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Louisiana High Court declines to review ruling that foreign limited partner lacked nexus

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On March 2, 2012, the Louisiana Supreme Court declined to review an appeals court decision that held the passive ownership of an interest in a limited partnership that conducts business in Louisiana, by itself, was not sufficient to subject the foreign corporate limited partner to Louisiana franchise tax. In addition, the appeals court invalidated the Louisiana Department of Revenue's regulation interpreting the franchise tax imposition statute. [[UTELCOM, Inc. and UCOM, Inc. v. Department of Revenue](#), writ denied, La. Sup. Ct., No. 2011-C-2632, 3/2/12; [La. Ct. of App., Dkt. No. 535, 407, Division "D", 9/12/11](#)]

Statutory provisions at issue

LSA-R.S. 47:601, during the relevant periods, imposed a franchise tax upon all corporations, domestic or foreign, doing business in the state. A corporation was doing business in the state if it exercised any incident of taxation set out in the statute, including exercising its charter within the state or owning or using any part or all of its capital, plant or other property in the state in a corporate capacity. Reg. LAC 61:I.301(D) states that the mere ownership of property with the state, or an interest in property within the state, whether owned directly or through a partnership or joint venture or otherwise, renders the corporation subject to franchise tax in Louisiana since a portion of its capital is employed in the state.



Background facts

UTELCOM, Inc. and UCOM, Inc (collectively, the "taxpayers") are corporations organized under the laws of Kansas and Missouri, respectively ("foreign corporations" for purposes of Louisiana law). At all relevant times, the taxpayers did not engage in any business activities in Louisiana and had no physical or other presence in the state. Taxpayers (1) were not registered or qualified to do business in the state, (2) did not render any services to or for any affiliate, or to or for any other party in the state, (3) did not have employees, independent contractors, agents, or other representatives in the state, (4) did not buy, sell, or procure any services or property in the state, and (5) did not maintain any bank accounts in the state.

Taxpayers, as holding companies, owned limited partnership interests as passive investors in Sprint Communications Company LP, which was registered in Louisiana as a foreign limited partnership and conducted business in the state.

Taxpayers initially filed Louisiana Corporation Income/Franchise Tax returns for each of the relevant tax periods. Thereafter, the Department conducted an audit and assessed additional taxes due. Taxpayers filed a petition for recovery of all franchise taxes paid, denying that they were subject to the tax and claiming that the Department had improperly applied the franchise tax imposition statutes. The trial court ruled in favor of the Department, finding that the taxpayers owed the additional Louisiana franchise tax for the relevant periods. Further, the trial court found no issue with the Department's interpretation of the franchise tax imposition statutes.

Unreasonable interpretation

On appeal, the Department's main argument in support of its position that the taxpayers are subject to the franchise tax is based on its own regulation, LAC 61:I.301(D), outlined above. The court noted that the salient issue is "whether this regulation was a reasonable interpretation of the relevant statutory authority setting forth the bases for the imposition of Louisiana's corporate franchise tax, or was a prohibited expansion of the scope of the statute."

In reversing the trial court's decision, the court held that LAC 61:I:301(D) was an unreasonable interpretation of the franchise tax statute because it sets forth additional incidents of tax not present in the imposition statute. Specifically, the regulation attempted to subject a foreign corporation to tax merely because it owned or used part of its capital in the state indirectly through a limited partnership. The court found this to be an impermissible expansion of the statutory language. As such, the court reversed the trial court and entered judgment in favor of the taxpayers. The Department appealed the case to the Louisiana Supreme Court.

PwC Observes

"This decision may have applicability to other forms of pass-through entities," observes Robin Sigur, SALT Director with PwC in Houston, Texas.

"Under Louisiana law, an LLC is treated as a limited partnership for franchise tax purposes. Thus, out-of-state taxpayers with interests in Louisiana flow-through entities should determine their positions in considering whether to file refund claims," suggests Sigur.

"In addition, state law also provides that taxpayers that decide to pursue refund claims related to this issue most likely will have to file an appeal with the Louisiana Board of Tax Appeals or Louisiana District Court," explains Andrew Kim, SALT Partner with PwC in Houston.

LSA-R.S 47:1621 provides the statutory authorization for the Secretary to grant refunds of overpayments of tax. "Part F of this provision states "[t]his Section shall not be construed to authorize any refund of tax overpaid through a mistake of law arising from the misinterpretation by the secretary of the provisions of any law or of the rules and regulations promulgated thereunder. In the event a taxpayer believes that the secretary has misinterpreted the law or promulgated rules and regulations contrary therewith, his remedy is by payment under protest and suit to recover, or by appeal to the board of tax appeals in instances where such appeals lie."

"Historically, the Louisiana Department of Revenue has enforced LSA-R.S. 47:1621 (F) and denied refund claims in cases where its interpretation of the law has been incorrect, and the taxpayer has originally filed under the Department's mistaken interpretation, but later files an amended return with the corrected amount. As such, regardless of the Louisiana Supreme Court and Court of Appeals' decisions in *UTELCOM*, it is likely that the Department may deny refund claims related to this issue under LSA-R.S. 47:1621(F), and will require entities to appeal to the Louisiana Board of Tax Appeals or Louisiana District Court to obtain a refund," Drew explains.

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