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BOARD OF EQUALIZATION

STATE OF CALIFORNIA

In the Matter of the Appeal of:	**HEARING SUMMARY**
	CORPORATION FRANCHISE TAX APPEAL
CRAIGSLIST, INC.	Case No.'s 725838, 843070

Year	Refund	Proposed Assessment	Penalty
2007	$789,799[1]	$274,427[2]	$43,005

Representing the Parties:

For Appellant: Robert L. Mahon, Perkins Coie LLP

For Franchise Tax Board: Katie M. Frank, Tax Counsel III

[1] This is the approximate refund (or credit) amount appellant would receive if it prevails on appeal.

[2] This is the refund amount claimed. If the FTB's actions are sustained, appellant will owe the additional tax and penalty set forth above, which were set forth in a Notice of Action (NOA) dated July 18, 2014. Appellant is not contesting the underlying adjustment to income set forth in the NOA and agrees that, if its refund claim is denied, it would be subject to the accuracy-related penalty set forth above ($43,005) for that income adjustment. On the other hand, the parties agree that, if appellant prevails with respect to the apportionment arguments raised in its refund claim and in this appeal, the accuracy-related penalty would be removed (because there would no longer be an underpayment) and the amount of tax arising from the adjustments in the NOA would be reduced from $274,427 to $177,469, which would reduce the refund amount from the $789,799 amount which was claimed to approximately $612,331 (rounded).

NOT TO BE CITED AS PRECEDENT - Document prepared for Board review. It does not represent the Board's decision or opinion.

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QUESTION: Whether, in determining the percentage of appellant's business income that is apportioned to California, sales attributable to certain states and the District of Columbia[3] should be excluded from appellant's sales factor on the ground that appellant was not taxable in such states pursuant to Revenue and Taxation Code (R&TC) section 25122.

HEARING SUMMARY

Section 40 Appeal

This appeal involves an amount in controversy that is $500,000 or more and thus is covered by Revenue and Taxation Code section 40, as explained below in Staff Comments.

Background

Appellant allows users to post classified advertisements on its website. Appellant charges a fee for a relatively small portion of those advertisements consisting of job postings in certain areas, brokered apartment rental listings in New York City, and therapeutic service advertisements. (Appeal Letter, p. 2; Resp. Op. Br., p. 1.)[4]

Appellant filed an original return for 2007 that assigned, or sourced, its gross receipts from the advertisements pursuant to the general sourcing rule at that time, which assigned the receipts to the state with the greatest income-producing activity. This resulted in all or substantially all of its gross receipts being assigned to California. (Resp. Op. Br., p. 1; Pre-hearing Conf.)

On July 28, 2009, appellant petitioned the FTB to use a special apportionment formula pursuant to R&TC section 25137. In a letter dated June 29, 2010 (Determination Letter), the Franchise Tax Board (FTB or respondent) partially granted appellant's request to use an alternative apportionment formula for tax years from 2007 to 2010. Pursuant to the alternative formula, the FTB allowed appellant to source its gross receipts from advertising on a "market basis." Specifically, the FTB allowed appellant to source its gross receipts to the state where the advertisement generating the

[3] The relevant jurisdictions are the District of Columbia, Illinois, Massachusetts, New York, Oregon, and Washington, and are referred to by the parties and herein as the States at Issue.

[4] Unless otherwise noted, references to briefing refer to briefing in Case No. 725838, which includes the most recent briefing. After the filing of appellant's appeal letter for Case No. 843070, the two cases were consolidated with Case No. 725838 acting as the lead case in the consolidated appeals.

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income was targeted. For example, income from a job posting for San Francisco would be assigned to California. However, the FTB provided that appellant's receipts would be subject to "the throw-out rule," stating as follows:

> There is a concern regarding income earned in states and countries where the taxpayer is not taxable, i.e., "nowhere" income. For that reason, the throw-out rule will be utilized meaning that gross receipts sourced to a location in which the taxpayer is not taxable, as defined in RTC section 25122, will be excluded from the sales factor calculation. This will more accurately represent the taxpayer's business in California. Based on [the] Appeal of Dresser Industries, 83-SBE-118, June 29, 1982, aff'd Oct. 26, 1983, United States constitutional standards for nexus will be used to determine whether a foreign country or state has jurisdiction to tax. Taxpayer will bear the burden of proving nexus in all cases.

(Appeal Letter, pp. 2 – 3 and attachment [June 29, 2010 letter from respondent]; Resp. Op. Br., p. 1; Pre-hearing Conf.)

Thus, under the alternative apportionment formula, the percentage of appellant's sales that were sourced to California would not be reduced by a sale that was sourced to a state in which appellant was not taxable. Put differently, sales that arose in a state where appellant was not taxable would be "thrown out" of the sales factor calculation. This would have the effect of reducing the percentage of business income (or loss) that would otherwise, but for the throw-out rule, be apportioned to California.[5]

On September 9, 2011, appellant filed an amended California tax return for 2007 claiming a $789,799 refund applying the alternative apportionment methodology based on its view of where it was taxable pursuant to R&TC section 25122. The amended tax return included sales from the States at Issue in the denominator of its sales factor (which reflects sales everywhere), which reduced appellant's California sales factor. The amended tax return thus apparently reflected appellant's view that it was taxable in the States at Issue based on having more than $500,000 in sales in those states.[6]

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[5] Consider an example in which appellant sold only three advertisements, each for $1, with one targeted to California, one targeted to state "T" in which appellant was taxable, and one targeted to state "N" in which appellant was not taxable. Appellant's sales factor would be 50 percent based on $1 of California sales divided by sales everywhere of $2 ($1 of California sales plus $1 of state T sales). The sales in state N would be disregarded or "thrown out," and therefore would not reduce appellant's sales factor. In contrast, if the sales in state N had not been thrown out, the sales factor would have been 33.33 percent based on $1 of California sales divided by sales everywhere of $3.

[6] The parties agree that appellant had more than $500,000 in sales in each of the States at Issue.

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Respondent audited the amended tax return and determined that appellant was not taxable in the States at Issue. On this basis, respondent determined that the sales sourced to the States at Issue should be thrown out of the sales factor calculation. Accordingly, respondent denied the claim for refund. Appellant subsequently filed a timely appeal from this refund denial (Case No. 725838).

As noted in footnote 2, the FTB also determined that appellant owed additional tax as a result of an unrelated income adjustment and, following an audit and protest, the FTB issued a NOA reflecting $728,341 in additional tax plus an accuracy related penalty of $133,788.25. Appellant also appealed this action (Case No. 843070). The parties do not dispute the change to income made in the NOA. However, the amount of California tax on that income will vary depending on the resolution of the apportionment issue raised in this appeal.

The two appeals were then consolidated to form this consolidated appeal.

Applicable Law[7]

Apportionment of Business Income

Article 2 of Chapter 17 of the Corporation Tax Law sets forth the provisions of the Uniform Division of Income for Tax Purposes Act (UDITPA) as adopted by California and set forth in R&TC sections 25120 through 25141. For the year at issue (2007), California's version of UDITPA generally required that the taxpayer's business income be apportioned by a four-factor formula composed of a property factor, a payroll factor, and a double-weighted sales factor. (Rev. & Tax. Code, § 25128.) The numerators of the respective factors represent the taxpayer's property, payroll, and sales in California, while the denominators represent the taxpayer's property, payroll, and sales everywhere. (Rev. & Tax. Code, §§ 25129, 25132 & 25134.)

R&TC section 25136 addresses how to assign or source sales of other than tangible personal property for purposes of determining whether the sales are inside California. If sales are assigned to California, such sales are included in the numerator of the sales factor as well as the denominator, which includes sales everywhere. However, if sales are assigned outside of California, the sales are excluded from the numerator of the sales factor and only included in the denominator. As

[7] Applicable law is provided prior to contentions in order to assist in reviewing the legal issues raised in the contentions.

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a result, the assignment of sales outside of California generally reduces the percentage of unitary business income of a multistate business that would be taxable by California (or reduces any business loss that is apportioned to California where the business has a unitary business loss).

Determining Whether a Taxpayer is Taxable in a Jurisdiction

As noted above, the Determination Letter provides that, under the special apportionment methodology approved by the FTB, the throw-out rule would be applied to exclude appellant's sales that were not taxable pursuant to R&TC section 25122. Under that provision, as relevant in this appeal, a taxpayer is "taxable" in a state if "that state has jurisdiction to subject the taxpayer to a net income tax *regardless of whether, in fact, the state does or does not [subject the taxpayer to a net income tax]*." (Rev. & Tax. Code, § 25122 [emphasis added].) Whether the state has "jurisdiction to subject the taxpayer to a net income tax" is determined by examining whether the taxpayer could constitutionally be subject to a net income tax by the state. (Cal. Code Regs, tit.18, § 25122, subd. (c); *Appeal of Dresser Industries, Inc.*, 82-SBE-307, June 29, 1982, petition for rehearing denied, 83-SBE-118, Oct. 26, 1983 (*Dresser Industries*).) Specifically, California Code of Regulations, title 18, section (Regulation) 25122, subdivision (c), states that jurisdiction to tax is present "if the taxpayer's business activity is sufficient to give the state jurisdiction to impose a net income tax by reason of such business activity under the Constitution and statutes of the United States."

Under R&TC section 25135, shipments of tangible personal property from California to a state in which the taxpayer is not "taxable" are "thrown back" to California in determining the sales factor. Specifically, the sales are included in the numerator of the California sales factor, and would thereby increase the taxpayer's California sales factor. Like the throw-out rule, the throwback rule determines whether the taxpayer is "taxable" by reference to R&TC section 25122 and the regulations thereunder.

Early in 2009, the California Legislature enacted amendments to the Revenue and Taxation Code. (See Stats. 2009-2010, 3rd Ex. Sess., c. 17 (S.B.15), § 7, eff. Feb. 20, 2009.) Among other amendments, the Legislature amended R&TC section 23101 to provide a number of bright line

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rules that will establish that a business is "doing business" in California for purposes of taxation.[8] One of these rules is that a business generally will be considered to be "doing business" in California and therefore subject to California taxation if it has more than $500,000 in California sales. The Legislature provided that the amendments are only effective for tax years beginning on or after January 1, 2011.

In FTB Chief Counsel Ruling 2012-03,[9] the FTB states that, for tax years beginning on or after January 1, 2011, a taxpayer would be considered to be taxable in another state, for purposes of the throwback rule, if the taxpayer's activities in that state exceeded any of the conditions set forth in R&TC section 23101, as amended effective January 1, 2011, for taxation by California law. Thus, for example, for tax years beginning on or after January 1, 2011, if the taxpayer had more than $500,000 of sales in the other state, it would be considered taxable in that state under R&TC section 25122, just as a taxpayer making sales into California would be considered taxable under R&TC section 23101, as amended.

In FTB Technical Advice Memorandum (TAM) 2012-01,[10] the FTB states that, for tax years beginning prior to January 1, 2011, it requires that a taxpayer have a physical presence in a jurisdiction in order to be considered taxable in that jurisdiction under R&TC section 25122. The TAM cites for support the *Appeal of John H. Grace*, 80-SBE-115, decided October 28, 1980 (*Grace*), *Dresser Industries, supra*, and nonprecedential decisions of the Board of Equalization.[11] The TAM further explains as follows:

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[8] In addition, among other things, the amendments generally provide for market-based sourcing of receipts from intangibles (rather than sourcing based on cost of performance). Also, the amendments allow an election to use single-factor apportionment based on the sales factor (rather than based on sales, property, and payroll factors).

[9] The FTB's website states that Chief Counsel Rulings are taxpayer specific and may not be cited as precedent. This ruling is described to provide legal background.

[10] The FTB's website states that the FTB's TAMs are informational only and may not be cited as precedent. This TAM is described to provide legal background.

[11] *Grace* and *Dresser Industries* are discussed below.

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> By enacting legislation providing that a taxpayer is doing business in California where a taxpayer's only contact with this state are sales exceeding $500,000, California's Legislature determined for the first time that substantial economic presence meets U.S. Constitutional standards under California law. In enacting this statutory provision, California's Legislature determined that under California law, physical presence is no longer required in order for the state to subject a business to tax. However, the amendment to section 23101 specifically provides that the newly enacted circumstances applied only to taxable years beginning on or after January 1, 2011.
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> Accordingly, for taxable years beginning before January 1, 2011, California law required physical presence (either directly or through agents or independent contractors) to establish substantial nexus under the commerce clause. Thus, for throw back purposes in taxable years beginning before January 1, 2011, a taxpayer must demonstrate physical presence (either directly or through agents or independent contractors) in the destination state to establish that it is subject to taxation in that state and avoid the application of the throwback rule under section 25122 and Regulation 25122(c).

Appeal of John H. Grace Company, 80-SBE-115, Oct. 28, 1980 (*Grace*)

In *Grace*, the taxpayer was an Illinois corporation that leased railroad cars to industrial companies that then arranged for railroads to ship their products on the cars. The Board stated that the taxpayer "conducts no business in California, has no agents in California, does not solicit leasing customers in California, and does not have any leasing customers in this state." The Board further stated that the taxpayer's only contact with California was that some of the leased railroad cars passed through or into California. The FTB sought to tax the taxpayer, arguing that the railroad cars provided sufficient nexus to subject the taxpayer to income tax. Appellant argued both that it was not taxable under the relevant statutes and, in the alternative, that the imposition of such a tax would violate the United States Constitution.

The Board first noted that Section 3.5 of Article III of the California Constitution prohibits it from ruling that statutory provisions are unenforceable or invalid under the United States Constitution. The Board further noted that it has a well-established policy of abstention from deciding constitutional questions in an appeal involving proposed assessments of tax. The Board explained that the policy "is based upon the absence of any specific statutory authority which would allow the [FTB] to obtain judicial review of an adverse decision in a case of this type, and our belief that such review should be available for questions of constitutional importance."

However, the Board added that ". . . the fact we cannot decide the constitutional issue

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does not mean we can ignore existing constitutional limitations when interpreting the applicable statutes." The Board stated that, "since the Legislature intended the taxing statutes to reach only to the limits permitted by the Constitution, our application of the statutes to the facts presented is restricted by existing constitutional limitations."

The FTB argued that the railroad cars were used in California to generate income, causing the taxpayer's income from the cars to be "derived from sources within this state" under the statute. The Board stated that the FTB relied upon "the economic presence theory posited by the court in *American Refrigerator Transit Co. v. State Tax Commission*, 238 ORE. 340 . . . (1964) [*American Refrigerator*]." The taxpayer countered that its leasing business was conducted outside of California and that the presence of its railroad cars in California was not sufficient to subject it to taxation, citing various cases.

The Board found the cases cited by the parties to be "of little assistance[,]" and stated that the Oregon case (*American Refrigerator*) cited by the FTB had been criticized as "a carte blanche for aggressive state tax administrators." The Board stated that "[i]n the 16 years since the Oregon case was decided, no United States Supreme Court case has adopted the economic presence theory, and one case has suggested that some physical presence on behalf of the taxpayer is required." (Citing *National Bellas Hess, Inc. v. Department of Revenue* (1967) 386 U.S. 753 [*Hess*].) Accordingly, the Board stated that it "decline[d] to follow the lead of the Oregon Supreme Court by accepting mere economic presence as constituting sufficient statutory nexus to support the corporate income tax."

The Board summarized the nexus requirements by stating as follows:

> . . . no barrier exists to prevent the taxation of income derived wholly in furtherance of interstate commerce so long as the corporation's in-state business activities have some regular, systematic and substantial connection with, *and physical presence within*, the taxing state. [emphasis added by Appeals Division staff] The controlling test which the United States Supreme Court has repeatedly noted as underlying minimally sufficient nexus is whether by the practical operation of the tax the state has exerted its taxing power in relation to opportunities which it has given, to protection which it has afforded, to benefits which it has conferred by the fact of being an orderly, civilized society. [citing cases]

Applying the foregoing principles, the Board found that appellant had no "activities" within California as contemplated by the statute. The Board further found that the railcars were under

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control of the lessees so that the presence of any of the cars in California was "entirely fortuitous" and the income did not arise from a source in California. Finding that the taxpayer had insufficient connection with California for the state to legitimately impose its income tax, the Board reversed the action of the FTB.

Appeal of Dresser Industries, Inc. (*Dresser Industries*)[12]

In *Dresser Industries*, the Board considered whether the FTB properly applied the throwback rule to products that were shipped from California to foreign countries. During the years at issue, the taxpayer, through subsidiaries, sold pumps in foreign countries, and shipped them from California. In countries where the activities of the sales subsidiaries were limited to taking sales orders, respondent threw back the sales "on the theory that if [Public Law] 86-272 were applicable to foreign commerce, these countries would not have jurisdiction to tax appellant's income."[13]

In its initial decision, dated June 29, 1982 (82-SBE-307), the Board stated that "[i]t appears that respondent's only reason for reaching this conclusion is its view that uniformity in the interpretation of UDITPA's statutes and regulations requires the application of P.L. 86-272's jurisdictional limitations to the taxation of income . . . ." Quoting R&TC section 25122, subdivision (b), the Board stated that, since appellant was not actually subject to tax, the Board's "sole concern [was] whether any of those countries had jurisdiction to subject appellant to a net income tax." Quoting Regulation 25122, subdivision (c), the Board observed that both parties agreed that United States jurisdictional standards should be used to determine whether a foreign country had jurisdiction to tax the taxpayer. However, the taxpayer argued that P.L. 86-272 was irrelevant because it does not apply to foreign commerce, while the FTB argued that Regulation 25122 "require[d] not only that the same uniform standards be applied to determine both a sister state's and foreign country's jurisdiction to tax, but also that the jurisdictional limitations of P.L. 86-272 be applied – regardless of whether the taxpayer's business activities are in interstate or foreign commerce."

Reviewing the arguments, the Board stated that "[t]he notion that regulation 25122

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[12] 82-SBE-307, June 29, 1982, petition for rehearing denied, 83-SBE-118, Oct. 26, 1983.

[13] P.L. 86-272 is a federal law that, if certain conditions are met, provides a safe harbor from state taxation based on the mere solicitation of sales within a state.

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eliminates the basic distinction between interstate and foreign commerce is supported neither by the language of the regulation nor by the principle of uniformity . . . ." The Board further stated that, if California's jurisdiction to tax was limited in this way, "it would appear to . . . conflict with the rule that the reach of the California franchise tax is coextensive with the state's constitutional power to tax." The Board explained that "[t]here is no lack of uniformity simply because different jurisdictional standards are applied to different classes of commerce, so long as those standards are applied consistently to both foreign and domestic 'states'." The Board rejected the argument that the FTB's interpretation of Regulation 25122 should be followed in order for California to be in conformity with other states, stating that the FTB had not cited authority from such states in support of its interpretation. Accordingly, the Board determined that the taxpayer was "taxable" in the countries at issue, and reversed the FTB's determination to throw back the sales at issue.

The FTB filed a petition for rehearing, which the Board denied in an Opinion on Petition for Rehearing dated October 26, 1983 (83-SBE-118). In its petition for rehearing, the FTB contended that, even if P.L. 86-272 was not applicable, "constitutional jurisdiction to tax the appellant was lacking because of [the Board's] factual determination that appellant 'did not do business' in the countries in question." The Board stated that the referenced factual determination was merely taken from the statements of facts of the parties. The Board noted the relevant constitutional nexus standards and stated that the FTB contended that there was no nexus because the taxpayer itself, "as a separate corporate entity, did not do business in the foreign countries . . . , and because the acts of the sales subsidiaries . . . cannot be ascribed to appellant for nexus purposes." The Board observed that the FTB relied "in large part" on *Hess* . . . and [*Grace*], decided . . . on October 28, 1980.

The Board found that *Hess* and *Grace* were distinguishable because the record before the Board "reveal[ed] a regular and systematic pattern of local sales solicitation on appellant's behalf in the foreign countries in question." Citing the decision of the U.S. Supreme Court in *Scripto, Inc. v. Carson* (1960) 362 U.S. 207 (a sales tax case), the Board found that the fact the activities were conducted by subsidiaries was "without constitutional significance for nexus purposes." Summarizing, the Board stated that ". . . appellant's exploitation of foreign markets for the purpose of earning income from sales of its pumps, together with the benefits and protections which the market states provide

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during the process, is sufficient to satisfy the requisites of due process . . ." even if conducted through subsidiaries.

Appeal of Huffy Corp. (Huffy)[14]

In *Huffy*, the taxpayer argued that certain members of its unitary group were not taxable by California as they either lacked a nexus with California or taxation was prohibited by P.L. 86-272. The Board held that, for tax years beginning on or after the date of the opinion, it would overturn its prior *Finnigan* precedents (discussed below) and determine whether there was sufficient nexus to make a corporation taxable by considering whether the specific corporation was taxable rather than considering whether the unitary group was taxable. In doing so, the Board re-applied a rule that was previously set forth in the *Appeal of Joyce, Inc.*, 66-SBE-069, decided on November 23, 1966 (*Joyce*).

The Board noted that, in *Joyce*, it excluded from the sales factor inbound sales of a seller corporation that was not subject California tax due to P.L. 86-272, even though other members of the unitary group were subject to California tax. However, approximately 22 years later, it reached a contrary decision in the *Appeal of Finnigan Corp*., 88-SBE-022, decided on August 25, 1988, and the *Appeal of Finnigan Corp*., 88-SBE-022A, decided on January 24, 1990. In those decisions, the Board determined that the sales of a seller of tangible personal property to customers in other states, which sales could not be taxed in those states due to P.L. 86-272, should not be thrown back to California for inclusion in the California sales factor. The Board reasoned that, although the subsidiary selling the goods was not taxable in the other state, the unitary group was taxable in the destination state. Therefore, in these prior *Finnigan* decisions, the Board held that the sales should not be thrown back to California, as the taxpayer (referring to the unitary group) was taxable in the destination states.

In *Huffy*, the Board abandoned the *Finnigan* rule and re-adopted – on a prospective basis only – the rule it had set forth in *Joyce*. Thus, the Board held that the determination of whether a corporation was taxable would be made on the basis of the corporation in question, rather than on the basis of whether any members of the corporation's unitary business were taxable.

In *Huffy*, the Board stated that "a key factor" in its decision to overturn the *Finnigan* rule

[14] 99-SBE-022, April 22, 1999, petition for rehearing denied, 99-SBE-005-A, September 1, 1999.

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was the Board's "unfulfilled expectation" that most other taxing authorities would implement the same decision, as the majority of states did not follow the rule set forth in the *Finnigan* decisions. Given the lack of uniformity, the Board noted that the application of the *Finnigan* rule created a risk of income not being subject to tax in certain scenarios and the risk of double taxation in other scenarios. The Board noted that adoption of the *Joyce* rule would avoid these scenarios. The Board observed that its prior interpretation was inconsistent with nearly all other states and stated that it was "mindful of [R&TC] section 25138, which states that [UDITPA] shall be 'so construed as to effectuate its general purpose to make uniform the laws of the states which enact it.'"

While the Board found that a change in the rule was advisable, it noted that the FTB and the appellant, as well as other taxpayers, had "relied on the *Finnigan* decisions for roughly the past eight years." It observed that a prospective application of the new rule had a number of advantages as it allowed taxpayers to make informed decisions, did not penalize or provide a windfall to taxpayers based on standards taking effect after their tax planning, and it promoted stability. It also noted that California cases have applied the reasoning of *Chevron v. Huson* (1971) 404 U.S. 97 (*Chevron*).

The Board noted that *Chevron* set forth three factors, each of which supported its determination to make its ruling on a prospective basis. First, its decision over-ruled past precedent which taxpayers had relied upon. Second, considering the history of the rule and its purpose and effect, the prior rule had unintended effects and did not result in uniformity. Most important was the fact that tax planners had relied on the prior rule. Third, the Board found that the retroactive application of its new rule would cause injustice and inequity because it would risk penalizing taxpayers "for following the law in effect at the time their transactions were conducted." The Board therefore determined that the new rule should be applied only on a prospective basis to tax years beginning on or after the date of its opinion, with the result that the action of the FTB was sustained.

Both parties filed a petition for rehearing. Appellant argued that the Board's conclusion was correct but that the Board should not have limited its decision to prospective tax years. As an alternative, appellant argued that the Board's decision to adopt the *Joyce* rule for the treatment of inbound transactions was not necessarily inconsistent with the continued application of the *Finnigan* rule for outbound transactions. The FTB offered technical amendments to the opinion.

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In its Opinion on Petitions for Rehearing, *Appeal of Huffy Corporation*, 99-SBE-005-A, decided September 1, 1999, the Board denied the petitions for rehearing but amended its original decision to reflect some of the technical amendments requested by the FTB. The Board rejected the taxpayer's argument that California courts follow a different standard in determining whether prospective relief should be granted from the standard set forth *Chevron*. The Board found that the standards were essentially the same and that the "considerations of fairness and public policy" raised by California courts are "fully consistent" with the factors set forth in *Chevron*.

The Board also rejected the taxpayer's argument that it "inappropriately usurped a legislative or policymaking function by issuing a prospective decision." The Board stated that, when it reviewed income tax appeals, it was acting as a "quasi-judicial" body; therefore, like a court, it had the authority to make its decisions applicable on a prospective basis.

The taxpayer argued that the Board should selectively apply the *Joyce* rule to the taxpayer so it would receive "the benefit of its efforts in bringing the matter before [the] Board." Observing that such an approach has been rejected by the courts, the Board declined to selectively apply *Joyce* retroactively.

The Board also rejected the taxpayer's argument that it apply the *Joyce* rule to inbound transactions but continue to apply the *Finnigan* rule to outbound transactions. The Board stated that such an approach "would allow clearly taxable income to escape taxation by all states and is contrary to the fundamental premise of [UDITPA] which is intended to assure that '100 percent of income, no more [and] no less,' will be subject to taxation." The Board stated that "the treatment of both inbound and outbound transactions hinges on the same legal theory and must be resolved in a consistent fashion."

Constitutional Issues

The California Constitution prohibits any agency, including the Board, from refusing to enforce a California statute on the basis that federal law prohibits the enforcement of the statute, unless an appellate court has made a determination that the enforcement of such statute is prohibited by federal law. (Cal. Const., Art. III, § 3.5.) Further, the Board has a long-standing policy of abstaining from deciding constitutional issues, so that such issues may be litigated and definitively resolved in the courts.

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(See, e.g., *Appeal of Vortox Manufacturing Co*., 30-SBE-017, Aug. 8, 1930; *Appeal of Benjamin R. Du and Carmela Du*, 2007-SBE-001, July 17, 2007, fn. 3.)

However, as noted above, in *Grace, supra*, the Board observed that these limitations do not prevent it from considering constitutional issues when interpreting California statutes.

Contentions

Appeal Letter

Appellant states that the determination of whether it is "taxable" in another state is determined by reference to constitutional standards, citing the FTB's June 29, 2010 determination, *Dresser Industries*, and R&TC section 25122. Appellant argues that, under these authorities, it is "taxable" in the States at Issue "if its connections with each state meet the minimum nexus standards under the U.S. Constitution for imposing a net income tax regardless of whether those jurisdictions, in fact, impose net income taxes on craigslist." Appellant contends that the Board must conclude that California and its sister states have jurisdiction under the United States Constitution to impose net income tax on an out-of-state taxpayer whose only connection to the state is having more than $500,000 in sales sourced to the taxing state. Appellant further contends that the Board must conclude that such constitutional jurisdiction existed during 2007, the year at issue. (Appeal Letter, p. 5.)

In support, appellant argues that, through R&TC section 23101, subdivision (b)(2), "[t]he State of California has concluded that it has jurisdiction under the United States Constitution to impose tax on an out-of-state taxpayer by virtue of the taxpayer having $500,000 or more in receipts from a state during a taxable year." Appellant contends that, while one might debate whether the Constitution might permit a lower receipts threshold, ". . . the FTB cannot contend that $500,000 in receipts is sufficient under the U.S. Constitution to give California jurisdiction to impose its net income tax and deny that the same volume of receipts is sufficient under the U.S. Constitution to give its sister states jurisdiction to tax." Appellant states that, whether a state chooses to exercise its jurisdiction to the fullest extent possible is not the issue, as the only issue is whether the tax could be imposed under the Constitution. (Appeal Letter, p. 5.)

Appellant states that the FTB denied its refund claim on the basis that California's move to an economic or factor presence nexus standard is only applicable on or after January 1, 2011, and is

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not retroactive. Appellant argues that the issue is not whether California chose to apply the economic nexus standard, but whether California and its sister states could have imposed tax under the United States Constitution and statutes in 2007. Appellant asserts that, if California has jurisdiction under the Constitution to impose income tax based on economic nexus, "it should be self-evident that California's sister states have that same jurisdiction – and had it in 2007." (Appeal Letter, pp. 5 – 6.)

Appellant states that there is no dispute that it had more than $500,000 in receipts from each of the States at Issue. Accordingly, appellant argues, its gross receipts from these states "were properly included in the denominator of craigslist's sales factor calculation." (Appeal Letter, p. 6.)

Respondent's Opening Brief

Respondent contends that it included the throw-out provision "in order to prevent income from being assigned to jurisdictions where appellant was not subject to tax, resulting in income escaping taxation entirely." Respondent notes that appellant argues that it is taxable in the other states because it had more than $500,000 in sales and that appellant cites in support R&TC section 23101 which provides that a taxpayer is doing business in California if it meets this threshold. Respondent emphasizes that R&TC section 23101 was enacted and became effective January 1, 2011, which respondent states is four years after the year on appeal. Respondent states that it denied appellant's refund claim because ". . . under California law, a physical presence was required to be considered taxable for years beginning before January 1, 2011." (Resp. Op. Br., p. 2.)

Respondent argues that the throw-out rule "has the practical effect of distributing the income of a taxpayer, which is normally assigned to a state that is prohibited from taxing the taxpayer, among the states in which the taxpayer is taxable."[15] Respondent asserts that "[t]his rule is utilized to ensure that 100 percent of a taxpayer's income, no more and no less, is subject to taxation, consistent with the unitary business formula apportionment method of taxation." Respondent states that the throw-out rule works similarly to the throwback rule found in R&TC section 25135, subdivision (b), which provides for sales of tangible personal property to be thrown back and assigned to the state from which the property is shipped if the taxpayer is not taxable in the state of the purchaser. Respondent

[15] In support, respondent cites Hellerstein & Hellerstein, *State Taxation* (3d ed. 2011 & Supp. 2014-2) at par. 9.18[1][c].

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states that the throwback and throw-out rules differ slightly in that the throw-out rule distributes income among all states where a taxpayer is taxable, while the throwback rule throws the income back to the state in which the goods are shipped. Respondent argues that the two rules are similar in that they "are designed to ensure that all of a taxpayer's income, no more or no less, is subject to taxation in the states in which it does business . . . ." (Resp. Op. Br., pp. 3 – 4.)

Respondent notes that ". . . appellant did not file tax returns in any of the States at Issue and does not claim that it was subject to tax in those states as set forth in [R&TC] section 25122, subdivision (a) [which addresses states where a taxpayer is actually subject to tax]." Instead, respondent notes, "appellant argues that the States at Issue had jurisdiction to subject it to a net income tax, as a result of appellant's economic presence within those states consisting only of making sales in those states in excess of $500,000." Respondent argues that appellant cites amendments to R&TC section 23101, which are only applicable to tax years after 2010, to support its argument that "a purely economic presence of sales is sufficient to make it taxable in 2007." (Resp. Op. Br., p. 5.)

Respondent asserts that appellant's argument fails for three reasons. First, respondent contends, appellant's argument fails because "the principles of UDITPA require that [R&TC] section 25122 use the same jurisdictional standard as that of [R&TC] section 23101." Citing case law, respondent notes that courts construe the words of statutes in context in light of the statutory purpose. Respondent contends that, when determining the meaning of R&TC section 25122, subdivision (b), the Board should look at the context and purpose of the statute. Respondent observes that William Pierce, the primary drafter of UDITPA, stated that, if adopted by all states having a net income tax or a tax measured by income, UDITPA "would assure that 100 percent of income, and no more or no less, would be taxed."[16] Respondent contends that R&TC section 25122, subdivision (b), as part of the throwback rule under UDIPTA, must be read with this context and purpose in mind. (Resp. Op. Br., p. 6.)

Respondent contends that, in order for this purpose to be achieved, "the jurisdictional standard under [R&TC] section 25122, which governs outbound transactions, must be the same as the standard used to determine [the] taxability of inbound transactions under [R&TC] section 23101." To

[16] Citing William J. Pierce, *The Uniform Division of Income for Tax Purposes Act*, 35 Taxes 747, 748 (1957).

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illustrate, respondent provides the following example:

> Assume State A requires a taxpayer [to] be physically present in that state in order to subject it to taxation as a result of inbound transactions. However, the jurisdictional standard that State A uses to determine taxability in other states for outbound transactions does not require physical presence; but rather, requires a taxpayer only to have sales over $500,000 to be considered taxable in the other state. Taxpayer X makes $600,000 in sales into State B, which are shipped from State A. Because State A doesn't require outbound sales to be thrownback if a taxpayer has sales over $500,000 to the other state, Taxpayer X's sales into State B would not be thrownback to State A. In turn, those same sales constitute inbound sales of State B. If State B imposed the same formula for inbound sales, i.e., it required a physical presence to be taxable, Taxpayer X would not be taxable in State B because it has no physical presence there. In this situation, UDIPTA's purpose is defeated because Taxpayer X's sales are not taxable by either State A or State B, resulting in less than 100 percent of the taxpayer's income being subject to taxation.

Respondent argues that less than 100 percent of the income is taxed despite the fact the two states impose the same apportionment formulas and contends that "[t]his scheme would result in a classic 'whipsaw,' because both State A and State B would be prohibited from taxing the income associated with the sales in question." (Resp. Op. Br., pp. 6 – 7.)

Respondent argues that, in *Huffy*, *supra*, the Board affirmed that inbound and outbound sales must be determined using the same rule. Respondent states that, in *Huffy*, the appellant argued that the *Finnigan* rule should be applied to outbound sales after the Board had determined that the *Joyce* rule applied to inbound sales. Respondent states that the *Joyce* rule provides that a state must look only to the activities of the corporation, rather than the activities of all the members in a combined report, when determining whether sales and other factors of the corporation should be included in the apportionment formula. In contrast, respondent states, the *Finnigan* rule looked to the activities of the entire combined reporting group when determining whether sales should be thrown back to the state of origin. Respondent states that the Board declined to adopt an approach in which one rule would apply to inbound transactions and another to outbound transactions, noting that such an approach would "allow clearly taxable income to escape taxation by all states and is contrary to the fundamental premise of [UDITPA] which is intended to assure that '100 percent of income, no more [and] no less,' will be subject taxation." Noting that the Board found that inbound and outbound transactions should be treated similarly, respondent argues that it is clear that the same standard must apply to both types of

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transactions. On this basis, respondent contends that R&TC section 25122, "as the standard applicable to outbound transactions, must be applied using the same jurisdictional standard applicable for [the] determination of [the] taxability of transactions within California for the year at issue." (Resp. Op. Br., p. 7.)

Second, respondent argues that, under the laws for the year at issue, an economic presence alone was not sufficient to assert jurisdiction under R&TC section 23101. Respondent contends that, for tax years beginning before January 1, 2011, R&TC section 23101 "required a physical presence to assert jurisdiction because (a) your Board determined that, under the laws existing for the year at issue in this appeal, a physical presence was necessary, and (b) the explicit statutory language permitting the imposition of the franchise tax does not permit applying the economic presence standard prior to January 1, 2011." (Resp. Op. Br., p. 8.)

In support of its assertion that the Board has determined that physical presence was required to establish jurisdiction to tax for years prior to 2011, respondent cites *Grace*, *supra*, 80-SBE-115, October 28, 1980, and two nonprecedential summary decisions, the *Appeal of Personal Selling Power, Inc*. Case No. 380557, decided March 16, 2009 (*Personal Selling Power*), and the *Appeal of Warwick McKinley Inc*., Case No. 489090, decided January 11, 2012 (*Warwick McKinley*).[17] Respondent notes that, in *Grace*, the Board held (quoting the Board): ". . . [n]o barrier exists to prevent the taxation of income . . . so long as the corporation's in-state business activities have some regular, systematic and substantial connection with, *and physical presence within*, the taxing state. . . . [respondent's emphasis]." Respondent states that this same standard was applied in the appeals of *Personal Selling Power* and *Warwick McKinley*. Respondent notes that the *Warwick McKinley* appeal involved the 2006 tax year, and it was rendered in 2012, "after the economic presence standard applicable for taxable years beginning on or after January 1, 2011." Respondent asserts that the Board "was aware of the new economic presence standard and even then, ruled that for the 2006 tax year, which is only one year prior to the year at issue, physical presence was the appropriate standard to

[17] *Personal Selling Power* and *Warwick McKinley* were decided as Summary Decisions. Board regulations provide that Summary Decisions are Nonprecedential Opinions that "may not be cited as precedent in any matter or proceeding before the Board." (See Cal. Code Regs., tit. 18, § 5451, subd. (b)(4), § 5511, subd. (u).)

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determine taxability."[18] (Resp. Op. Br., p. 9.)

Respondent acknowledges that *Personal Selling Power* and *Warwick McKinley, Inc.* are not to be cited as precedent, but states that these decisions are informative when determining how to apply the law, citing *Microsoft Corp. v. FTB* (2006) 212 Cal.App.4th 78, 93-94. Respondent further contends that ". . . a review of your Board's decisions reveals that it has never held that this state had jurisdiction to impose the franchise tax under [R&TC section 23101] for taxable years beginning before January 1, 2011, based upon economic presence alone." Respondent asserts that ". . . it follows that a physical presence is required . . . for taxable years beginning before January 1, 2011." Respondent further asserts that, since physical presence is required under R&TC section 23101 for years prior to 2011, "the same standard is required under [R&TC] section 25122." (Resp. Op. Br., p. 10.)

Respondent states that legislation applies prospectively, unless explicitly stated otherwise, citing *Aetna Cas. & Surety Co. v. Ind. Acc. Com.* (1947) 30 Cal.2d 388, 393. Respondent observes that R&TC section 23101, subdivision (b), expressly provides that it applies for taxable years beginning on or after January 1, 2011. Respondent argues that, because R&TC section 23101 does not apply retroactively, economic nexus may not be established for inbound transactions for years prior to 2011 and "the same treatment is required for outbound sales." (Resp. Op. Br., pp. 10 – 11.)

Third, respondent argues that economic presence alone is not sufficient to find appellant taxable under the terms of the Determination Letter which allowed appellant a special apportionment methodology. Respondent emphasizes the following italicized portions of the Determination Letter:

> *There is a concern regarding income earned in states and countries where the taxpayer is not taxable, i.e., "nowhere" income."* For that reason, the throw-out rule will be utilized meaning that gross receipts sourced to a location in which the taxpayer is not taxable, as defined in RTC section 25122, will be excluded from the sales factor calculation. This will more accurately represent the taxpayer's business in California. Based on [the] *Appeal of Dresser Industries*, 83-SBE-118, June 29, 1982, aff'd Oct. 26, 1983[.] *United States constitutional standards for nexus will be used to determine whether a foreign country or state has jurisdiction to tax.* Taxpayer will bear the burden of proving nexus in all cases. [respondent's emphasis]

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[18] Staff notes that both *Warwick McKinley* and *Personal Selling Power* involved taxpayers who were physically present in California. Accordingly, neither decision discussed whether nexus might be established in some circumstances without a physical presence, and neither decision addressed the amendments to R&TC section 23101, which were effective for tax years after the years at issue in those cases.

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Based on the above, respondent argues that "the Determination Letter specifically requires application of your Board's interpretation of the Constitutional nexus standards as set forth in [*Dresser Industries*] for purposes of determining whether appellant was taxable in another country or state." Respondent observes that, in *Dresser Industries*, the Board found that the activity of unitary subsidiaries caused the taxpayer in that appeal to be physically present, and therefore taxable, in the foreign countries. Thus, respondent contends, the U.S. Constitutional standard applied in *Dresser Industries* requires a physical presence. Respondent asserts that, since the Determination Letter required the application of the standard set forth by *Dresser Industries*, the Determination Letter required that appellant have a physical presence in other states in order to be found taxable. (Resp. Op. B., pp. 11 – 12.)

Appellant's Reply Brief

Appellant argues that the FTB is erroneously contending the jurisdiction of the States at Issue to impose tax on appellant in 2007 "turns on how California chose to [exercise] its taxing jurisdiction in 2007." Appellant contends that "[t]he FTB's position is contrary to the plain language of [R&TC section] 25122(b) and is not supported [by] 'principles of UDITPA,' the decisions of this Board, or the FTB Determination Letter." (App. Reply Br., p. 2.)

First, appellant argues that the FTB ignores the plain language of R&TC section 25122. Appellant observes that the statute provides "two alternative bases" to conclude that a taxpayer is taxable and that the second basis, set forth in paragraph (b), finds that a taxpayer is "taxable" in a state where "that state has jurisdiction to subject the taxpayer to a net income tax regardless of whether, in fact, the state does or does not." Appellant also notes that the FTB's regulations provide that the determination of whether a taxpayer's business activity is sufficient to provide jurisdiction to tax will be determined "under the Constitution and statutes of the United States[,]" quoting California Code of Regulations, title 18, section (Regulation) 25122, subdivision (c). Appellant also observes that the Determination Letter states that "United States constitutional standards for nexus" will be used to determine whether a state has jurisdiction to tax. (App. Reply Br., pp. 2 – 3.)

Appellant argues that the States at Issue had jurisdiction to tax craigslist in 2007 "for the same reason that California has asserted such jurisdiction beginning in 2011." Appellant asserts that the FTB does not dispute "the ultimate legal issue in this appeal: the States at Issue had jurisdiction under

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the U.S. Constitution to impose a net income tax on craigslist in 2007." Appellant contends that "[t]he FTB's silence is telling." (App. Reply Br., p. 3.)

Appellant reiterates that R&TC section 25122, subdivision (b), does not require that a state actually tax a taxpayer. Appellant states that this is why the statute contains the concluding phrase: "regardless of whether, in fact, the state does or does not." Appellant observes that the statute only requires that the state have the constitutional authority to tax. Appellant argues that the statute is "an acknowledgement that states in our federal system may not choose to exercise their taxing jurisdiction to the full extent of the U.S. Constitution." (App. Reply Br., p. 3.)

As an example, appellant points to Washington State, which is one of the States at Issue. Appellant states that Washington "made a policy decision not to impose a net income tax" and instead impose a business and occupation tax that would only be imposed on taxpayers with a physical presence. Appellant states that Washington changed this policy decision effective June 1, 2010 to assert tax based on a market factor presence (including more than $250,000 in Washington receipts). Appellant argues that, although Washington's policy, as reflected in its statute, has changed, its "jurisdiction to impose tax did not change . . . ." (App. Reply Br., pp. 3 – 4.)

Appellant argues that "the FTB does not dispute that each of the States at Issue had jurisdiction under the US, Constitution to impose an income tax on out-of-state taxpayers with more than $500,000 in gross receipts." Appellant further argues that "there is no factual dispute that, during tax year 2007, craigslist had more than $500,000 in receipts from each of the States at Issue." Appellant contends that each of the States at Issue had jurisdiction to tax appellant under R&TC section 25122, subdivision (b), regardless of whether any of the states did, in fact, subject appellant to tax. (App. Reply Br., p. 4.)

Appellant disputes the FTB's contention that "principles of UDITPA" support the FTB's position. With regard to William Pierce's observation that UDITPA, if enacted, would result in 100 percent of income being taxed, no more or no less, appellant states that the premise of the quotation "has never been fulfilled." Appellant contends that "very few states" conform to UDIPTA and that California has contributed to a lack of uniformity by, among other things, adopting a single-factor apportionment method. (App. Reply Br., pp. 4 – 5.)

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Appellant argues that UDITPA is "not harmed" when states choose not to impose a tax and that this "is the simple result of a federal system in which states exercise their jurisdiction to tax in different ways." For example, appellant argues, the FTB would not appear to dispute that craigslist could apportion gross income to Texas (based on having more than $500,000 in Texas receipts) for years after 2010, "despite Texas' decision not to impose an income tax . . . ." (App. Reply Br., p. 5.)

Appellant further argues that R&TC section 25122 "specifically contemplated that states may choose to exercise their jurisdiction differently" by expressly providing that a taxpayer is taxable if the jurisdiction to tax is present "regardless of whether, in fact, the state does or does not." Appellant contends that the FTB cannot resort to appeals to uniformity principles when the Legislature "plainly rejected state law uniformity as a prerequisite to apportionment." Appellant argues that the sole question is whether the States at Issue had jurisdiction to tax and asserts that the FTB does not dispute that the answer is "yes." (App. Reply Br., p. 5.)

Appellant disputes the FTB's contention that *Grace* and two later nonprecedential decisions (*Personal Selling Power* and *Warwick McKinley*) support the FTB's position. Appellant notes that the taxpayer in *Grace* had a physical presence in California and argues that, "[b]ecause the taxpayer had ample sales and other connections, this Board's suggestion that physical presence might be necessary for nexus was *dicta*." Appellant emphasizes that a more important distinction is that all three decisions involved how California exercised is taxing jurisdiction while, in contrast, "the right to apportion under Section 25122(b) turns on whether other states have jurisdiction 'under the Constitution and statutes of the United States' to impose tax," citing Regulation 25122, subdivision (c). (App. Reply Br., p. 6.)

Appellant argues that FTB does not dispute that the States at Issue had the constitutional power to tax it in 2007 and asserts that the FTB "could hardly argue otherwise." Appellant contends that, if New York did not have the constitutional power to tax a California company based on over-$500,000 in sales in 2007, then "California does not have the same constitutional power currently."[19]

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[19] In footnote 3 of its brief, appellant notes that, in 2002, the Multistate Tax Commission (MTC) promulgated model legislation providing for jurisdiction where the taxpayer had more than $500,000 in sales. Appellant argues that the model legislation reflects the MTC's view that states had the constitutional power to impose tax on taxpayers like craigslist without a physical presence.

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(App. Reply Br., p. 6.)

Appellant also contends that the FTB's Determination Letter does not support the FTB's position that the States at Issue did not have the jurisdiction to tax in 2007. Appellant notes that the determination letter requires the use of constitutional standards for nexus. Appellant disputes the FTB's contention that the fact the Determination Letter cites *Dresser Industries* "somehow negates its clear instruction" that constitutional standards will be used. Appellant argues that the FTB "mischaracterizes" *Dresser Industries* "as holding that physical presence is constitutionally required to apportion." Appellant contends that nexus was not even an issue until the consideration of the petition for rehearing, "much less part of the Board's holding." Appellant quotes the Board's statement in *Dresser Industries* that the FTB's "only reason for reaching this conclusion [that the taxpayer was not taxable in the state of purchaser] is its view that uniformity in the interpretation of UDITPA's statutes and regulations requires the application of P.L. 86-272's jurisdictional limitations to the taxation of income from both interstate and foreign commerce." Appellant argues that the parties agreed that the taxpayer had nexus in the jurisdictions at issue and "the sole question . . . was whether Public Law 86-272 deprived foreign (non-U.S.) jurisdictions of jurisdiction to subject the taxpayer to a net income tax under "United States jurisdictional standards." On these grounds, appellant argues that *Dresser Industries* does not provide anything "to contradict the FTB's plain instructions to craigslist that '**United States constitutional standards for nexus** will be used to determine whether a foreign country or state has 'jurisdiction to tax.' [appellant's emphasis]" (App. Reply Br., p. 7.)

Respondent's Reply Brief[20]

The FTB reiterates that the throw-out rule was included in the Determination Letter to ensure that appellant was subject to tax on 100 percent of its income, "no more or no less." The FTB contends that "appellant's tax liability over the entire relief period (i.e., 2007-2010) was reduced due to

[20] In footnote 1 of its reply brief, the FTB argues that deciding whether the U.S. Constitution permitted a state to exercise jurisdiction to tax based on economic presence alone prior to January 1, 2011 "would effectively require your Board to make a constitutional determination . . . ." Respondent requests that the Board abstain from addressing this constitutional issue, pointing to the Board's longstanding policy of abstaining from making constitutional determinations and citing the *Appeal of Granite Construction Co., Inc*., 52-SBE-011, decided July 22, 1952, and the *Appeal of Coro, Inc*., 55-SBE-001, decided March 30, 1955. However, respondent requests that, if the Board "determines that it can resolve this case on other grounds, . . . your Board publish a precedential, written opinion." Respondent contends that the issue in this appeal has been raised in numerous other matters and argues that issuing a precedential opinion will provide guidance.

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the alternative apportionment formula granted by respondent."[21] The FTB asserts that appellant "is now request[ing] additional relief by attempting to retroactively use a change in law" that the Legislature explicitly provided would only have prospective effect. Respondent characterizes appellant's argument as contending that "even though [appellant] did not pay taxes in [the States at Issue], it is taxable in the States [at] Issue under R&TC section 25122." Respondent observes that appellant is arguing that the States at Issue could tax appellant under the U.S. Constitution such that appellant was taxable under R&TC section 25122, subdivision (b), "and the States at Issue merely opted not to exercise jurisdiction." (Resp. Reply Br., p. 1.)

The FTB argues that case law and other authorities "prohibit a finding that appellant is taxable in the States at Issue during 2007." Summarizing its arguments, the FTB contends that other authorities supporting its position include (i) the Legislature's prospective enactment of an economic presence standard, (ii) the principle that outbound sales under R&TC section 25122 must be treated the same as inbound sales, and (iii) that the standard set forth in the Determination Letter requires a physical presence. (Resp. Reply Br., p. 2)

The FTB argues that, while R&TC section 25122, subdivision (b), requires the application of a constitutional standard, it does not set forth what contacts with a state are sufficient to meet that standard. Therefore, respondent argues that other authorities such as cases must be consulted to determine the constitutional standard. (Resp. Reply Br., p. 3.)

Respondent notes that in *Grace* the Board stated, citing authorities, that "[s]ince the Legislature intended the taxing statutes to reach only to the limits permitted by the Constitution, our application of the statutes to the facts presented is restricted by constitutional limitations." Respondent argues that the Board thus confirmed that California tax statutes "do not have a narrower jurisdictional

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[21] The parties agree that, under respondent's application of the throw-out rule, the alternative apportionment formula did not reduce appellant's tax for the year at issue (2007). Based on pre-hearing conference discussions, it appears the parties may disagree regarding whether, under respondent's application of the throw-out rule, the alternative apportionment formula significantly reduced appellant's liabilities for the 2008 – 2010 years. Following the pre-hearing conference, respondent stated that its records show appellant would receive, using respondent's application of the alternative apportionment formula, a reduction in tax of $21,243, $146,520, and $193,001 for, respectively, the 2008, 2009, and 2010 tax years. It is not clear whether appellant agrees that this would be the tax reduction if one applied the throw-out rule in the manner advocated by respondent.

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standard than what is permitted by the Constitution."[22] (Resp. Reply Br., p. 4.)

Respondent argues that the Board applied the physical presence standard in *Dresser Industries*. Respondent observes that, in *Dresser Industries*, the Board "contrasted the contacts present in that case with the lack of substantial contacts, including the requisite physical presence, in *Appeal of John H. Grace* . . . ." Respondent argues that it is notable that the Board never discussed the issue of whether the sales or economic presence of the appellant in *Dresser Industries* was sufficient to create taxability. Respondent argues that the Board applied the same physical presence standard for R&TC section 25122 that it applied for R&TC section 23101 for tax years beginning before January 1, 2011.[23] (Resp. Reply Br., pp. 5 – 6.)

Respondent contends that the Legislature's "prospective enactment of an economic presence standard to determine taxability, as well as settled principles of reliance, require [the] application of a physical presence standard for the years at issue." Respondent argues that, by making amendments to R&TC section 23101, subdivision (b), effective only for tax years beginning on or after January 1, 2011, ". . . the Legislature determined that for taxable years beginning on or after January 1, 2011, substantial nexus will exist under California law based upon economic presence." Respondent argues that this "new standard is possible since the Constitution was intended to adapt to new, unforeseen situations, and thus, it can evolve to recognize changing standards as to what constitutes sufficient nexus or connections with a state." Respondent argues that this is especially true given changes in the economy, "as the Internet now allows entities to have substantial nexus or connection in this state, and thereby meet the constitutional requirements without being physically present."[24] Respondent argues that the Legislature's "adoption of the economic presence standard effectively

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[22] In its footnote 5, respondent also cites *Appeal of Atlantic, Gulf and Pacific Company of Manila, Inc.*, 82-SBE-255, decided November 17, 1982. Respondent further asserts that the following cases concerning California taxes "have been analyzed to the extent permitted by the Constitution[,]" citing as examples *Communications Satellite Corp. v. FTB* (1984) 156 Cal.App.3d 726, *Current, Inc. v. State Board of Equalization* (1994) 24 Cal.App.4th 382, and *Container Corp. of Amer. v. FTB* (1983) 463 U.S. 159.

[23] In support, respondent also cites *Appeal of Union Carbide*, 84-SBE-057, decided April 5, 1984 (*Union Carbide*) and *Appeal of Christie Electric*, 87-SBE-062, decided August 18, 1987 (*Christie Electric*). Respondent also cites these cases on page 10 of its reply brief.

[24] In its footnote 7, respondent cites a concurrence by Justice Kennedy in *Direct Marketing Association v. Brohl* (2015) 135 S. Ct. 1124, 1135 (*Direct Marketing*). Appellant addresses this argument on page 4 of its supplemental reply brief.

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reflects the Legislature's recognition of the changed economy, and the prospective application provides a bright-line determination that the change in the nature of the economy occurred as of January 1, 2011." Respondent argues that "[t]axpayers and the state must respect this bright-line rule as to prospective application of the economic presence standard." (Resp. Reply Br., pp. 6 – 7.)

Respondent contends that this case would not have arisen absent the Legislature's enactment of an economic presence standard "because prior to that time California law, which this state exercised to the extent permitted by the Constitution, unambiguously required a physical presence to impose a tax." Respondent argues that appellant is asking the Board to disregard the Legislature's specific language and apply the economic presence standard "in a year that was never intended by the Legislature." Respondent further argues that "use of an economic presence standard in 2007 would render the qualifying language in [R&TC] section 23101 limiting the application of such standard a nullity, and would create an absurd result." (Resp. Reply Br., p. 7.)

Respondent further contends that the "retroactive application of the new economic presence rule will infringe upon settled principles of reliance and will result in injustice or hardship to taxpayers and the government alike." Respondent argues that ". . . other taxpayers who relied on your Board's authorities requiring physical presence in this state will suddenly be exposed to potential enforcement actions based on the fact that they had economic presence in California before 2011." Respondent asserts that, "[w]hen such reliance interests are present, the Legislature, the courts, and respondent each possess authority to prospectively apply new rules."[25] Respondent observes that the Board exercised this authority, acting in its role as a quasi-judicial body, in *Huffy*, *supra*, in which the Board held that the *Joyce* rule, which departed from the prior *Finnigan* rule, should be applied prospectively. Respondent notes that, in applying the new rule prospectively, the Board stated:

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[25] In its footnote 8, respondent cites in support *Forster Shipbldg. Co. v. County of Los Angeles* (1960) 54 Cal.2d 450 in which the court held that the Legislature could apply a new rule prospectively. Respondent also cites R&TC section 19503, which allows it to prescribe rules and regulations and the extent to which such rules and regulations shall be applied without retroactive effect. Respondent argues that, because this authority extends to rules under Part 11 of the R&TC, and R&TC sections 23101 and 25122 are in Part 11 of the R&TC, it has the authority "to apply rules regarding these provisions on a prospective basis only."

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> . . . A prospective ruling allows taxpayers to make an informed decision concerning their tax matters.[] Prospective application does not penalize or provide a windfall to taxpayers with standards which took effect subsequent to their tax planning. When a "new" [principle] of law is created by the overruling of past precedent, stability should remain a consideration.
> (Resp. Reply Br., pp. 7 – 8.)

Respondent argues that the same considerations relied on in *Huffy* were present before the Legislature when it enacted R&TC section 23101, subdivision (b), effective beginning in 2011. Respondent argues that adopting a new constitutional standard now "might require the state to assert jurisdiction and attempt to impose tax upon uncounted taxpayers who had a purely economic presence in this state prior to January 1, 2011, but who relied on the unambiguous physical presence standard applicable in this state at that time." Conversely, respondent argues that other taxpayers in a similar situation to appellant "might receive a windfall." (Resp. Reply Br., pp. 8 – 9.)

Respondent further contends that, in *Chevron, supra*, 404 U.S. 97, the United States Supreme Court recognized that considerations cited in *Huffy* constitute a basis for the prospective application of new rules. Respondent argues that the Court found that the prospective application of a rule of law is proper where, quoting the Court, the rule of law is a new one, by considering whether a retrospective operation will "further or retard" the application of the rule and finally, by "weighing the inequity imposed by retroactive application . . . ." (Quoting *Chevron, supra*, 404 U.S. 97, at p. 106.) Respondent contends that the *Chevron* rule has been approved or used by many courts, citing *Nunez-Reyes v. Holder* (2011) 646 F.3d 684, *Citicorp North America, Inc. v. FTB* (2000) 83 Cal.App.4th 1403 and *Am. Trucking Assoc. v. Smith* (1990) 496 U.S. 167 (*Am. Trucking*). (Resp. Reply Br., p. 9.)

Respondent argues that this case involves a new principle of law that was established by the Legislature and "which overruled a clear past precedent on which taxpayers relied." Respondent asserts that "taxpayers and the state alike relied on the decisions of your Board in the decisions of [*Grace*, *Personal Selling Power*, and *Warwick McKinley*]."[26] Respondent further asserts that "[t]hese decisions all determined that taxpayers are taxable in this state, as applicable for years beginning before January 1, 2011, only upon a showing of some physical presence." Respondent asserts that the Board,

[26] Respondent notes that *Personal Selling Power* and *Warwick McKinley* are not to be cited as precedent but argues, citing *Microsoft Corp., supra*, 212 Cal.App.4th 78, 93-94, that such decisions may be "informative."

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in its decisions in *Dresser*, *Union Carbide*, *supra*, 84-SBE-057, and *Christie Electric*, *supra*, 87-SBE-62, found that taxpayers were taxable in other states under R&TC section 25122 only upon a showing of physical presence. Respondent observes that the Board has never previously held that a taxpayer is taxable based on a purely economic presence for years prior to 2011. Respondent therefore concludes that the precedents clearly provided that physical presence was the standard prior to 2011, that taxpayers and respondent relied on this rule, and that the economic presence standard reflects a new rule. (Resp. Reply Br., pp. 9 - 10.)

Citing *Chevron*, *supra*, 404 U.S. 97, and *Am. Trucking*, *supra*, 496 U.S. 167, 180-181, respondent argues that the Board must consider the purpose and effect of the rule in question. Respondent argues that, because the prior physical presence rule constituted a legitimate state tax, as no precedential decision has ruled otherwise, the commerce clause "does not require retroactive application." (Resp. Reply Br., p. 10.)

Respondent further argues, citing *Chevron*, that a retroactive application would produce substantial inequitable results. Respondent asserts that, if the Board were to accept appellant's arguments, "it would be effectively holding that the U.S. Constitution would have permitted California to assert jurisdiction upon a purely economic presence prior to January 1, 2011." Respondent contends that such a holding would extend beyond the Board's policy of abstaining from deciding constitutional issues. Respondent further contends that ". . . such a holding could require respondent to assert jurisdiction and taxes upon taxpayers that previously had little or no tax obligation." Also, respondent contends, "such a ruling could potentially create a hardship on the state to refund taxes under [R&TC] section 25122, based upon a jurisdictional standard that did not exist at the time." Respondent concludes that, if the Board "opts to render a decision that the economic nexus standard is constitutional, the principles of *Chevron* oblige your Board to do so prospectively as of January 1, 2011." (Resp. Reply Br., pp. 10 – 11.)

Citing *Huffy*, *supra*, respondent contends that "the standard to determine taxability for outbound sales under [R&TC] section 25122, subdivision (b) must be the same standard to determine taxability as inbound sales and during the year at issue the taxability of inbound sales requires a physical presence." Respondent asserts that the U.S. Constitution, "as interpreted in California law,

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prohibited the assertion of jurisdiction upon a purely economic nexus presence prior to January 1, 2011." Respondent further asserts that, even if this were not the case, "a physical presence is still required for the purpose of determining whether appellant is taxable in the States at Issue in 2007[,]" because R&TC section 23101 "requires a physical presence during the years at issue" and the standard must be the same for outbound sales. (Resp. Reply Br., p. 11.)

Respondent argues that the Determination Letter required a physical presence by stating that "based upon [*Dresser Industries*], United States constitutional standards will be used to determine . . . jurisdiction to tax." Respondent asserts that "the U.S. constitutional standard articulated in [*Dresser Industries*], i.e., physical presence, will be the standard used under the Determination Letter to determine whether a foreign country or state has jurisdiction to tax." Thus, respondent contends, "because appellant lacked a physical presence in the states at Issue during 2007; it cannot be found taxable and it must throw-out its sales assigned to these states under the terms of the Determination Letter." Respondent further states that, when the Determination Letter cited *Dresser Industries*, it was citing the opinion on rehearing, and that the issue on rehearing was solely whether the taxpayer had nexus in other countries.[27] For this reason, respondent disputes appellant's argument that nexus was not a part of the holding in *Dresser Industries.* (Resp. Reply Br., pp. 12, 14 - 15.)

The FTB contends that appellant, in responding to its quotation of Mr. Pierce, "appears to argue" that because states do not uniformly follow UDITPA "the purpose of [R&TC] section 25122 should simply be disregarded." The FTB argues that appellant's response "misses the point" because, as explained by Mr. Pierce, "the concept of taxability in other states, which California has codified in [R&TC] section 25122, is based on the *assumption* that every state imposes a tax, which *theoretically* subjects all of a taxpayer's income to tax in the jurisdictions in which it conducts business. [respondent's emphasis]" On this basis, respondent argues that appellant's argument that other states have not conformed to UDIPTA "is simply not relevant to the analysis." (Resp. Reply Br., pp. 12 – 13.)

Respondent disputes appellant's argument that the physical presence standard set forth

[27] Respondent apparently refers here to the Opinion on Petition for Rehearing, as the petition for rehearing was denied so there was no rehearing.

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in *Grace*, *supra*, was dicta and thus not relevant. Respondent notes that dicta is defined as expressions in an opinion which are not necessary to support the decision. Respondent observes that, in *Grace*, the Board stated "**[w]e decline to follow the lead of the Oregon Supreme Court by accepting mere economic presence** as constituting sufficient statutory nexus to support the corporate income tax" and instead stated that "no barrier exists [to taxation] . . . so long as the corporation's in-state business activities have some regular, systematic and substantial connection with, and **physical presence** within, the taxing state . . . . [respondent's emphasis]." Respondent further argues that the Board found that the appellant in *Dresser Industries* conducted no business and had no agents in California, and therefore it had no "activities" within the state. Respondent argues that the Board thus found the lack of the requisite physical activities in the state. On these grounds, respondent argues that the discussion of physical presence is not dicta and further argues that the Board has reiterated this standard in *Personal Selling Power* and *Warwick McKinley*. (Resp. Reply Br., pp. 13 -14.)

Appellant's Supplemental Reply Brief

Appellant argues that the FTB "struggles to complicate a simple case." Appellant observes that R&TC section 25122 provides that a taxpayer is "taxable in another state" under subdivision (a) if the taxpayer is subject to a net income tax or certain other taxes, ***or*** (appellant's emphasis) under subdivision (b) if "that state has jurisdiction to subject the taxpayer to a net income tax regardless of whether, in fact, the state does or does not." Appellant argues that R&TC section 25122 "does not require a state to exercise its jurisdiction in the same manner as California or even to exercise its jurisdiction at all." Appellant contends that, since R&TC section 25122 applies a disjunctive test, a taxpayer is taxable if the state, under subdivision (b) of R&TC section 25122, "has jurisdiction to subject the taxpayer to a net income tax, regardless of whether, in fact, the state does or does not." Appellant asserts that "nowhere" in the FTB's briefs does the FTB assert that the "State at Issue did not have 'jurisdiction to subject' craigslist to tax in 2007." (App. Supp. Reply Br., pp. 1 – 2.)

Appellant argues that the FTB concedes that California imposes tax based on an economic presence standard for years after 2010 and further concedes, "as it must[,]" that California has jurisdiction under the United States Constitution to impose tax on that basis. Appellant argues that it is irrelevant whether California decided to exercise its jurisdiction to impose tax based on economic

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presence. Instead, appellant argues, the issue is whether the "the States at Issue had 'jurisdiction to subject the taxpayer to a net income tax' in 2007." (App. Supp. Reply Br., p. 2.)

Appellant disputes the FTB's "theory regarding the evolving Constitution." Appellant argues "there is no U.S. constitutional authority for the proposition that a taxpayer must have physical presence in a state in order to be subjected to a net income or business activity tax." Quoting *Quill Corp. v. North Dakota* (1992), 504 U.S. 298, 317 (*Quill*), appellant argues that, while the court has set forth a physical presence standard for sales and use tax collection, it has declined to adopt a similar physical-presence requirement for income taxes. (App. Supp. Reply Br., pp. 2 – 3.)

Appellant contends that "the overwhelming majority of states that have addressed whether a state has jurisdiction to impose income or business activity tax on the basis of economic activity have concluded that physical presence is not required."[28] Appellant observes that the Multistate Tax Commission (MTC), of which California was a member, urged states to adopt a "factor presence" nexus statute in 2002, which appellant notes is "five years before the first year at issue in this appeal and more than a decade before California changed its doing business standard to reflect the MTC approach." Appellant argues that the FTB presumably would not contend "that the MTC was urging the adoption of a model statute that violated the constitutional nexus standard in 2002 and that states had no jurisdiction to adopt." (App. Supp. Reply Br., p. 3.)

Appellant emphasizes that, "perhaps most importantly," the Determination Letter was issued on June 29, 2010, which was "a year after the legislature adopted the market factor nexus standard that became effective beginning tax year 2011." Appellant argues that, when the FTB issued the Determination Letter, the Legislature and the FTB "understood that California had jurisdiction to make the change to the doing business statute." Appellant further argues that the delay in implementing the change was a "a matter of policy, not jurisdiction." Appellant contends that "the 2009 bill analysis suggests that the Legislature understood that economic activity was sufficient to create nexus under state law before 2009[,]" by stating that R&TC section 23101 was being amended

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[28] In appellant's footnote 2, it cites many state court cases in support, including *Borden Chems. & Plastics, L.P. v. Zehnder* (Ill. App. Ct. 2000) 726 N.E.2d 73, *MBNA Am. Bank, N.A. v. Ind. Dep't State Revenue* (Ind. Tax Ct. 2008) 895 N.E.2d 140, and *KFC Corp. v. Iowa Dep't of Revenue* (Iowa 2010) 792 N.W.2d 308, *cert. denied*, 132 S. Ct. 97 (2011).

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"to clarify and specify" that companies that operate "or make sales in the state are doing business in California and subject to California tax." (App. Supp. Reply Br., pp. 3 – 4.)

Appellant disputes the FTB's argument that "changes to the economy as the result of the Internet have caused a constitutional evolution in income tax nexus." Appellant argues that "none of the numerous income or business activity tax nexus cases noted in footnote 2 [of appellant's brief] involve Internet-based businesses." Appellant notes that the FTB cites Justice Kennedy's concurring opinion in *Direct Marketing*, *supra*, 135 S. Ct. 1124, 1135, in support of the FTB's argument about changes in the economy.[29] Appellant argues that Justice Kennedy was discussing economic changes as a basis for reconsidering *Quill*'s physical presence standard for sales and use tax collection, and contends that "such changes are not constitutionally relevant to income tax nexus, which has never been subject to the same physical presence standard." (App. Supp. Reply Br., p. 4.)

Appellant argues that "California's 2009 decision to assert its jurisdiction on the basis of a factor presence nexus standard beginning in 2011 does nothing to detract from the jurisdiction of other states to exercise their jurisdiction differently." Appellant notes that some states provide standards different from California's standard of $500,000 in sales and other states may choose to exercise jurisdiction to tax on the basis of physical presence. Appellant argues that "the FTB would not presumably question any of those states' jurisdiction to tax." (App. Supp. Reply Br., p. 5.)

Appellant concludes by arguing that the only question is whether the States at Issue had "jurisdiction to subject the taxpayer to a net income tax" during 2007 "under the Constitution and statutes of the United States[,]" quoting R&TC section 25122 and the regulations thereunder. Appellant asserts that "the FTB does not dispute [the States at Issue] had such jurisdiction."[30] Thus, appellant argues, it was "taxable" in those states "under the plain language of [R&TC] section 25122." (App. Supp. Reply Br., p. 5.)

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[29] The FTB cites to *Direct Marketing* in footnote 7 of its reply brief.

[30] In a pre-hearing telephone conference held on November 3, 2015, the FTB confirmed that it disputes that the States at Issue had jurisdiction to tax appellant during 2007.

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STAFF COMMENTS

Application of R&TC section 25122 and Regulation 25122

Under R&TC section 25122, subdivision (b), and Regulation 25122, subdivision (c), appellant was taxable in another state during 2007 if it had a sufficient nexus with that state to subject it to a net income tax under the laws and Constitution of the United States, regardless of whether the state actually imposed a tax. The parties agree that, at some point, a taxpayer could be subject to net income tax in a state without a physical presence under the United States Constitution, as interpreted by the courts. However, the parties differ on whether constitutional standards required a physical presence during the year at issue, 2007.

Appellant argues that it could have been subject to tax in the States at Issue without a physical presence during 2007, which respondent disputes. Both parties note that the California Legislature amended R&TC section 23101 to allow taxation without a physical presence where a taxpayer has more than $500,000 in sales. The FTB points out that the legislation was not effective until January 1, 2011, and argues that applying the rule set forth in the legislation prior to its effective date would lead to inequitable results and require the FTB to issue assessments to companies making sales in California without a physical presence prior to the effective date of the statute. Appellant observes that, although the legislation was not effective until 2011, it was enacted early in 2009 (prior to the issuance of the Determination Letter), and argues that the legislation reflected a determination that physical presence was not constitutionally required and is consistent with state court decisions finding that a physical presence is not constitutionally required.

It appears to staff that, while both parties present compelling arguments, it is difficult to determine whether the United States Constitution, as interpreted by the courts, allowed income taxation without a physical presence during 2007. In *Grace*, *supra*, 80-SBE-115, decided October 28, 1980, the Board declined to accept "mere economic presence as constituting sufficient statutory nexus to support the corporate income tax." While an increasing number of state court cases have found that a physical presence is not necessary, the United States Supreme Court has not so held, and there is no Board decision or California court decision finding that nexus to impose an income tax may be established

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without a physical presence.[31]

In light of the foregoing, it appears that a decision of the Board finding that physical presence was not required during 2007 would establish a new rule of law in an unsettled area. Moreover, it is a constitutional issue, which the Board has traditionally avoided addressing in order to allow such issues to be resolved in the courts. It is not clear to staff that the Board should abstain entirely from making this determination, as R&TC section 25122, subdivision (b), and the FTB's regulation thereunder, Regulation 25122, subdivision (c), require that the determination of whether a taxpayer is taxable shall be made by applying constitutional law. However, the constitutional nature of the issue, as well as the reliance and consistency interests raised by the FTB, suggest that the Board should exercise great caution when determining the constitutional limits of taxation for the 2007 year. Also, Section 3.5 of Article III of the California Constitution precludes the Board from ruling that California's statute exceeds the bounds of the United States Constitution. In light of the foregoing considerations, the Board may wish to consider whether the physical presence standard should be retained for any tax year for which there is not controlling authority, such as a California appellate court decision, a United States Supreme Court decision, or a California statute, holding that physical presence is not required for that year.

Interpretation of the Determination Letter

As the Determination Letter appears to govern the taxation of appellant for the year at issue, the parties should be prepared to discuss further the discussions that preceded the Determination Letter and appellant's acceptance of the Determination Letter. The parties should be prepared to discuss how the throw-out rule came to be included in the Determination Letter and what the anticipated results of the special apportionment formula were.

Formal Opinion

Respondent has suggested that the Board issue a precedential Formal Opinion in this

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[31] In *Harley-Davidson, Inc. v. Franchise Tax Board* (2015) 237 Cal. App. 4th 193, 212, fn. 11, the California Court of Appeal discusses the case law and notes that, while most state courts to consider the issue have found economic presence to be sufficient to establish nexus for taxes other than sales and use taxes, it would not reach the issue of whether physical presence was required because physical presence was established on the facts before it through the presence of subsidiaries acting on behalf of the taxpayer.

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matter if the Board does not reach the constitutional issues and resolves the appeal on other grounds (apparently referring to respondent's arguments regarding prospective enactment, consistency between inbound and outbound sales, and the standard set forth in the [Determination Letter).[32] Respondent states that there are many other matters presenting the same issue in the context of the throwback rule. As noted above, this appeal involves the interpretation of language in a Determination Letter regarding a throw-out rule, and both parties have raised arguments regarding the meaning and effect of the language used in the Determination Letter. The Board may wish to consider whether the fact this appeal involves arguments regarding the language and scope of a specific Determination Letter suggests that a Formal Opinion in this appeal may not be helpful to other taxpayers. The Board may also wish to consider whether any later appeals involving the throwback rule, rather than the throw-out rule, could present issues that are not anticipated at this time.

Additional Evidence

If either party has any additional evidence or exhibits to provide, staff requests that, pursuant to the Rules for Tax Appeals, Regulation 5523.6, such evidence be provided to the Board's Board Proceedings Division at least 14 days prior to the hearing, in order to facilitate a productive hearing.

Section 40 Matter

As noted above, this matter is subject to Revenue and Taxation Code section 40. Therefore, within 120 days from the date the Board's vote to decide the appeal becomes final, a written opinion (i.e., Summary Decision or Formal Opinion) must be published on the Board's website. (Cal. Code Regs., tit. 18, § 5552, subds. (b), (f).) The Board's vote to decide the appeal will become final 30 days following the date of the Board's vote, except when a petition for rehearing is filed within

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[32] Respondent should be prepared to address whether the issues it has raised regarding taxation of 100 percent of income ("no more and no less"), and consistency between inbound transactions under R&TC section 23101 and outbound transactions under R&TC section 25122, subdivision (b), and Regulation 25122, subdivision (c), might be more comprehensively addressed by the Legislature and/or by amendments to its regulation.

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that period.[33] (Cal. Code Regs., tit. 18, § 5460, subd. (a).)

Following the conclusion of this hearing, if the Board votes to decide the appeal, but does not specify whether a Summary Decision or a Formal Opinion should be prepared, staff will expeditiously prepare a nonprecedential Summary Decision and submit it to the Board for consideration at a subsequent meeting. (Cal. Code Regs., tit. 18, § 5551, subd. (b)(2).) Unless the Board directs otherwise, the proposed Summary Decision would not be confidential pending its consideration by the Board (Cal. Code Regs., tit. 18 § 5551, subd. (b)(5)); accordingly, it would be posted on the Public Agenda Notice for the meeting at which the Board will consider and vote on the Summary Decision.

A taxpayer may request that the Board hold in abeyance its vote to decide the appeal so the taxpayer may review the Board's written opinion prior to the expiration of the 30-day period for the filing of a petition for rehearing. If the vote is held in abeyance, the proposed Summary Decision will be confidential until it is adopted by the Board. (Cal. Code Regs., tit. 18, § 5551, subd. (b)(5).) Any request that the Board's vote be held in abeyance should be made in writing to the Board Proceedings Division prior to the hearing or as part of oral argument at the hearing. Any such request would then be considered by the Board during its deliberations on the appeal.

[33] If a petition for rehearing is filed, the Board's decision will not become final, and no written opinion under Section 40 will be considered until after the petition for rehearing is decided.

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