SALT BUZZ HF

Is the Grass Any Greener After *Greenscapes*?

December 16, 2019

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We previously described the decision of the Tenth District Court of Appeals of Ohio ("Tenth District") affirming the Ohio Board of Tax Appeals' ("Board") decision upholding an assessment of Commercial Activity Tax ("CAT") against Greenscapes Home and Garden Products, Inc. ("Greenscapes"). *Greenscapes Home and Garden Products, Inc. v. Testa, 2019-Ohio-384* (February 7, 2019). That decision relied heavily on the fact that Greenscapes knew its products would be delivered to Ohio, that the situsing methodology for the CAT is consistent with other states, and that by selling to a national retailer, Greenscapes had purposefully availed itself of the Ohio market such that the imposition of the CAT was constitutional. The Ohio Supreme Court declined jurisdiction to consider the case on June 12, 2019. *06/12/2019 Case Announcements, 2019-Ohio-2261*. This Buzz describes some of the issues being considered in the aftermath of the Tenth District's decision.

At the Board, Greenscapes had acknowledged that it sold "products directly to its retail customers by providing its products at its Georgia location, loading it onto the customer's selected mode of transportation, i.e., pre-arranged truck, and providing a bill of lading to the truck driver indicating the ultimate "ship to" address. * * * the product becomes the property of its customers as it crosses appellant's dock to the truck." *Greenscapes Home and Garden Products, Inc. v. Testa,* BTA No. 2016-350 (2017). After the transfer of goods

to a truck, Greenscapes acknowledged that it no longer tracked the location of its product. The Board determined: "At the time appellant sold products to its customers, it knew their ultimate destination to be Ohio, based on its customer's orders and the bills of lading it provided to the drivers transporting the products. Our inquiry ends here, as did the commissioner's, in the absence of any evidence indicating that goods were ultimately received elsewhere." *Id.* Consistent with its determination that the situsing statute provided for destination situsing, the Board effectively determined that the fact that the taxpayer was not responsible for shipping the product and/or that title transferred outside of Ohio did not matter.

Knowledge of the Shipping Destination in Customer Pick Ups

The Board's conclusion, affirmed by the Tenth District, regarding knowledge of the destination could be problematic for some manufacturers and other sellers of tangible personal property. If bills of lading and/or other shipping information is provided (which is common), sellers will likely be deemed to have knowledge of Ohio sales. Further, many sellers of tangible personal property whose customers pick up or arrange transportation claim Public Law 86-272 protection in income tax states and may follow that non-filing approach in non-income tax states. Thus, such sellers may not have been filing in Ohio because they have no connection to Ohio other than goods that are initially shipped to an Ohio location.

Before a case can be appealed to the Board, the Appeals Division of the Ohio Department of Taxation ("ODT") issues a Final Determination ("FD") describing its position in the matter. The FDs are an indicator of the audits being conducted by ODT. A review of FDs issued by the Appeals Division, reveals a number of recent FDs with this fact pattern of non-filers with Ohio sitused sales of tangible personal property through customer or common carrier pick up of the goods out-of-state. This indicates that ODT has been successful in identifying non-filers with Ohio sitused sales of tangible personal property through customer or common carrier pick up of the goods out-of-state.

While it is more likely that out-of-state businesses whose customers pick up or arrange transportation are not filing in Ohio and other destination states, sellers that ship or arrange shipment of goods for their customers may not be filing in Ohio and may have similar issues regarding limited knowledge of the shipping destination. The considerations described below can be applicable in either situation.

Prospective Options For Out-of-State Sellers

Businesses that have a significant amount of goods shipped to an Ohio distribution center, which goods are further shipped outside of Ohio by the customer should try to obtain additional shipment information from its customers. Having discussions with customers can help the business understand the

information available and evaluate the quality of such information. Depending on the type of goods and the industry, the shipping information may be more specific and more readily available. For example, in some situations the customer may have information as specific as the goods final destination based on the stockkeeping unit ("SKU"). More commonly, businesses may not be able to obtain destination information after the distribution center or may not be able to obtain the shipping information specifically by product. The business can use the information to determine the amount of gross receipts potentially subject to CAT in Ohio and evaluate their options.

One option these businesses may consider is a voluntary disclosure agreement ("VDA") with ODT to limit prior exposure. These businesses may also consider the impact in certain home states, such as California that throwback sales from states where the taxpayer does not file in another state. The business may be able to request a refund in the home state for sales situsing to Ohio.

If the business is already under audit, the business may be able to use the shipping information from its customer during the audit to further settlement Alternatively, a business may use the discussion with its customers as a prospective planning opportunity in which the taxpayer reaches out to its significant customers and requests the ultimate destination be provided in a purchase order or within the shipping materials. This type of prospective planning can be used in conjunction with a VDA, for taxpayers under audit, or in situations where a taxpayer has been paying Ohio CAT based on an ultimate destination methodology that may not be fully supported by shipping records.

Where the information is not SKU or similarly specific, the taxpayer may ask the customer or logistics company to prospectively obtain a Qualified Distribution Center ("QDC") certificate. Vendors that ship goods to a QDC do not have to provide the specific destination of each good. Instead, the vendors merely pay CAT based on the QDC percentage certified by ODT for all the goods shipped through the Ohio QDC by all vendors. Because a QDC requires a fee and effort on the owner of the distribution center's part, the vendors may have to educate the customer on the CAT impact and the impact on the price of the product.

Potential Favorable Impact for Certain Out-of-State Sellers

The knowledge component of the decisions in *Greenscapes* can also be helpful to some taxpayers. If the only information available is shipping information to distribution centers and all or a portion of those distribution centers are outside of Ohio, the decisions suggest that the sales are situsued to the non-Ohio distribution center location even if the taxpayer believes that some of the sales will be further shipped to an Ohio store. In other words, the taxpayer is not required to situs the sales to Ohio if the taxpayer has no evidence

of their further shipment. It is also unlikely that ODT could provide evidence of where the goods were further shipped in such cases. Taxpayers should be cautioned that ODT has used the Ohio population ratio in some instances but typically in instances where no shipping information was provided. Taxpayers should reach out to their customers so they understand what shipping information could be available, in case ODT requests such information during an audit.

What is the Required Level of Evidence?

Because *Greenscapes* provided no evidence in support of the shipment of the goods from the initial Ohio location (a distribution center) to retail stores of its customers outside of Ohio, the decisions in *Greenscapes* do not provide guidance on the type of information that may be available or acceptable to support the ultimate destination of the goods. The taxpayer has the burden of showing in what manner and to what extent the tax commissioner's position in the FD is in error. In these situsing cases, the tax commissioner is typically relying on the bills of lading that reflect shipment to an Ohio distribution center.

In *Mia Shoes, Inc. v. McClain*, BTA No. 2016-282[1], the taxpayer arranged shipping to its customers' (i.e., national retailers') distribution centers in Ohio and nationwide. The taxpayer argued that its sale of goods should be sitused to the national retailers' stores where the goods were shipped after the distribution center, but the taxpayer did not have specific shipping information beyond its shipment to the national retailers' distribution centers. The taxpayer argued that the sales should be sitused based on the ratio of the national retailers' Ohio to non-Ohio stores, using publicly available information. The Board rejected the taxpayer's argument. The Board noted that the taxpayer acknowledged it lost visibility of where the goods were destined once they left the distribution center in Ohio. The Board held that the taxpayer had not "affirmatively proved" that the goods were ultimately received elsewhere within the meaning of the statute. Thus, a taxpayer must provide more specific evidence on the shipment of the goods from the distribution center to the stores than the taxpayer's estimate based on the ratio of Ohio to everywhere stores. One question is whether testimony from the customers or evidence such as a letter or document in support of the subsequent shipments would "affirmatively prove" the destination of the goods at the Board. For example, if the customers testified that the ratio of Ohio stores to total stores was consistent with the destination of the goods, perhaps the taxpayer would have satisfied its burden.

In a recent FD, ODT accepted notarized statements that the item that was sold and received in Ohio could not be legally used in Ohio and that it was all ultimately received at foreign locations. Thus, evidence that the goods are merely traveling through Ohio and won't be sold in Ohio may be acceptable during

[1] The case was appealed to the Ohio Supreme Court but was dismissed for want of prosecution on 11/14/2019.

audit or during litigation. This example suggests that testimony or a notarized statement may be accepted in some factual situations.

Time of Sale Requirement?

Another question is whether the taxpayer has to have knowledge of the ultimate destination at the "time of sale." This requirement can also be helpful or hurtful depending on the taxpayer's specific facts. ODT's policy is that the information must be available at the time of sale and ODT has typically accepted such information. R.C. 5733.033(E) does not contain such a requirement and the Board never referred to such a requirement in *Mia Shoes, Inc.*, which appears to have considered documentation obtained after the sale.

The Future?

One area that taxpayers may consider as a legislative change is having ODT apply an approach similar to the "for storage only" exemption available under the former Ohio personal property tax. The exemption allowed the use of estimates for purposes of determining which goods were ultimately destined outside of Ohio and that should, therefore, be exempt from Ohio personal property tax. Such an approach seems reasonable in these distribution center situations. Further, it could help Ohio further grow its role as one of the major locations for distribution centers.

If you would like to discuss this article, please contact Debora McGraw, Rich Farrin, or any of the other professionals at Zaino Hall & Farrin LLC.

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