

DEATH OF THE BRIGHT LINE NEXUS TEST IN NEW HAMPSHIRE

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At the core of state taxation is the principle of nexus. Nexus describes the amount and degree of business activity that must be present before a state can tax the income of an entity or individual. If a business or individual has sufficient contacts in a particular state (i.e. nexus), then the taxpayer must pay and collect or remit taxes in that state. Taxing organizations or individuals outside this limitation is unconstitutional. The amount of activity or connection that is necessary to create nexus is defined by state statute, case law and/or regulation and, consequently, nexus tends to vary from state to state. This makes assessing whether or not nexus exists for a particular taxpayer a challenge because tax practitioners often find themselves chasing a moving target due to developing case law, changing statutes and recent trends of moving away from bright line nexus tests. Assessing whether an out-of-state business is subject to the New Hampshire Business Profits Tax ("BPT") can be particularly challenging.

The standard for BPT nexus, which is relatively new (effective July 1, 2007) is an unformulated "substantial economic presence" test. The BPT applies to any business organization, organized for gain or profit, and which carries on "business activity" within the state which is defined as "a substantial economic presence evidenced by a purposeful direction of business toward the state examined in light of the frequency, quantity, and systematic nature of a business organization's economic contacts with New Hampshire." **RSA § 77-A:1, XII**. With such a broad standard, we ask whether there are any bright line tests that tax practitioners can look to when assessing nexus in New Hampshire?

Our checklist begins with what New Hampshire recognizes as activities which are exempt from the BPT – sales and solicitation activities. **N.H. Administrative Rule, Rev. 304.01(b)** subjects an

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out-of-state business to the BPT if “its in-state activities exceed the protection of P.L. 86-272”. P.L. 86-272 (codified at 15 USC §§ 381-384) prohibits states from imposing a tax measured by net income on companies whose only presence in the state consists of “solicitation” of orders for tangible personal property approved and sent in from out-of-state. The U.S. Supreme Court later determined that the term “solicitation” encompasses requests for purchases and activities entirely ancillary to such requests. See Wisconsin Department of Revenue v. William Wrigley, Jr. Company, 112 S. Ct. 2447 (1992). There is no comparable Federal statute that protects businesses that solicit orders for services.

In *Vector Marketing Corporation v. New Hampshire Dept. of Revenue Admin.*, 2008 WL 612251 (N.H. 2008), the court alluded to the fact that “[P.L. 86-272 is] a guidepost by which [taxpayers] may determine whether they are subject to the BPT.” *Rev. 304.01(d)(2)* provides examples of the kind of solicitation activities that New Hampshire considers within P.L. 86-272: advertising, checking customers’ inventories without a charge for purposes of completing a replacement order, maintaining temporary samples or displays for things like trade shows, and under some circumstances, a sales person maintaining a home office.

Beyond sales activities covered by P.L. 86-272 as exemplified in *Rev. 304.01(d)(2)*, substantial economic presence allows for an expansive taxing arm. See, i.e., Vector, 2008 WL 612251 (concluding that “[i]f [P.L. 86-272] does not immunize [the taxpayer] from state taxation, then the DRA will, according to Rule 304.01, subject them to the BPT.”).

The classic bright line test of physical presence certainly applies to the BPT. Foreign corporations which employ capital, own or lease property, or maintain an office within the state create a substantial economic presence.

What about the New Hampshire Secretary of State’s requirement that foreign businesses register to do business in the state? Is the registration a bright line test to assess nexus? Using this registration requirement alone as a benchmark could be problematic for two reasons. First, the statute indicates that relying on this requirement for assessing tax liability is a bad idea. See RSA 293-A:15.01(d) (“[n]othing in this section shall be construed so as to preclude a determination that a foreign corporation is carrying on business activity within this state within the meaning of the [BPT statute]).” Second, there are certain activities that the corporations statute considers exempt from registration that the DRA would consider taxing. For example, according to the statute, activities like maintaining bank accounts, holding meetings of the

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board of directors or shareholders, collecting debts, or simply the passive ownership of real or personal property, are activities which may not require a foreign business to register to do business in New Hampshire. These activities, however, may be sufficient enough to qualify as a substantial economic presence.

Beyond physical presence and registration requirements, the closest thing to a checklist that tax practitioners can turn to is provided for in [Rev. 304.01\(d\)](#). This rule includes a list of activities that the DRA considers to be sufficient to subject a foreign business to the BPT. The list is as expansive as it is random and includes activities like the following:

- Using a meeting place for directors, officers or employees;
- Handling financial matters such as collecting current or delinquent accounts and accepting customer deposits;
- Using mobile stores such as a truck with a driver salesman making sales from the vehicle;
- Installing merchandise or equipment or supervising such work;
- Conducting training programs, seminars or lectures for personnel other than personnel involved only in the solicitation of sales; investigating, handling, or otherwise assisting in resolving customer complaints;
- Approving or accepting customer orders as well as accepting deposits from customers;
- Providing any kind of technical assistance or services, such as engineering assistance or services;
- Picking up or replacing damaged or returned property;
- Repossessing property; and
- Providing shipping information and coordinating deliveries.

There is of course a “catch all” in the rules which includes any activities which are not entirely ancillary to the solicitation of sales orders. [See Rev. 304.01\(d\)\(1\)\(s\)](#).

What is clear from the enumerated list of activities is the notion that the New Hampshire “substantial economic presence” standard goes beyond bright line tests. Without these well-defined



standards, tax practitioners and clients must continue to use their best judgment and as a result, the bounds of the BPT nexus standard will be tested. If you or your clients have concerns related to whether there has been nexus with a state, or if you are unclear whether certain activities fall within substantial economic presence, we recommend that you consider seeking legal expertise. There may be challenges available through developing case law and with respect to cases in which nexus has been established, there may be Voluntary Disclosure Programs available to your client.

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