).

Nev. Rev. Stat. section 363C.140 (2016).

Nevada Tax Commission Proposed Regs. R123-15, section 80(1) (Feb. 17, 2016); Nevada Tax Commission Adopted Regs. R123-15, section 79(1) (June 28, 2016).

Nevada Tax Commission Adopted Regs. R123-15, section 79(1) (emphasis added).

Nev. Rev. Stat. section 363C.200(2) (2016). While the 45th day after June 30 is technically August 14, the department appears to adopt August 15 as the de facto due date; see the commerce tax instructions issued by the department as of June 16, 2016, which states "The Commerce Tax return can be filed between July 1, 2016, and August 15, 2016." The Nevada commerce tax also states on its online home page: "This year, the first return is due August 15, 2016."

Id. at (4).

Nev. Rev. Stat. section 360.419 (2016). The department has indicated that the waiver of interest or penalty extends to the commerce tax return on both the commerce tax instructions sheet and on its online FAQ page for returns and payments.

See Return and Payment FAQs, Nevada Department of Taxation Website, *available at* <http://bit.ly/2egT4MI>.

Nev. Rev. Stat. section 363C.020(1) (2016).

Nev. Rev. Stat. section 363C.200(1) (2016).

Nev. Rev. Stat. section 363C.020(2) (2016).

Nev. Rev. Stat. section 363C.020(2)(m) (2016). The term "RIC" means an investment company under the Investment Company Act of 1940, 15 U.S.C. sections 80a-1 et seq.

See e.g., Nevada Tax Commission Adopted Regs. R123-15, sections 14(2)(j), (4)(b); 22(1); 23(3); 24(4); 25(1).

Nevada Tax Commission Adopted Regs. R123-15, section 15.

Nevada Tax Commission Adopted Regs. R123-15, section 14(2)(i) & (4)(a).

Nev. Rev. Stat. section 363C.020(2)(m) (2016).

Id.; IRC section 851; 15 U.S.C. 80 sections 80a-1 et seq.

Nev. Rev. Stat. section 363C.093(1)(a)-(c) (2016).

Id. at (1)(b)-(2)(a).

Id. at (1)(b).

Id. at (b).

Nevada Tax Commission Adopted Regs. R123-15, section 14(1) (2016).

See Nev. Rev. Stat. section 363C.200(1)-(2) (2016).

Nev. Rev. Stat. section 363C.015 (2016).

Nev. Rev. Stat. sections 363C.020, 363C.035 (2016).

Nevada Tax Commission Adopted Regs. R123-15, section 16(1)-(22) (2016).

Nevada Tax Commission Adopted Regs. R123-15, section 16(1)-(22) (2016).

The commerce tax nexus questionnaire is available from the Nevada tax department.

Nevada Tax Commission Adopted Regs. R123-15, section 14(1) (2016).

Nev. Rev. Stat. section 363C.055 (2016).

Nev. Rev. Stat. section 363C.045(1) (2016).

Id. at (2).

Nev. Rev. Stat. section 363C.140 (2016).

Nev. Rev. Stat. section 363C.045(3)(b)-(c), (e).

Id. at (3)(a).

Id. at (3)(d).

Id. at (3)(e)&(f).

Financial Accounting Standards Board Emerging Issue Task Force Issue 99-19, "Reporting Revenue Gross as Principal versus Net as an Agent."

Nev. Rev. Stat. section 363C.140 (2016).

ASC 605-50-25-1, -2, and ASC 605-50-45-12, -13.

IRC section 61 (2016); see also Rev. Rul. 73-161, 1973-1 CB 366 (Jan. 1973) (treating damages received for construction work as ordinary income replacing rental income); and *Benton v. Commissioner*, T.C. Memo 1962-292 (December 1962) (characterizing taxpayer's litigation settlement proceeds as ordinary income instead of long-term capital gain).

Nev. Rev. Stat. section 363C.020(1) (2016).

Nev. Rev. Stat. section 363C.210(1) (2016).

Id. at (1)(b), (e)-(k), (x)-(y).

Id. at (p).

Nev. Rev. Stat. section 363C.065 (2016).

Id. at (l).

Nev. Rev. Stat. section 363C.070(1)(a)-(b) (2016).

Id. at (c)-(d).

Id. at (f).

Id.

Nev. Rev. Stat. section 363C.210(1)(o).

Nev. Rev. Stat. section 363C.030

Nevada Commerce Tax Instructions, p. 2 (as of June 16, 2016).

Id. at p. 3.

Nev. Rev. Stat. section 363C.210(q)

I.R.C. section 1231 (2016).

I.R.C. section 1221 (2016).

Nev. Rev. Stat. section 363C.210(1)(c); 463.370 (2016).

Nev. Rev. Stat. section 363C.140 (2016).

Nev. Rev. Stat. section 463.370(4) (2016).

Nev. Rev. Stat. section 363C.210(1)(c); 463.370 (2016).

The Nevada Commerce Tax Form TXR-030.01 (revised August 9, 2016).

Nevada Commerce Tax Instructions, p. 2 (as of June 16, 2016).

Nev. Rev. Stat. section 363C.055 (2016).

Nev. Rev. Stat. section 363C.220(1)(c)-(d) (2016).

Id. at (1)(a)-(b).

Id. at (1)(f).

Id.

Id. at (1)(e).

Id. at (1)(g).

Id.

Id. at (2).

Nevada Tax Commission Adopted Regs. R123-15, sections 23-75 (2016).

Nev. Rev. Stat. section 363C.220(1)(f).

Nevada Commerce Tax Instructions, p. 3 (as of June 16, 2016).

Nev. Rev. Stat. section 363C.200 (2016).

Nev. Rev. Stat. section 363C.300 (2016).

Nev. Rev. Stat. sections 363C.310-.560 (2016).

Id.

Nev. Rev. Stat. section 363C.300 (2016).

Nevada Tax Commission Adopted Regs. R123-15, section 78(2)(b) (2016).

Id. at (2)(a).

Id. at (3)-(4).

Nev. Rev. Stat. section 363B.110(1) (effective until July 1, 2015).

Nev. Rev. Stat. section 363B.110(1) (effective July 1, 2015).

Id. at (4).

Id.

Id.

Nevada Tax Commission Adopted Regs. R123-15, section 11(2)(b) (2016). To be designated a payroll provider, the employer provided payroll services must be a member of an affiliated group that:

- provides payroll services for one or more members of the affiliated group;
- pays wages to employees who provide services for one or more members of the affiliated group; and
- pays the MBT on wages paid to those employees.

For the payroll provider to claim the credit, it must be determined that each member of the affiliated group for which the payroll provider pays the MBT would have its own MBT liability if the persons who provide the services for that member were treated as employees of that member rather than as employees of the employer.

Id. at (4).

END FOOTNOTES

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