

Allied Domecq: Nexus-Combined Reporting

Article By:

Stephen P. Kranz

In **Allied Domecq Spirits & Wines USA, Inc. v. Commissioner of Revenue**, the Massachusetts Court of Appeals held that the parent company of a **Massachusetts taxpayer** could not be included in the taxpayer's Massachusetts nexus-combined returns because the parent's nexus with Massachusetts was a sham. Regardless of the validity of the parent's presence in the state, an argument exists that the nexus limitation on filing combined returns as it existed during the tax years discriminated against interstate commerce in violation of the Commerce Clause.

The parent company, ADNAC, was incorporated in Delaware and headquartered in Canada. ADNAC carried substantial losses. Beginning in August 1996, ADNAC engaged in activities to create a Massachusetts presence, such as reimbursing an affiliate with Massachusetts nexus for the salaries of insurance and tax employees and renting Massachusetts office space from the affiliate to house the employees. Further, ADNAC's Massachusetts' affiliate transferred three internal audit department employees working in Massachusetts to ADNAC. For the years in question, 1996 – 2004, Massachusetts required corporations to have in-state nexus in order to file combined reports and share losses with affiliated entities. Mass. Gen. Laws ch. 63, § 32B. As a result of these transactions, the taxpayer believed ADNAC had established nexus with Massachusetts and included ADNAC in its Massachusetts combined returns.

The Massachusetts Court of Appeals held that, because of the sham transaction doctrine, ADNAC did not have nexus with Massachusetts for tax purposes and could not file on a combined basis in the state. The court ruled, in part, that the transactions involving insurance and tax employees were shams because two memos developed by the taxpayer's tax department described the plan as a "state tax planning project," indicated the favorable tax consequences of the transaction, and stated that the plan would have "no impact to the management results." The court viewed these communications as the taxpayer admitting that the transactions involving tax and insurance employees were conceived of entirely for tax planning purposes and for no business purpose. While the court could not point to any documents stating a tax purpose behind the movement of the internal audit department employees to Massachusetts, the court decided that because no contemporaneous records indicated a business motivation, the court would grant the use of the sham transaction doctrine.

Practice Note: The taxpayer did not argue that Massachusetts' requirement of in-state nexus to file on a combined basis discriminated against interstate commerce and violated the Commerce Clause. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977). Allied Domecq is similar to USX

Corporation v. Revenue Cabinet, Kentucky, in which a Kentucky Circuit Court declared that a provision of Kentucky's capital stock tax that limited to domestic corporations the ability to file on a combined basis or exclude investments in subsidiaries from its tax base discriminated against interstate commerce. *USX Corp. v. Revenue Cabinet*, No. 91-CI-01864 (Ky. Cir. Ct. 1992); see also Hellerstein & Hellerstein, *State Taxation* 4.14[3][j] (Thomson Reuters/Tax & Accounting, 3rd ed. 2001 & Supp. 2014-1). The court held that the law "clearly establish[ed] a taxing scheme which discriminate[d] against out-of-state businesses. It impose[d] a higher tax burden on non-domestic corporations than on similarly situated domestic corporations, thus creating a direct commercial advantage to local businesses." *Id.*; see also *South Cent. Bell Tel. Co. v. Alabama*, 526 U.S. 160 (1999). Similarly, the Massachusetts statute permitted the use of combined reporting and the accompanying sharing of losses to only companies with Massachusetts nexus. Much like as in *USX*, the requirement discriminated against non-domestic corporations by providing this incentive to only corporations with Massachusetts nexus and creating a direct commercial advantage to local businesses. Had this argument been litigated in *Allied Domecq*, the limitation may have been struck down, permitting corporations without Massachusetts nexus to file on a combined basis.

Allied Domecq Spirits & Wines USA, Inc. v. Commissioner of Revenue, 10 N.E.3d 178 (Mass. App. Ct. Jun. 18, 2014).

© 2025 McDermott Will & Emery

National Law Review, Volume IV, Number 197

Source URL: <https://natlawreview.com/article/allied-domecq-nexus-combined-reporting>