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THE STATE OF SOUTH CAROLINA
In The Court of Appeals

APPEAL FROM THE ADMINISTRATIVE LAW COURT

Ralph King Anderson, III, Chief Administrative Law Judge

Appellate Case No. 2024-000013
Administrative Law Court Case No. 19-ALJ-17-0416-CC

Tractor Supply Company, Appellant,

v.

South Carolina Department of Revenue, Respondent.

RECORD ON APPEAL
VOLUME II

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TABLE OF CONTENTS

VOLUME I

ORDERS

PLEADINGS

PRE-TRIAL MOTIONS

TRANSCRIPTS

VOLUME II

VOLUME III

VOLUME IV

VOLUME V

VOLUME VI

POST-TRIAL SUBMISSIONS AND MOTIONS

VOLUME VII

TRIAL EXHIBITS

VOLUME VIII

VOLUME IX

VOLUME X

VOLUME XI

CERTIFICATE

MS. MCKEOWN: I do.

COURT REPORTER: Thank you.

MS. MCKEOWN - DIRECT EXAMINATION BY MS. WOOTEN:

Q: Good morning. Could you please state your name for the record?

A: Marjorie Helen McKeown.

Q: May I call you Marjorie? Will that -- is that okay?

A: That's fine.

Q: Okay. I, I know that I'm gonna keep messing your name up.

All right. You served as the Tractor Supply 30(b)(6) designee in a deposition in June of 2022, correct?

A: That is correct.

Q: Okay. And at the time of your deposition, you were the Director of Tax and Incentives with Tractor Supply Company, correct?

A: That is correct.

Q: And is that still your position today?

A: That is still my position.

Q: Okay. All right. Let's talk about Tractor Supply Company and it's subsidiaries. I'm gonna refer to Tractor Supply Company as TSC. I'm gonna refer to Tractor Supply of Texas as the Texas entity. And I'm gonna refer to Tractor Supply Company Michigan as the Michigan entity.

A: Okay.

Q: Do you understand those parameters that I've just set?

A: You're referring to TAC as the TAC parent?

Q: Yes.

A: Okay.

Q: That is correct.

A: Yes.

Q: If you have any questions, please ask me. If you need any clarification on that.

A: Okay.

Q: All right. TAC, Tractor Supply Company the parent, they have retail operations in all states except Texas, Michigan, Utah and Hawaii?

A: And Alaska, 'cause we're not in Alaska yet.

Q: But in the states they do operate in, Tractor Supply Company the parent, operates the retail operations for all of the 48 States -- 49 States with the exceptions of the ones that I just had mentioned?

A: Yeah, I ---

Q: Texas, Michigan, Utah and Hawaii?

A: Correct.
Q: Okay. All right. If you will look at the first page of Joint Exhibit 4.
MS. WOOTEN: Ms. Buckner, may we have the ---
MS. BUCKNER: Yes.
MS. WOOTEN: --- computer, please?
MS. BUCKNER: (Whispering) let's see.
Q: All right. This is Joint Exhibit 4, do you recognize this Exhibit?
A: I do.
(Joint Exhibit Number 4 was introduced into the record at this time.)
Q: Okay. And it's an org chart of the Tractor Supply entities, correct?
A: It is.
Q: Okay. And it shows Tractor Supply as the parent company, correct?
A: Correct.
Q: And Tractor Supply is the Taxpayer in this matter, correct?
A: Correct.
Q: Okay. Tractor Supply Company is the only Tractor Supply entity that files a 10-K, correct?
A: It's a -- it files it in the name of its, you

know, it's group, it's name.
MS. WOOTEN: (To Ms. Gamble) it's okay.
Q: Just for clarification, Tractor Supply of Texas does not file a 10-K?
A: It does not.
Q: And Tractor Supply of Michigan does not file a separate 10-K.
A: Correct.
Q: Okay. All right. So let's look at Tractor Supply's 10-K. That should be Joint Exhibit Number 6.
MS. WOOTEN: (To Ms. Gamble) and if you'll go to PDF page 15. I apologize, it's 3.
Q: Sorry. It's Joint Exhibit 3.
A: Oh, that's all right.
Q: I was looking at the tag she wrote.
All right. Do you recognize this Annual Report and 10-K?
(Joint Exhibit Number 3 was introduced into the record at this time.)
A: Not this specific one, but I recognize it as being an Annual Report ---
Q: Okay.
A: Yes.
MS. WOOTEN: (To Ms. Gamble) and if you'll go to

page 15. 15 in the PDF. Okay. Right there, stop.

Q: All right. And in Tractor Supply's own words, it is the largest operator of, operator of rural lifestyle retail stores in the United States, right?

A: Yes.

Q: Okay. All right. Let's back up and talk about a 10-K. It's an Annual Report that is required to be filed by the U.S. Securities and Exchange Commission for publically traded companies, correct?

A: Correct.

Q: All right. And it's a detailed summary of the Company's financial statements?

A: Correct.

Q: Okay. And Tractor Supply Company publishes their Annual Report and 10-KS on their website?

A: Correct.

Q: Okay. And it also publishes other financial information on its website, correct?

A: It does.

Q: Okay. So, stock information?

A: Yes.

Q: Okay. It also publishes 10-Qs, or quarterly

reports?
A: Yes.
Q: Okay. 10-Qs are also required to be filed by the U.S. Security and Exchange Commission, correct?
A: I believe so.
Q: Okay. And quarterly reports are done in three-month summaries, whereas Annual Report 10-KS are done in 12-month summaries?
A: Correct.
Q: Okay. Other information -- financial information Tractor Supply Company files on their website are earnings calls, correct?
A: I am not sure on that piece, if they're on there. Unau- -- I'm unsure on that piece.
Q: Okay.
MS. WOOTEN: (To Ms. Gamble) If you will pull up TractorSupplyCompany.com?
Q: And while she's pulling that up, earnings calls are conferences or webcasts were TSC discusses a particular financial document such as a 10-Q, correct?
A: Yes. Information that, you know, would've been applicable to the quarter report.
Q: Okay. And they also have earnings calls for

10-Ks as well, correct?
A: Yeah. It would've been that -- just that quarter, you know, thing for the quarter.
Q: Okay.
MS. WOOTEN: (To Ms. Gamble) if you'll scroll down to the bottom.
Q: Do you agree that we are on Tractor Supply Company's web page?
A: Yes.
Q: Okay.
MS. WOOTEN: (To Ms. Gamble) if you'll scroll down all the way to the bottom. And go up a little bit, and there is a link for investor relations. If you'll click on that tab -- or that link, right there. All right. And if you will just hover over investor relations at the top, don't click anything. And go down to events and presentations. And scroll down just a little bit. Keep going. Keep going. Okay.
Q: On the screen is a Annual Investment Conference from 2022. And there are also Tractor Supply Company's earnings conference call listed on this web page as well, correct?
A: It appears so, for this year.
Q: Okay.

MS. WOOTEN: (To Ms. Gamble) so if you'll click up at the top of the box, there's a 2022. Okay. Up. Click on that. All right. And go down to 2018.

Q: And you would agree that Tractor Supply publishes earnings calls and conferences -- conference presentations all the way back to 2018 on its website, correct?

A: Can we click into that next link?

Q: Sure. And you would agree that they have published information about earnings calls on their website?

A: It appears that there is a link that would've possibly -- could've had information, but I can't tell if there's anything there, or if anything was ever included there.

Q: Okay. That's fine. Same thing for conference calls -- or excuse me ---

MS. WOOTEN: (To Ms. Gamble) if you'll go back one page.

Q: --- for presentations?

MS. WOOTEN: (To Ms. Gamble) go back one more page -- or, stay right there.

Q: That Tractor Supply also publishes, and you'll see the webcast PDF sign on the side, that

Tractor Supply also publishes investment conference webcast on its website?
A: It looks like it does so for 2022.
Q: Okay. All right. Thank you. All right. I'm gonna hand you a few exhibits.
MS. WOOTEN: Your Honor, may I approach the witness?
THE COURT: You may.
A: Thank you.
Q: You're welcome.
(Whispering.)
Q: I've handed you a document that has been marked Respondent's Exhibit 5. Could you tell me what the name of that document is?
A: Tractor Supply Company NASDAQ GS: TSCO, Fiscal Quarter for 2016, Earnings Call Transcripts.
Q: Okay. And fiscal year 2016 is a issue -- is a year at issue in this case, correct?
A: 2016 is a year in issue, yes.
Q: Okay.
THE COURT: Tractor Supply's in the NASDAQ?
MS. MCKEOWN: We trade.
(*Whispering*.)
Q: All right. I'm gonna ha- -- hand you another exhibit that's been -- this is the full copy of the earnings report. What you have is just a

selected portion.

All right. In Respondent's Exhibit 5, if you'll turn to page three, there's several participant names listed on that, that document, correct?

A: Correct.

Q: Okay. And the fifth one down is Steve Barbarick?

A: Correct.

Q: Okay. And what is his position?

A: He's the Chief -- well, President and Chief Operating Officer.

Q: Of what company?

A: I believe, I believe Tractor Supply Company, but it could've been Tractor Supply Company of Texas.

Q: Okay.

A: It has flipped over the years.

Q: If you'll flip to page 21 in that document. Mr. Barbarick's statement begins at the top of that page, correct?

A: Yes.

Q: Okay. And if you'll flip to page 23, he has another statement that begins at the bottom of page 23, correct?

A: There's a couple statements on here, but -- it appears that there's a couple statements from him on this page.
Q: Okay. And if you'll flip onto page 24, his statement continues onto 24, correct?
A: Yes, that statement from before continues onto page 24.
Q: Okay. Thank you. I'm gonna grab those -- or -- yeah. We'll leave the, the marked one up there, but I'll get this one back from you.
A: Okay.
Q: All right. I'm gonna hand you another set. This has been marked as Respondent's Exhibit 6. It's selected pages, but I'm also gonna -- I'll hand you the entire Exhibit.
All right. Same thing, looking at it -- Respondent's Exhibit 6, can you tell me the title of this document?
(Respondent's Exhibit Number 6 was introduced into the record at this time.)
A: Tractor Supply Company NASDAQ GS: TSCO Company Conference Presentation.
Q: And it's dated November 18th, 2015, correct?
A: Correct.
Q: And the year at issue in this case is 2015,

correct?

A: Correct.

Q: All right. If you'll turn to page three, there's several participants listed down there. The second one down is Gregory Sandfort, correct?

A: Correct. Gregory Sandfort.

Q: Sandfort. And what is his position?

A: He's the CEO, and was a Director.

Q: Of?

A: The Board.

Q: Which company?

A: Tractor Supply Company.

Q: Okay. If you'll flip to page four.

A: Sorry, there's a little stickiness going on here.

Q: It's all right.

A: Okay.

Q: All right. If you'll -- at the bottom of this page, Mr. Sandfort's statement begins, is that correct?

A: It appears so, yes.

Q: And if you'll flip to pages five and six, his statement continues onto those two pages?

A: Yes.

Q: Okay. Thank you. I need -- so we can have -- yes, just that one. And if you'll leave that one up there, please. Thank you.
All right. Let's go back and talk about Tractor Supply Company. It is loc- -- the headquarters are located --
MS. GEER: I apologize, Your Honor. I just want to make sure I understand. Have -- are you getting tho- -- trying to move those into evidence now, or?
MS. WOOTEN: Not now.
MS. GEER: Okay.
MS. WOOTEN: I just gave her that and got mine back.
MS. GEER: Got it. Thank you.
MS. WOOTEN: Thank you.
Q: Back to Tractor Supply Company. The headquarters are located in Brentwood, Tennessee, correct?
A: Yes, the Store Support Center.
Q: Store Support Center. Okay. And the Store Support Center provides management, or administrative services to the related entities or affiliates out of tran- -- Tractor Supply Company, correct?
A: It provides, kind of, back-office operations

management to Tractor Supply Company and its affiliates, yes.
Q: Okay. And the Store Support Center does not provide those same type of services to any entity outside of Tractor Supply's subsidiaries or affiliates?
A: Correct.
Q: Okay. And 99 percent of Tractor Supply Company's revenue is derived from its retail operations, correct?
A: That's correct.
Q: Okay. And the remaining one percent comes from interest or miscellaneous income, like recycling pallets or rental income?
A: That's correct.
Q: Okay. And you agree that this remaining income is inconsequential?
A: It's immaterial to the bigger piece, yes.
Q: Okay. During the audit period, Tractor Supply Company operated up to fift- -- or, excuse me, 42 retail stores in South Carolina, correct?
A: That sounds about right, yes.
Q: Okay. And Tractor Supply Company will lease it's employees to the Michigan entity?
A: It does.

Q: Okay. Tractor Supply Company does not lease any other employees to any other Tractor Supply entity, correct?
A: That is correct.
Q: And that also includes -- Tractor Supply does not lease any employees to any outside entity, meaning outside of the Tractor Supply Company subsidiaries or affiliates?
A: That's correct.
Q: Okay. All right. Let's talk about Michigan. The Michigan entity has retail operations in, in the State of Michigan only, correct?
A: That is correct.
Q: And we just talked about the leased employees from the parent company. 95 to 99 percent of Michigan's third party revenue comes from the customers and retail stores, correct?
A: Correct.
Q: Okay. And Michigan did not have any officers, executives or directors during the audit period, correct?
A: That is correct.
Q: Okay. All right. Let's move to the Texas entity. The Texas entity has retail operations in Texas only, correct?

A: That is correct.
Q: Okay. It also has a distribution center, correct?
A: Distribution center and a couple mixing centers, yes.
Q: I'm gonna get to that.
A: Oh, sorry.
THE COURT: And a couple of what?
A: Mixing centers.
MS. WOOTEN: She's jumping ahead, Your Honor.
A: Sorry.
THE COURT: Okay.
(*Laughter*.)
Q: All right. It has one distribution center, correct?
A: That is correct.
Q: All right. It also has several mixing centers?
A: That is correct.
Q: Okay. Can you please describe what a mixing center is?
A: It's considered a cross-stop facility. It is a -- kind of, like a mini DC, but it carries certain types of products in, in order to kind of streamline getting those, kind of, products to the store. Also to help with inventory

storage constraints at the stores. We have a small backroom, so it just allows us to get inventory there quicker, but they're very very small focused DC's if you want to -- if you will.

THE COURT: And a DC is a what?

A: DC is a distribution center.

THE COURT: Okay. There's -- so it's -- okay.

Q: Texas's distribution center also serves retail stores outside of Texas, correct?

A: It does.

Q: Okay. All right. So now, let's -- we've talked about Texas retail operations, we've talked about the Texas distribution center, now let's talk about the procurement function or service.

All right. Texas provides procurement function -- the procurement function for all Tractor Supply entities, correct?

A: Mostly.

Q: With the exception of Petsense?

A: With the exception of Petsense.

Q: Okay. So -- let's go back. Tractor Supply Company retail operations, Michigan retail operations, and Texas retail operations, the

Texas entity provides procurement services for those three entities?
A: For the TSC operations, you know, held by those -- or done by, kind of, TSC of Michigan and Texas.
Q: All right. Let's back up and talk about Petsense real quick. Petsense was acquired by Tractor Supply Company in the last quarter of this audit period, correct?
A: Correct.
Q: Okay. All right. Going back to the procurement service ---
THE COURT: The last quarter of ---
MS. WOOTEN: The aud- ---
THE COURT: --- this audit period, which would be what?
A: 2016.
MS. WOOTEN: The audit period ---
THE COURT: Their ---
MS. WOOTEN: --- in this matter is fiscal year '14 -- 2014, 2015, and 2016.
A: That is correct.
Q: So Petsense would've been acquired the last quarter of 2016?
THE COURT: There you go.

A: That is correct.

THE COURT: That's what I'm wondering.

Q: The procurement service or function identifies and sources products for the group, is that correct?

A: Yeah. That's some of its activities, yes.

Q: Okay. And it's determining which products to buy and where those are gonna come from, that's what sourcing is?

A: Correct.

Q: Okay. It also has a Product Development Team?

A: Yes.

Q: Okay. And Texas does not provide any procurement services to any entity outside of the Tractor Supply Group?

A: That is correct.

Q: And the procurement employees are referred to as buyers, correct?

A: Some are.

Q: Okay. The procurement employees are physically located in the Store Support Center in Tennessee?

A: Correct.

Q: Okay. But you would agree that, even though some of those procurement employees are referred to as buyers, they -- you are all considered "team members, because we're all part of one team"?

A: Yes.

Q: Okay. All right. And the procurement team predominantly works with third parties in Asia to serve -- source certain products, correct?

A: Not predominantly, but it does work with third parties in, in Asia to source certain products.

Q: If you'll bear with me just a second.

(*Whispering*.)

MS. WOOTEN: Your Honor, I need to use -- would like to use a deposition transcript. I can rip open the sealed copy or I can provide her one of our copies.

MS. GEER: It doesn't matter to me.

MS. WOOTEN: Okay. May I approach her with -- (to Ms. Geer) I mean, I'm happy to let you inspect it, if you'd like to?

MS. GEER: Okay. I'll, I'll pull it up myself.

MS. WOOTEN: Okay.

Q: All right. I'm gonna hand you this large notebook. I'm sorry. I don't mean to get in your space. All right.

If you will look -- we talked earlier, you were deposed in June of 2022 as a 30(b)(6), is that correct?

A: I think it was June, May, sometime that -- yeah.

Q: You can flip to the front page of -- no, wait, wait, wait. Let me ---

A: Sorry.

Q: --- get them straight. Here we go.

A: Okay.

Q: Do you agree ---

A: June.

Q: June of 2022. And you were deposed in the capacity of a 30(b)(6) witness, correct?

A: That is correct.

Q: Okay. If you'll look at page 72.

A: Yes.

Q: And if you'll look at lines 18 through 21. And we were just talking about -- the question I asked was, the procurement team predominantly works with third parties in Asia to source certain products, correct? If you will read lines -- well, let me ask you. Do you -- if you'll read that to refresh your memory.

A: Can I read above just to make sure I got the proper ---

Q: Sure.
A: --- context ---
Q: Of course.
A: --- in my response?
Q: Sure.
A: (Reviews document.)
MS. GEER: And I apologize, Nikki. Can you tell me the page and line on that again?
MS. WOOTEN: 72, page number. Line 18 through 21.
A: So the sentence -- can I read the sentence before that?
Q: Yes.
A: Some of it is not just domestically, but also looking for vendors globally to source that product. So in that context, working with third parties predominantly in Asia ---
Q: Okay.
A: --- makes sense.
Q: All right. Thank you. I'll grab that from you. Or, just leave it there.
All right. So those products that are sourced from Asia have to be shipped to the United States for placement in Tractor Supply retail stores, correct?
A: Yes.

Q: And Tractor Supply purchases insurance on that inventory that's shipped from Asia to the United States, correct?
A: Yes.
Q: Or goods that are purchased from a vendor outside of the United States, correct?
A: Correct.
Q: All right. And that insurance is referred to as Marine Cargo insurance, correct?
A: I believe so.
Q: All right. And Tractor Supply keeps records of its insurance policies on inventory, correct?
A: I believe so.
Q: And as part of the 30(b)(6) Deposition, Tractor Supply Company provided a copy of its Marine Cargo insurance to -- coverage, correct?
A: Yes.
Q: And you've seen a copy, and we talked about it during your deposition, correct?
A: Yes.
Q: All right. All right. I'm gonna hand you what's been marked as Respondent's Exhibit 10.
THE COURT: Mr. Luther, we've been talking about tax stuff.
(*Laughter*.)

MR. LUTHER: Riveting.
MS. WOOTEN: (To Ms. Geer) there you go. I'm sorry. I didn't realize that was stapled. Excuse me. Would the Court also like a copy to look at while we're discussing this?
THE COURT: No.
MS. WOOTEN: No, okay. I'll leave that right there.
THE COURT: Trying to get this ...
MS. WOOTEN: Your Honor?
THE COURT: Yeah, go ahead.
MS. WOOTEN: Okay.
(*Whispering*.)
THE COURT: Yeah, you could put it on the Elmo.
MS. WOOTEN: Okay. Or, do you have it pulled up?
THE COURT: That'll take care of it for all of us.
MS. WOOTEN: Oh, I think Jennifer's got it on ---
MS. BUCKNER: Okay. She's got in on there ---
MS. WOOTEN: --- electronically.
MS. BUCKNER: --- I can -- got it.
MS. GEER: Nikki, I just have a question. So is this ---
MS. WOOTEN: Yeah?
MS. GEER: --- is this a Joint Exhibit?
MS. WOOTEN: It is not.
MS. GEER: Is it ---

MS. WOOTEN: It's one of the ones you objected to.
MS. GEER: Oh, okay. Thank you.
MS. WOOTEN: You're welcome.
(Respondent's Exhibit Number 10 was introduced into the record at this time.)
Q: All right. During the deposition we talked about the Marine Cargo Insurance Policy, correct?
A: I believe so.
Q: Okay. And again, we received a copy of this insur- -- or this Policy from Tractor Supply in discovery, correct?
A: Correct.
Q: Okay. And do you confirm that insurance policies related to Marine Cargo insurance is term -- quote, term for insurance for regarding our inventory, correct?
A: Correct.
Q: And that's the general type of goods sold by Tractor Supply Company in their retail stores, correct?
A: Correct.
Q: And those retail stores include Texas and Michigan, correct?
A: Correct.

Q: Okay. All right.

MS. WOOTEN: At this time, Your Honor, we -- the Department would offer Respondent's Exhibit 10 into evidence?

(Respondent's Exhibit Number 10 was offered into evidence.)

MS. GEER: No objection.

THE COURT: It's admitted.

(Respondent's Exhibit Number 10 was admitted into evidence.)

MS. WOOTEN: Thank you.

Q: All right. And on this policy, Tractor Supply Company is listed as the assured, correct?

A: Correct.

Q: And the parent company pays the insurance premium on this insurance policy, correct?

MS. WOOTEN: You can scroll -- it's either on that page or the next page.

A: All right. I have one page.

Q: You only have one page?

A: Yeah.

Q: I -- my apologies. I'm not sure what happened. There we go.

A: Thank you.

Q: You're welcome.

A: I'd assume that we paid for it -- or trac- -- Tractor Supply Company paid for it.
Q: Okay. And you would agree that Tractor Supply Company is the largest buyer of inventory and not Texas, correct?
THE COURT: Say that again, so I can ...
MS. WOOTEN: Sure.
Q: TSC the parent company, is the largest buyer of inventory and not Texas ---
THE COURT: Okay.
Q: --- correct?
A: Tractor Supply Company of Texas is the larger buyer -- I mean, they buy all of our inventory.
Q: Okay. If you will turn to page 131 in the deposition.
MS. GEER: Nikki, can you say that again? 131?
MS. WOOTEN: Sure. Page 131.
MS. GEER: Okay.
(Whispering.)
Q: Are you there yet, page 131?
A: Yes.
Q: Okay.
A: Yes.
Q: In lines 17 and 20?

A: Right.
Q: And I'm gonna open the deposition transcript. This may be easier if I gave you this.
A: Oh. I didn't mean to -- I'm right there with you.
Q: Okay.
A: Yep.
Q: I'd prefer to have my book though.
Gotcha. Excuse me, thank you.
A: What page was that again, please?
Q: Sure. 131.
A: Of -- would it ... Which -- oh, sorry. Line 7.
Q: That's okay.
THE COURT: So that document is the deposition?
MS. WOOTEN: Yes, Your Honor.
THE COURT: Hope it includes exhibits.
MS. WOOTEN: It does.
THE COURT: Looking at the thickness of it.
MS. WOOTEN: These are all the depositions, Your Honor.
THE COURT: Oh, those are all of them?
(*Laughter.*)
MS. WOOTEN: These are all of them. This is not just one deposition.

(*Laughter.*)

MS. GEER: Margie might not be here if her deposition was that long.

(*Laughter.*)

A: All right. 131, you say?

Q: Uh-huh.

A: Okay.

Q: And if you'll start with line 17. If you can read -- well, 17 through 20, just to refresh your memory?

A: I feel like I'm not on the same page as what I was looking in your book.

Q: Page 131.

A: Which is where I'm at. Does that look like the same?

Q: That does not look like the same.

A: Okay. That's what I ...

Q: That is concerning.

A: Yeah. It looks like the same section is still -- but.

Q: All right. Let me see. Yeah, that is concerning. So we'll get back to that soon.

MS. WOOTEN: Do you have 131 beginning with question; all right?

MS. GEER: 131.

MR. STREISEL: Yes. Well, I do. That line.
MS. GEER: I guess -- yes, I do too.
MS. WOOTEN: That is not the beginning of that page over there.
MS. GEER: Uh oh.
Q: All right. So, I'm gonna give you this one.
THE COURT: Well, now what is this one?
MS. WOOTEN: I'm sorry. This, this is a -- the condensed version of her transcript from the deposition.
THE COURT: Okay.
MS. WOOTEN: This is the -- supposed to be the full and original. Oh, okay. (Whispering) I think that's what happened.
Q: Okay. All right. If you'll begin with line 17 and read 17 through 20?
A: I can.
Q: Okay.
A: But the context is the same. I will have that same request, to be able to go back and look at ---
Q: Okay.
A: --- the context.
THE COURT: So the record will be clear, we're reading the condensed version of the transcript

on page 131?

MS. WOOTEN: Yes, Your Honor. Thank you.

THE COURT: Okay.

A: And TSC would be probably the largest buyer, you know, when you think about the user of the, of the products, that would make sense to me.

But, to clarify?

Q: Sure.

A: We were just talking and -- or I had just been saying that Texas has bought the goods and it comes -- when it comes time to ship -- the logistics part of that -- of that amount -- or, I'm sorry, I -- I'll say the exact sentence. It comes time to ship the, the logistics part that, you know, that -- that's on, you know -- gosh -- I guess, the buyer at that point.

Tractor Supply Company of Texas is the buyer, but then the -- there's intercompany buyers, you know, underneath that, and that's -- of the group, TSC would be the largest, kind of, next-level buyer when you break it down. Tractor Supply Company of Texas buys it all, so then we think we'd buy the most of that -- well, I guess, the fraction, TSC would represent most of the inventory.

THE COURT: I don't think I followed all that.
(Laughter.)
A: What, what exactly ...
THE COURT: Well, if I didn't follow it, I don't think I can explain what I did not follow. But, I ---
A: Tractor ---
THE COURT: So you've got -- Tractor Supply of Texas, you're saying, buys most of the inventory?
A: They buy all of the inventory.
THE COURT: All of the inventory.
MS. WOOTEN: All right.
THE COURT: And then, then they filter that inventory down to Tractor ---
A: So they, they, in turn, then sell that to ---
THE COURT: Tractor Supply ---
A: --- Tractor Supply Company and ---
THE COURT: --- who ---
A: --- Tractor Supply Company of Michigan.
THE COURT: Well, if Tractor Supply is predominantly the ma- -- the major part of the Company, what -- what does Michigan do again?
A: Retail stores.
THE COURT: Okay. But only in Michigan?

A: But only in Michigan.
THE COURT: So what you're really saying is, Tractor Supply of Texas buys all of the inventory, it funnels that inventory to either, the rest of the retail stores through Tractor Supply or the inventory that would go to Michigan through Tractor Supply of Michigan?
A: Tractor Supply Company of Texas buys all inventory for the TSC entity -- you know ---
THE COURT: Yeah.
A: --- retail store entities, which includes Tractor Supply Company of Texas. It has its own retail stores as well as Tractor Supply Company the parent, and Tractor Supply Company of Michigan.
THE COURT: So was my question wrong or right?
A: Could you repeat the question, please?
THE COURT: Okay. One more time. Tractor Supply of Texas buys all of the inventory, that inven- -- once they buy all of that inventory, that inventory either goes to Tractor Supply for all of the nation except Tractor Supply of Michigan, of which, that inventory goes solely to Michigan?
A: Almost correct.

THE COURT: Almost. Well, I don't ---

A: A portion, a portion of the inventory that Tractor Supply Company of Texas procures stays with Tractor Supply Company of Texas ---

THE COURT: Oh ---

A: --- for the retail stores that it has.

THE COURT: But it still could -- okay. 'Cause it -- that -- but that's still going to Tractor Supply, it's just going to the stores in Texas?

A: No. Tractor Supply Company of Texas has its bri- -- it actually owns the ref- -- or has, not owns in all cases, I mean, it's -- sometimes it's a lease, but, but the locations in Texas belong to Tractor Supply Company of Texas.

THE COURT: Okay. And that Company also provides other services that were referenced earlier?

A: The distribution center.

THE COURT: Oh, okay. So it -- Tractor Supply of Texas has its general functions for all the facilities, and then the retail stores just for Texas, is that right?

A: Tractor Supply Company of Texas has the -- these related inventory procurement functions, it has a distribution center and the mixing centers, and the retail stores operations.

THE COURT: I got it. Go ahead.

Q: All right. Jumping back to procurement. We're still talking about Texas being the procurement service and function that it provides.

They have -- Texas' responsibility has -- they have responsibility for pricing decisions related to the inventory split between Texas and Tractor Supply Company the parent, correct?

A: Could you repeat your question, please?

Q: Sure. Responsibility for pricing, the pricing team, responsibility for pricing inventory of Tractor Supply inventory falls between Tractor Supply Texas and Tractor Supply Company the parent company?

A: Yeah. It's a shared, kind of, collaboration that the, the buyers -- I guess, the merchants of Tractor Supply Company of Texas ultimately sets the prices that is advised by the pricing team that -- which is the parent.

Q: The pricing team advises based on zones, correct?

A: Correct.

Q: But the pricing team advises all the zones within Tractor Supply Company?

A: It would provide feedback on them.
Q: Okay. And you agree that retail store managers can ultimately set pricing in their retail stores, correct?
A: In limited circumst- -- in certain -- limited, certain circums- -- I can't speak -- situations (laughter).
Q: But they can, again?
A: When it gets to a point of clearancing or moving some, like, flow -- moving inventory for next season, that type of thing.
Q: All right. The Texas entity also holds the intellectual property trademarks for Tractor Supply Company, correct?
A: It holds the trademarks, yes.
Q: Okay. And it does not charge any of the related entities for use of the intellectual property?
A: Correct.
Q: Okay. It could, but it chooses not to charge them?
A: That is correct.
Q: All right.
THE COURT: So, where I could be clear on what you said awhile ago. When you say that Tractor

Supply of Texas, it sets pricing and that it does it zone areas, the local retail store can set its own prices. But it doesn't really set the initial price, is what it sounded like to me, that they can later adjust those prices for clearance purposes and other type reasons?

A: Correct. So after a point of time, you know, there may, there may be -- there's a classification, I can't remember exactly what it is, but I think it's like code 13, it's when -- it's a term used when we're ready to basically get rid of that inventory. It's not moving anymore or maybe it's just slow, maybe it's the change of the season.

THE COURT: Yeah.

A: And at that point, the store manager has the, you know, has the ability to start changing the pricing in its store. But up until that point, it's not something that they can control.

THE COURT: So, you use a code 13 for the inventory of which you've had bad luck?

A: Maybe, not the ---

THE COURT: I was just -- I'm just kidding you.

A: Yeah.

THE COURT: 13 and bad luck.

(*Laughter.*)

A: (Laughter.)

Q: Okay. I neglected to ask this earlier, so let's, let's go back and talk about this.

All Tractor Supply entities are owned 100 percent either, directly or indirectly, by the parent company, Tractor Supply Company?

A: That is correct.

Q: Okay. Michigan is owned 100 percent by Tractor Supply Company?

A: Yes, that's correct.

Q: Okay. Texas is a limited partnership and Michigan owns 99 percent and TSC owns one percent?

A: That is correct.

Q: Okay. All right.

All right. So let's talk about the retail stores, the typical retail, retail stores, and this is across the nation. There is a standardized retail store format for efficiency purposes, correct?

A: What format are you referring to?

Q: Let's go back to your deposition. I think -- let's see ... All right. Before that, let me -- well, let's see if I can bring this up.

Tractor Supply retail stores on average have the same square footage of approximately 19,000 square feet?

A: On average.

Q: Okay. And Tractor Supply's inventory is generally the same across all retail stores with the exception of, maybe, some geographical differences such as snow plows or horse farming, things of that nature, but general merchandise is across the board at all retail stores?

A: Generally, you would have this -- you know, a similar type of array or assortment, but that can vary based on size of the store volume and the geographical.

Q: All right. And Tractor Supply's signage at the store is generally the same with the exception of maybe some local ordinances?

A: Correct.

Q: Okay. And employees must wear the same or similar red aprons with name tags, correct?

A: Correct. Correct.

Q: And this is across all Tractor Supply retail stores?

A: Correct.

Q: Okay. So with that in mind, I think that, that this was the lead up to that. The inventory, the signage, the square footage of the stores, the layout, Tractor Supply has a general standardized retail store for, quote, efficient purposes?

A: Yes.

Q: All right. Let's talk about gift cards. When a customer purchase a gift card, he can use that gift card at any Tractor Supply retail store, correct?

A: Yes.

Q: Okay. So you could purchase a gift card in South Carolina and use it at a Texas retail store?

A: Correct.

Q: And you could purchase a gift card in South Carolina and use that at a Tractor Supply retail store in Michigan?

A: Correct.

Q: All right. Same thing with returns. If a customer purchased an item from a South Carolina retail store, they could return that same item to a Texas retail store, correct?

A: That is correct.

Q: All right. And if a customer purchased in a -- in South Carolina, purchases an item, they can return that same item to a retail store in Michigan, correct?
A: Yes.
Q: Okay. All right. Let's move on to the intercompany transactions in this case.
Tractor Supply entities rely on related entities for necessary business functions, correct?
A: Rely? More -- probably, the word would be, uses.
Q: Okay. Well, we'll talk about that in a minute. And these transactions relate to leasing of employees, correct?
A: Okay.
Q: It's a yes or a no.
A: You said Tractor Supply Compan- -- can you repeat the question one more time? I'm sorry.
Q: Sure. The intercompany transactions that we're gonna be discussing today, one of them relates to leasing of Tractor Supply employees, correct?
A: That is correct.
Q: Okay. And one of them also relates to

administrative or management services, correct?
A: That is correct.
Q: One of them relates to procurement functions or services?
A: Yes.
Q: And there is also an agreement that relates to licensing of trademarks, correct?
A: Correct.
Q: All right. And Tractor Supply Company entities could not operate without those services or functions provided by the other entities, correct?
A: Not correct. It could function by use of, you know, external third parties to provide those functions, but we choose to use our services.
Q: Tractor Supply Company has to have those functions, correct ---
A: You hav- ---
Q: --- in order to operate?
A: In order to operate, you have to have those functions.
THE COURT: Ms. Wooten, do you have to have trademarks to operate? It may not be wise, but ---
MS. WOOTEN: I don't think it would be wise not to,

but.

THE COURT: Well -- yeah, but ---

MS. WOOTEN: That might be the busi- ---

THE COURT: --- your question was, have to.

MS. WOOTEN: That's a business que- -- that's a business question.

THE COURT: Okay.

Q: All right. And Tractor Supply Company documents these services or functions through intercompany agreements, correct?

A: Yes.

Q: All right. So let's talk about the leasing agreement.

You've testified that Michigan leases employees from the Tractor Supply Company, the parent company, correct?

A: Correct.

Q: And there's an agreement that specifies the terms of that transaction ---

A: Yes.

Q: --- correct?

A: Correct.

Q: And that agreement was in effect during the audit period in this case, correct?

A: Correct.

Q: I'm gonna hand you what's been marked as Department Exhibit -- or Respondent's Exhibit 7.

All right. I've got Respondent's Exhibit 7 on the screen. And we were just discussing the leasing of employees from Tractor Supply Company to Michigan. What is Exhibit 7 that's on the screen?

A: Master Shared Services Agreement between Tractor Supply Company and Tractor Supply Company of Michigan.

(Respondent's Exhibit Number 7 was introduced into the record at this time.)

Q: So this is the intercompany agreement that we were just discussing ---

A: Yes.

Q: --- related to leasing employees? Okay. What is the date of the agreement?

A: September 30th, 2001.

Q: Okay. And 2001 is the date of the Tractor Supply Company reorganization, correct?

A: Correct.

Q: Okay. And that is when the Texas and Michigan entities were initially formed, correct?

A: Correct.

Q: And prior to this agreement, all employees in all the Tractor Supply Company retail stores would've been employees of the parent company, correct?

A: Correct.

Q: Okay. And that includes the Michigan retail stores, correct?

A: Correct.

Q: And that includes the Texas retail stores?

A: Correct.

Q: All right. Well, let's go back to the entity -- or, or the agreement.

Tractor Supply provides these leasing services to Michigan at a rate of cost plus a 10 percent markup, correct?

A: Correct.

Q: Okay. And there's no transfer pricing study related to this agreement, correct?

A: To my knowledge.

Q: Okay. And Tractor Supply does not know how it determined the markup for this agreement, correct?

A: No. It was 20 some odd years ago.

Q: Okay. And again, Michigan does -- or Tractor Supply Company does not provide leasing of

employees to any other entity, correct?
A: Correct.
Q: All right. And for this particular transaction, it's documented in the taxpayer's books and records as a journal entry, correct?
A: Correct.
Q: Okay. And that means there's no check cut or no cash deposited into a bank account?
A: Correct.
Q: Okay. All right. If you will turn to the last page of this agreement. All right. Who signed on behalf of the Michigan entity?
A: David Lewis.
Q: All right. And Mr. Lewis is an Officer of Tractor Supply Company, the parent company, correct?
A: Correct.
Q: Okay.

MS. WOOTEN: Your Honor, at this time the Department would offer Respondent's Exhibit 7 into evidence.

(Respondent's Exhibit Number 7 was offered into evidence.)

MS. GEER: No objection, Your Honor.

THE COURT: It's admitted.

(Respondent's Exhibit Number 7 was admitted into evidence.)

(Whispering.)

Q: All right. All right. I'm gonna hand you a document that's been marked Respondent's Exhibit 8.

MS. GEER: If this short-circuits anything, I would agree to this one coming in.

MS. WOOTEN: Okay. That's fine. You initially had it --

MS. GEER: I know ---

MS. WOOTEN: Just so ---

MS. GEER: I apologize.

MS. WOOTEN: I'm gonna go through all of them.

MS. GEER: Yep. I'm sorry.

MS. WOOTEN: All right. So, the Department would offer in Respondent's Exhibit 8, which is the Master Shared Services -- or Administrative Services Agreement between Tractor Supply Company and Tractor Supply Company of Texas.

(Respondent's Exhibit Number 8 was offered into evidence.)

THE COURT: It's admitted.

MS. WOOTEN: Okay.

(Respondent's Exhibit Number 8 was admitted into

evidence.)

Q: All right. So, just a few things about this agreement. This agreement's between Tractor Supply Company and Tractor Supply Company of Texas, correct?

A: Correct.

Q: And it's related to administrative services like accounting, financial services, legal services, executive, information technology, human resources, marketing and advertising and quality control, is that correct?

A: That is correct.

Q: All right. That's a lot of headquarter functions. Did -- are there any that I missed that you're aware of?

A: There could be others in here, but it's -- I think it, it also says that other services -- there may be some other, you know, as we continue to grow, would fall into this, in Section I.

Q: All right. And Tractor Supply Company provides these services to the related entities based on an allocation of cost, correct?

A: Yes.

Q: And there's no transfer pricing study related

to this agreement, correct?
A: Correct.
Q: And Tractor Supply Company does not provide these services to anybody outside of the entity -- or outside of the group, correct?
A: Correct.
Q: And this transaction is recorded in the taxpayer's books and records as a journal entry?
A: Correct.
Q: And again, like we discussed, that means there's no check cut and there's no cash that's being deposited into a bank account?
A: That is correct.
Q: All right. I'm gonna hand you what's been marked as Exhibit 9 -- Respondent's Exhibit 9.
MS. GEER: Nikki, we don't object to this one either.
MS. WOOTEN: Okay. Thanks.
Q: Marjorie, if you could identify Respondent's Exhibit 9 for us?
A: Licensing Agreement between Tractor Supply Co. of Texas LP and Tractor Supply Company.
(Respondent's Exhibit Number 9 was introduced into the record at this time.)

Q: Okay. And this agreement was in effect during the audit period?

A: Yes.

Q: Okay. And again, what's the date of this agreement?

A: September 30th, 2001.

Q: During the audit period, Texas did not charge Tractor Supply Company for the licensing of the IP, correct?

A: Correct.

Q: Even though PricewaterhouseCoopers recommended charging a price in its 482 Study, correct?

A: I don't know that they recommended it, but they did offer up a comp for that.

Q: Okay. And you would agree that Tractor Sup- ---

THE COURT: They offered up a comp? Can you ---

A: Yes. In the 482 Study, there are comps of what they ---

THE COURT: Just ---

A: Comparisons of what a, I guess, a -- well, appropriate charge would be ---

THE COURT: Oh, okay.

A: --- if we decided to charge for that.

THE COURT: All right.

Q: And you agree that Tractor Supply's intellectual property has value, correct?
A: Yes.
Q: Okay. And to your knowledge, no one outside of the Tractor Supply entities can use this IP without Tractor Supply's permission, correct?
A: Correct.
Q: Okay.
MS. WOOTEN: Your Honor, at this time we would offer Respondent's Exhibit 9 into evidence.
(Respondent's Exhibit Number 9 was offered into evidence.)
THE COURT: Ms. Geer didn't object, so ---
MS. WOOTEN: She did not object.
THE COURT: --- it's admitted.
(Respondent's Exhibit Number 9 was admitted into evidence.)
Q: All right. Now, lastly, let's go to Joint Exhibit 22.
THE COURT: Have the Joint Exhibits been offered?
MS. WOOTEN: Yes, Your Honor. We did that, I believe, at the beginning of the hearing.
THE COURT: Okay. I'm just making sure.
MS. WOOTEN: But for the record, if it was not, we would jointly offer ---

MS. GEER: We do so now.
MS. WOOTEN: We do so now.
(Laughter.)
THE COURT: Well, I don't -- I can't specifically remember one way or the other, whether I admitted them.
MS. WOOTEN: Okay. The court reporter's telling me ---
THE COURT: Offering it doesn't get it in.
MS. WOOTEN: Your Honor, the Department offers Joint Exhibits 1 through 53 into the record in this matter.
(Joint Exhibit Numbers 1 through 53 were offered into evidence.)
MS. GEER: No objection.
THE COURT: They are admitted ---
MS. WOOTEN: Thank you.
THE COURT: --- 1 through 53.
(Joint Exhibit Numbers 1 through 53 were admitted into evidence.)
Q: Marjorie, if you could please identify what's been -- it's displaying on the screen as Joint Exhibit 22.
A: Inventory Procurement Agreement between Tractor Supply Co. of Texas LP and Tractor Supply

Company.

(Joint Exhibit Number 22 was introduced into the record at this time.)

Q: So, we've been talking a lot about intercompany transactions in Texas and the procurement service. This is the agreement that documents that particular transaction for the Tractor Supply Company Group, correct?

A: For Tractor Supply Company and Texas, yes.

Q: All right. What is the date of this agreement?

A: September 30th, 2001.

Q: Okay. And prior to this agreement, Tractor Supply Company the parent, was providing the procurement function, correct?

A: Not exactly. We were doing a lot of procuring using third parties, so going through third party distributors and whole- -- wholesalers.

Q: Tractor Supp- -- quote, Tractor Supply had buyers at this time, before the procurement function moved into Tractor Supply Company of Texas, correct?

A: Yes. We had a very small group of, of buyers at this point.

Q: And those buyers were physically located in the headquarters in Tennessee, correct?

A: In the store's for -- in Tennessee, yes.

Q: Okay. All right. Going back to the Agreement. Tractor Supply Company provides the procurement services for the group for a 9.7 percent markup, is that correct?

A: Yes.

Q: Okay. And Tractor Supply has offered a 482 Study to support that markup, correct?

A: That's correct.

Q: All right. And Texas does not provide this procurement function or service for any entity outside of the group, correct?

A: That is correct.

Q: And this transaction is recorded in the taxpayer's books and records as a journal entry, correct?

A: That is correct.

Q: And again, no check was cut, no cash was deposited into a bank account?

A: That is correct.

Q: All right. We talked about the procurement function before the restructuring in 2001, let's talk about it after the restructuring.

In 2001, Texas was formed under the restructuring plan and now provides the

procurement function for Tractor Supply Company the Group, correct?
A: That is correct.
Q: Okay. But Tractor Supply of Texas employees performing the procurement function are physically located in Tennessee?
A: That is correct.
Q: All right. Texas does not physically hold the inventory, correct, that it's purchasing under this procurement function?
A: It can, depending on if it's in a Texas facility -- a Texas-owned facility.
Q: But for the other retail stores in Michigan and all of the retail stores operated by the parent company, it's then shipped directly to the retail store or a distribution center, correct?
A: Sometimes it's directly shipped from the vendor. No.
Q: But to the retail stores operated by Tractor Supply Company?
A: Sometimes.
Q: Okay. All right. If you will turn to the last page of this Agreement. It is not signed, correct?
A: It is not signed.

Q: All right.

MS. WOOTEN: (To Ms. Gamble) if you will pull up Joint Exhibit 23.

Q: And that's because the initial version provided to the Department did not have a signature, correct?

(Joint Exhibit Number 23 was introduced into the record at this time.)

A: Correct.

Q: All right.

MS. WOOTEN: (To Ms. Gamble) if you'll flip to the signature page on this one.

Q: So, we're looking at Joint Exhibit 23. And could you identify this particular document -- or Exhibit for the Court?

A: Inventory Procurement Agreement between Tractor Supply Co. of Texas LP and Tractor Supply Company.

Q: And it is a -- an identical copy of Joint Exhibit 22 other than this one, as we'll see in a few minutes, is executed by the Company, correct?

A: I believe so.

Q: Okay. All right.

MS. WOOTEN: (To Ms. Gamble) if you'll scroll down to the signature page.

Q: All right. Who signed this agreement on behalf of Texas?

A: Cal Massmann.

Q: Okay. And he is a Senior VP, CFO of Tractor Supply Company, correct?

A: Correct.

Q: All right. And who signed on behalf of Tractor Supply Company?

A: David C. Lewis.

Q: And he is also an Officer or dir- -- yeah, an Officer of Tractor Supply Company, correct?

A: Correct.

Q: All right. Let's talk about Tractor Supply's tax returns.

Tractor Supply Company and its subsidiaries file a federal consolidated return for the years at issue in this matter, correct?

A: Yes.

Q: And that included Michigan and Texas on that return, correct?

A: Yes.

Q: And that's because all of these entities are owned 100 percent, either directly or indirectly by the parent company?

A: That's correct.
Q: And the parent company is the taxpayer, correct?
A: The parent company is the taxpayer, yes.
Q: All right. On federal consolidated returns, intercompany transactions are eliminated or zeroed out, correct?
A: Correct.
Q: And that's because the two entities on the return, one is receiving income and the other's reporting it as an expense, correct?
A: Correct.
Q: During the audit period, Tractor Supply Company filed combined unitary returns in some states, correct?
A: Yes, because we were required to.
Q: One of those states is California, correct?
A: Correct.
Q: And another state they filed was Illinois, they filed a combined unitary return in Illinois, correct?
A: Yes.
Q: All right. During the audit period, Illinois did not have any distribution facilities, correct?

A: Correct.
Q: And it did have -- not -- it did not have any other activity other than operating retail stores, correct?
A: Correct.
Q: All right. I'm gonna hand you two exhibits.
All right. The first is Respondent's Exhibit 19. And could you identify it for the Court, please?
A: Sure. It's Form 100, the California Franchise and income tax return for the tax year ended December 26th, 2015.
(Respondent's Exhibit Number 19 was introduced into the record at this time.)
Q: All right. And fiscal year 2015 is one of the years at issue in this matter, correct?
A: Correct.
MS. WOOTEN: All right. I will represent to the Court, this is not the entire California return, I don't have the white pages. What I have is, is through the signature page, so I'm happy -- I'm not offering it at this time, but to let the witness know, it does not include the white pages with the return.
Q: If you will flip to the last page, which is

page four. It's Bates Stamped TSC 00002733. All right.

A: My ---

Q: This return is signed and dated, correct?

A: It is.

Q: Okay. And Blake Snider signed it, correct?

A: Correct.

Q: And he was your boss ---

A: Correct.

Q: --- in 2016, correct?

A: Correct.

Q: Okay. All right. I'm gonna hand you another one. I'll hand you an Exhibit that's been identified as Respondent's Exhibit 20. Can you identify that for the Court, please?

A: Sure. It's the Illno- -- Illinois Department of Revenue's 2015 Form, Illinois 1120, corporation income and replacement tax return.

(Respondent's Exhibit Number 20 was introduced into the record at this time.)

Q: Okay.

A: And that's also for the 2015 year.

Q: All right. If you'll turn to Bates stamp TSC 00002972.

A: Is that on a particular page?

Q: It should be Bates stamped at the bottom ---
MS. GEER: Mine aren't ---
Q: --- there's a series of numbers.
MS. GEER: --- are not Bates stamped.
A: I don't see any.
Q: Here, I'll give you this one. This one is Bates stamped.
MS. WOOTEN: It is page three of the document, Bryson.
THE COURT: Let's make sure we're all on the same page, so. You there?
MS. GEER: Yes. Thank you.
Q: This return is signed and dated, correct?
A: It is.
Q: And Jeff Olsberg signed it?
A: Jeff Olsberg signed it.
Q: And he was your boss during the audit period, correct?
A: Yes.
Q: Okay.
THE COURT: Another boss?
A: Yeah. There was a changing of the guard. My first boss left and he came in.
THE COURT: Are you the boss now?
A: We don't have a VP of Tax, currently.

THE COURT: Should we recommend you as a part of the decision in this case?
A: I don't know. It depends on this case, I guess.
(*Laughter.*)
Q: No pressure.
THE COURT: That was a good response.
Q: All right. During the audit examination, do you recall discussing calculations with an auditor regarding the proposed assessment?
A: I do.
Q: Okay. And in those -- in that correspondence, you agreed with the method -- the calculations under the, the Department's use of combined unitary reporting, but you did not agree that the method should be imposed, correct?
A: Yes. Initially, what was proposed by the auditor, if it was going to use a unitary method, wasn't being calculated correctly under any type of unitary combined approach. The eliminations that are generally applied to the base had not been applied, so in looking at the review of what had been initially proposed, I countered that, you know, one, we did not believe that we should be subjected to the

unitary method. And then, two, if we were going to file a unitary return, that the elimination should be included in the base.

Q: Okay. Setting aside the first point you made, that you do not believe the Department sh- -- can impose this method in this matter. So, we agree to disagree on that. Looking at the mathematical calculation under the unitary approach, you agree the auditor made the recommendations that you suggested for that calculation, correct?

A: Upon conversation, yes, that they went back and put that in.

Q: And ultimately you agreed with the Department's mathematical calculations of the combined unitary return, correct?

A: Yes.

Q: The only disagreement was whether or not the Department could impose an alternative method in this case?

A: Correct.

Q: Okay. So you do not dis- -- dispute the Department's calculation of the sales factor in this matter, correct?

A: No.

Q: Okay.

A: The numerator -- the, the denominator, of course, relates to which method that, you know, we ultimately land on, but -- so, let me back up there.

Q: Okay.

A: I don't disagree with -- (whispering to self) does that make sense? Yeah.

I do not ag- -- I agree with how an apportionment factor for South Carolina is generally calculated with a numerator and a denominator represented by sales of the, of the taxpayer that's subject to the filing. In our case and in our return, it would've been the numerator for the taxpayer, the parent, South Carolina sales divided by the sales of the parent. That's, that's -- I agree with that apportionment factor. I would not agree with necessarily a unitary apportionment factor, which would be suggested by, you know, the calculation.

Q: All right.

(Whispering.)

Q: All right. I'm gonna hand you what's been marked as Respondent's Exhibit 17. Do you

recognize this document?
A: Yes.
Q: Okay. If you could identify the parties to this e-mail, please?
A: Sure. It is myself, Steven Riggs, Rob King with South Carolina, and Matt Appelman who is on my team.

(Respondent's Exhibit Number 17 was introduced into the record at this time.)

Q: Okay. And if, if you can look in the first -- on the first page, the message beginning with Steven.
A: Yep.
Q: If you could read that first sentence, please?
A: Sure.
THE COURT: Can you put that up?
MS. WOOTEN: Sure.
A: "Steven, we are now in agreement with South Carolina Department of Revenue's mathematical calculation for the combination approach." So in agreement with the calculation. "We are not still in agreement with the approach. Just let me know if you need anything else." So not in agreement with the unitary method.
Q: That it could be applied, or the calculation?

Because -- at any point, did you raise the calculation of the sales factor -- that you disagreed with this calculation of the sales factor with the auditor?

A: I think we were referring to the -- I -- we were referring to the base, the calculation of the base under -- if you applied the unitary method. We disagreed on the calculation of the base, not the din- -- calculation of the apportionment factor, of which, that unitary base would be applied if the unitary method was applied.

Q: Okay. Does it say anything in this e-mail about disagreeing with the calculation of the base under a combined unitary reporting method?

A: I don't see anything in that specific sentence.

Q: Okay.

MS. WOOTEN: Your Honor, the Department would offer Respondent's Exhibit 17 into evidence.

(Respondent's Exhibit Number 17 was offered into evidence.)

MS. GEER: No objection.

THE COURT: It's admitted.

(Respondent's Exhibit Number 17 was admitted into evidence.)

Q: All right. And if you will bear with me one more second.

Do you recall discuss- -- so we just looked at an e-mail that was correspondence during the audit examination. Do you recall discussing this topic in your 30(b)(6) deposition?

A: I don't remember, honestly.

Q: Okay. All right. I'm gonna hand you the transcript from your 30(b)(6) deposition. And for the record, the dep- -- the witness is using page 24 from the official full transcript. In the condensed version of her deposition transcript, it's at page 25.

THE COURT: Are you there, Ms. Geer?

MS. GEER: Almost. Yes. Thank you.

Q: All right. If you will look at lines -- beginning at line nine.

A: Yep.

Q: All right. And if you could read that for us, please?

A: And there have been a couple audits, but I believe in this particular one we would've had at least been able to get to the point that they were calculated correctly under the method that was being proposed, not that we would've agreed with the method being proposed.

Q: Thank you. All right. Earlier in your testimony we, we talked about the intercompany agreements that are at issue in this matter, and they were signed in September of 2001, correct?

A: Correct.

Q: And they were done part as a -- part of the reorganization of the Tractor Supply entities, correct?

A: Correct.

Q: Okay. I'm gonna hand you what's been marked as Department Exhibit 12. Can you identify Respondent's Exhibit 12 for the Court?

A: Minutes of the meeting of the Board of Directors of Tractor Supply Company held on July 26th, 2001.

(Respondent's Exhibit Number 12 was introduced into the record at this time.)

Q: All right. And these documents were produced by Tractor Supply in discovery and subject to the Confidentiality Agreement, correct?

A: Correct.

Q: All right. And you discussed them during your

30(b)(6) deposition, correct?
A: Correct.
Q: Okay. And when we were discussing the intercompany agreements earlier, do you recall two of the Officers on those agreements were Cal Massmann and David Lewis, correct?
A: Correct.
Q: All right. If you will look to the second paragraph of the first page, which is Bates stamped TSC 4683.
A: Uh-huh.
Q: Cal Massmann and David Lewis are sited -- or are documented as present at this meeting, correct?
A: I see David Lewis. Maybe I'm not looking in the right spot.
Q: His first name is on the end of the third line and his last name is on the beginning of the fourth line.
A: Got it, yes.
Q: And both of them are there in their cap- -- positions as either, for Massmann, Senior Vice President, CFO of Tractor Supply Company, and David Lewis as Vice President of the -- and Corporate Secretary of the corporation,

correct?
A: Yeah. Controller.
Q: Oh, controller. Excuse me. Yes.
MS. WOOTEN: Your Honor, at this time the Department would move to -- or would offer Respondent's Exhibit 12 into evidence.
(Respondent's Exhibit Number 12 was offered into evidence.)
MS. GEER: Your Honor, the main concern we had with this one was relevance, but since we're non-jury, I'll, I'll agree to let it in now and I'll hear what the relevance is.
THE COURT: Okay.
(Respondent's Exhibit Number 12 was admitted into evidence.)
Q: During the meeting, Mr. Mass- -- or, if you'll turn to 4686. During the meeting, Mr. Massmann described an update to the Corporation's tax planning -- State Tax Planning Strategies, correct?
A: Yes.
Q: Okay. And part of that was the formation of two subsidiaries, correct? That's in part one of -- underneath the bullet ---
MS. WOOTEN: (To Ms. Gamble) Do you mind pulling

that up?

A: Yeah, but I would say that one doesn't necessarily drive the other. What I mean by that is, the formation of two new subsidiaries would've had a benefit of tax planning opportunities.

Q: And the two entities that we're talking about in this particular document is the Tractor Supply Company of Texas entity, correct?

A: With Tractor -- the, the formation of the two new subsidiaries?

Q: Yes.

A: Would've been the creation of Tractor Supply Company of Michigan and Texas.

Q: Right. Okay. All right. All right. If you'll look ---

MS. WOOTEN: (To Ms. Gamble) Is that 13?

Q: All right. Let's look at another exhibit.

MS. WOOTEN: (To Ms. Gamble) 14?

(Whispering.)

Q: All right.

THE COURT: Is 14 already in?

MS. WOOTEN: 14 is not in, Your Honor.

THE COURT: Okay.

MS. WOOTEN: I'm getting ready to hand it to her.

Q: I'll hand you what's been marked as Respondent's Exhibit 14.

MS. GEER: Just so I'm clear on my notes, was the last one 12, not 13?

MS. WOOTEN: Yes.

MS. GEER: Okay.

MS. WOOTEN: I skipped 13.

MS. GEER: Okay.

MS. WOOTEN: I didn't offer it.

Q: All right. Can you identify what's been marked as Respondent's Exhibit 14?

A: Texas and Michigan Restructuring.

(Respondent's Exhibit Number 14 was introduced into the record at this time.)

Q: All right. And, generally, if -- this document was also provided to you in the 30(b)(6) deposition, correct?

A: I believe so.

Q: And it was produced by Tractor Supply Company as part of discovery, correct?

A: Correct.

Q: Okay.

MS. WOOTEN: Your Honor, at this time, the Department would offer Respondent's Exhibit 14 into evidence. It is TSC 00004839.

(Respondent's Exhibit Number 14 was offered into evidence.)

OBJECTION:

MS. GEER: Your Honor, we do have an objection to this one. This is -- obviously, it seems to be a part of a document, so I'm not sure what the rest of it is, but I believe that it is a document created by PwC, not by Tractor Supply. And so ---

THE COURT: PwC?

MS. GEER: It'd be -- yeah, PricewaterhouseCoopers.

THE COURT: Okay.

MS. WOOTEN: Sure. So, Your Honor, I have the entire document as it was produced to us, understanding that Ms. Geer was gonna make this objection. It was produced as a part of a docu- -- or as a page within this document, but we do not believe it is a PwC document. And the reason why is, if you will look at the document and read the language, it is written in the first person. It is -- in order to enhance the earnings of Tractor Supply Company, we are working with representatives of our accounting firm, PwC. The entire document is written in the perspective of Tractor Supply

Company, it is not written from PwC. And if you -- and I have the document for inspection for the Court. It -- the first page and the other pages within this document are formatted completely differently than this particular document. So we believe that this is a Tractor Supply document. It was produced as part -- it was stuck in the PwC, what is purporting to be a PwC Memo, but it is clearly statements from Tractor Supply Company and not PwC.

MS. GEER: I mean, I, I can't tell that. I don't know that PwC didn't help us draft a document that they wanted us to be able to use for some purpose. I mean, I would think -- she can obviously ask the witness if she knows, but otherwise, I would think we would need a PwC witness here to tell us whether this was part of the ---

THE COURT: So your question ---

MS. GEER: --- document.

THE COURT: --- is, not as to, as to relevancy, but authentication?

MS. GEER: Correct. And hearsay, if I -- if we get past authentication.

THE COURT: Yeah, yeah.

MR. STREISEL: What's the full Bates label, Nikki?
MS. WOOTEN: It starts at 4836.
Your Honor, it was produced by Tractor Supply Company as part of discovery. It did not come from P- -- we did subpoena PwC and their files. This particular file did not come from PwC, it came from Tractor Supply Company. It is authen- -- I mean, it's authentic. I asked about it ---
THE COURT: I'm not -- as to authentication, since it was produced by Tractor Supply, I will find it authentic. That's the -- sufficiently established the authenticity of the document. But as to its relevancy -- or ... I think you -- explain that a little bit more.
MS. GEER: I -- well, I don't see how we -- I don't see how the auth- -- authenticity has been established. It is a document that -- and I don't have the whole one -- (to Ms. Wooten) do you mind?
MS. WOOTEN: Sure.
MS. GEER: Okay. So it's a memo to David Lewis as Tractor Supply from Kelly Smith and Mara Jolkovsky in the PwC Atlanta office, kick-off meeting agenda, May 17, 2001. And it says, as

you know, PricewaterhouseCoopers and Tractor Supply will meet on the 17th of May at Tractor Supply Company's Headquarters in Nashville to kick-off the restructuring project described below. And then it goes onto summarize it. And -- let's see ... This does not ...

So it has two -- actually two pages that have similar formatting. Let's see -- no. If you look at the page numbers on these, page number two has like a two in parenthesis, and then if you keep flipping, page number three, which is the document that we're talking about, that's being offered into evidence, has the same exact pagination formatting. And then the last page, which is Tractor Supply Kick-off Meeting Agenda, where it says we, and I think when you read the context it's clear it's PwC, would like to have the opportunity to meet with the following personnel either in-person or by phone. And it lists Tractor Supply positions. At the bottom ---

THE COURT: Can I stop you there?

MS. GEER: Yeah.

THE COURT: Okay. There's -- oh, two issues.

MS. GEER: Yep.

THE COURT: I think.
MS. GEER: Yes.
THE COURT: And you can tell me.
MS. GEER: Uh-huh.
THE COURT: Number one, whether the document itself is an authentic document.
MS. GEER: Right.
THE COURT: You provided it. I would think that your providing of it would be -- would verify it's authenticity. The question you seem to be presenting to me ---
MS. GEER: Yes.
THE COURT: --- is whether it is an authentic document of Pricewaterhouse or whether it's an authentic document of Tractor Supply, is that not? Or, are you saying that you don't even -- you just believe this document was made up and ---
MS. GEER: I think it ---
THE COURT: --- and supplied by your off- ---
MS. GEER: I, I think it appears to be a PwC document that they sent us and that we had in our files so we ---
THE COURT: Sent it back to them?
MS. GEER: --- produced it in discovery because it

was requested.

THE COURT: Okay.

MS. GEER: But I, I think it still appears to be, even by the pagination, a PwC document, which I would think would need to be authenticated by a PwC employee, especially if the Department is arguing that it's actually a Tractor Supply page in here and not a PwC page. I mean, they subpoenaed PwC's file. If the original is in the PwC file, then maybe you could compare and figure out whether it is. But still, I'd think that document would still have to come in through a PwC witness.

THE COURT: All right. Can you explain to me ---

MS. WOOTEN: Sure.

THE COURT: --- the provision of this document? All right. Ms. ---

MS. WOOTEN: How we received ---

THE COURT: --- Geer is saying that you sent it to them and they sent it back to you.

MS. WOOTEN: We received this particular document in discovery from Tractor Supply Company. It was a page within, what was produced as this document.

THE COURT: Was it a document that you had provided to Tractor Supply, is what I'm ---

MS. WOOTEN: We did not provide this document, we got it from Tractor Supply Company.

THE COURT: So you never had possession of this document prior to its provision?

MS. WOOTEN: That is correct.

THE COURT: (To Ms. Geer) that seems to be a little different than what you're telling me now

MS. GEER: No, I don't, I don't think ---

THE COURT: Oh, okay. That's ---

MS. GEER: I, I don't disagree that we -- so it was in our file. It appears to be a document that is in our file because PwC sent it to us. So PwC sent us a document. And in order to determine that it is an authentic PwC document, I would think a PwC witness would need to authenticate that.

MS. WOOTEN: And my argument ---

THE COURT: Well, she's arguing that it's not a ---

MS. WOOTEN: --- it's not PwC, it's a ---

THE COURT: That's the point I was ---

MS. WOOTEN: --- Tractor Supply Company document.

THE COURT: That's the point I was making, is that, that the question is, it's an authentic document, but by whom? And you're arguing that it's by Pricewaterhouse, she's arguing that it's by Tractor Supply. Well, I'm good for a break right now anyway, so.

MS. GEER: I'm sorry, I missed your -- what you said?

THE COURT: Well, my staff is telling me that I should take a break about every two hours.

MS. GEER: Oh, that's great. Yeah.

MS. WOOTEN: Okay.

MS. GEER: I'm good with that.

MS. WOOTEN: All right. Are we addressing this issue when we come back, Your Honor?

THE COURT: Oh, no, I'll just make it go away.

(Laughter.)

MS. WOOTEN: Well, you very much could make it go away. I will agree with that.

THE COURT: Yeah.

MS. WOOTEN: All right.

THE COURT: No, I'm gonna address when I come in.

MS. WOOTEN: Okay. Thank you.

THE COURT: I'm not playing.

MS. WOOTEN: I just want to make sure that there -- a decision hasn't been made before we adjourn?

THE COURT: No. No decision is made. The decision is made -- is for me to leave. Thank y'all.

MS. WOOTEN: Thank you.

MS. GEER: Your Honor, did you want to give us a time that you want us back?

THE COURT: Oh, five minutes, ten?

MS. GEER: Can we have ten?

THE COURT: Ten? Ten, Okay.

MS. GEER: Yeah. A bathroom break would be nice.

THE COURT: Okay.

MS. GEER: Thank you.

(Off the record from 11:56 a.m. through 12:10 p.m.)

THE COURT: So, I'm trying to read the rules real quick.

(Whispering.)

THE COURT: I can't find the rule I like. Sorry, y'all. All right. There, I just found it.

Okay. Are you wishing to offer -- you -- you're standing, are you ---

MS. GEER: Oh, I'm sorry. I -- if you're wanting to talk to her first, I can, I can wait.

THE COURT: I can tell y'all, I just have to -- cogitating if I may. I mean, I see Rule 1003 about duplicate documents. And it discusses if there's a genuine question was raised about the authenticity of the original. And I think what you're telling me, Ms. Geer, is there's --

well, are you telling me that you have a genuine question about whether this is a Tractor Supply document ---

MS. GEER: Yes.

THE COURT: --- and you believe this it, it is actually only a ---

MS. GEER: PwC.

THE COURT: So my problem is, you provided it, you didn't ... I think, I would rule -- or I'm going to rule that I find that it's authentic, but my problem is I don't -- I cannot determine it's probative value, because I cannot discern whether this authentic document -- (To Ms. Wooten) and I'm looking to you now -- is that of, of Pricewaterhouse or that of Tractor Supply. And I'm really not even sure about that, because I would have to know more about what purpose you're offering it for, Ms. Wooten.

MS. WOOTEN: Sure.

THE COURT: But if you're offering it for the fact that it is a admission by Tractor Supply, and that's the purpose for which you're offering, then I have to note -- determine if it's an admission by Pricewa- -- I mean, by Tractor

Supply if it indeed it was that -- written by Tractor Supply. And the first-person aspect of this, although, I think is a consideration, does not reach the level of establishing it's probative value for me at this point, but that doesn't mean I'm going to rule it out. It just means, at this point in the testimony, I'm not letting it in.

MS. GEER: Your Honor, I, I did not have the benefit of being able to see the full document at -- when I was making my earlier objection.

THE COURT: And I think you should do that, because if you're going to make a statement as an officer of the Court that you believe is no ---

MS. GEER: Well, I still believe that. Based on what I -- based on my limited, quick review of it, I still stand behind all of the statements that I've already made. But we were on break, I was able to review the full copy on our screen ---

THE COURT: Okay.

MS. GEER: --- and I have additional things that, to me, strongly suggest it's a PwC document that I would like to put in the record, not to, you know, argue against your ruling that you've just given, but just because I didn't have the full benefit of that when I was making my earlier objections because we didn't have a full copy.

THE COURT: So, having won the point, you wish to further argue the point?

MS. GEER: Well, I, I think it's important to put -- (laughter) -- I don't know, did I win?

(*Laughter*.)

THE COURT: You have at this point.

MS. GEER: Okay. So, so let me make sure, maybe I just didn't understand the ruling. Are you saying that you're not allowing it in now until the probative value is established further?

THE COURT: Yeah. That's what ---

MS. GEER: Okay. I'm, I'm fine with that, Your Honor. I think I just misunderstood.

MS. WOOTEN: Thank you, Your Honor.

Q: Marjorie -- and I apologize for calling you by your first name. I can't -- I can ---

THE COURT: Well, that was around ---

A: McKeown.

THE COURT: --- (inaudible due to multiple speakers) ---

MS. WOOTEN: Yeah, it ---

THE COURT: I'm all right with ---
MS. WOOTEN: I apologize.
Q: You would agree that in the restructuring process, Tractor Supply's -- one of Tractor Supply's goals was to have little or no impact on the day-to-day operations of Company personnel?
A: I would agree that if we were to do a restructuring, for many reasons, we would want to have as little of an impact at -- on the day-to-day lives of personnel.
Q: And you would agree that Tractor Supply's goal is not to change the method, how the impact is -- impacted employees currently do business with Tractor Supply, correct?
A: Their day-to-day operations, not to impact them or cause disruption.
MS. WOOTEN: Your Honor, that is the reason why we are proposing this, this particular document, is to show pre and post restructuring, one of their primary goals was not to impact the day-to-day operations of the employees. And we think that is an important fact in this case.
THE COURT: Well, she just testified to that.
MS. WOOTEN: She did. And whi- -- which again, I

think corroborates the document, that this is a document of Tractor Supply Company. It is outlining the goals and things that they are hoping to accomplish with this restructuring. And just -- I'll make this one point, and then I will ---

THE COURT: Well, you're not bothering me. It, it ---

MS. WOOTEN: I would just note ---

THE COURT: If she confirms every element of this document that lists all the goals, and that's what you're offering it for, I don't need the document -- or the document is not needed in the evidence anyway, and that lessens it's probative value, so why should I dance upon the head of the needle to get that which is already established in, when it -- when I'm not sure of the -- to who -- by whom the document was written?

MS. WOOTEN: Okay. That -- you're -- yeah -- that -- okay. We'll withdraw the ar- -- that -- the document, but I just wanted to -- now that I have that on the record, I will withdraw ---

THE COURT: Okay.

MS. WOOTEN: --- the document.

(Respondent's Exhibit Number 14 was withdrawn.)

THE COURT: Okay. Thank you.

MS. WOOTEN: For this -- at this time.

THE COURT: Well, somebody's back there shaking their head, do you want to talk?

MR. LUTHER: No (laughter).

THE COURT: Okay.

MS. WOOTEN: At this time, I will withdraw it. Your Honor, may I have five minutes, or two minutes?

THE COURT: Yeah.

MS. WOOTEN: Thank you.

THE COURT: How much longer are we gonna have this witness? Are you about to finish up?

MS. WOOTEN: I'm -- I possibly could be finishing up very soon.

THE COURT: Okay. Well then, that'll give me an idea of lunch breaks. Well, Ms. Geer, you're, you're only gonna be about, what, five minutes with her or maybe two?

MS. GEER: Yes, Your Honor.

THE COURT: I'm kidding ---

MS. GEER: No.

THE COURT: You serious ---

MS. GEER: Well, we're gonna call her in our case.

THE COURT: Oh, okay.

MS. GEER: So I'll, I'll probably just clear-up a few minor points, and then we could be done with her ---

THE COURT: Oh, okay.

MS. GEER: --- until our portion of the case.

THE COURT: And then you're gonna recall -- or you're gonna call her ---

MS. GEER: And then I'm gonna call her.

THE COURT: Yeah.

MS. GEER: Yeah.

THE COURT: Which, I guess, that would be recalling, to recall, yeah.

(Laughter.)

MS. WOOTEN: Your Honor, that's all for the Department at this time.

THE COURT: Thank you.

MS. MCKEOWN: Ouch.

THE COURT: Are you -- you okay?

MS. MCKEOWN: I just smacked my knee, that's all.

MS. WOOTEN: Oh, no.

(*Laughter.*)

MS. GEER: All right. One minute.

THE COURT: That chair -- the height of it adjusts up and down, if you need to.

MS. MCKEOWN: I'm good, I just didn't realize there was a beam underneath the, the table right where my knee was.

THE COURT: Well, I have experienced that up here many a time and it hasn't been pleasant. Of course, my thing isn't on a hinge.

MS. GEER: Your Honor, I apologize. I just need to just gather a couple of things really quickly.

Your Honor, I'm gonna continue with the Margie -- or Marjorie.

MS. MCKEOWN - CROSS EXAMINATION BY MS. GEER:

Q: Marjorie, who's permiss- -- first of all, who owns the trademarks?

A: Tractor Supply Company of Texas.

Q: Okay. So, who's permission would be needed to use those trademarks?

A: The general partner.

Q: Of which entity?

A: Of Tractor Supply Company of Texas.

Q: Okay. All right. And then, you referenced a few procurement activities in your discussions with Ms. Wooten, and I just wanted to ask you a couple of follow-ups to that.

Which entity finds vendors and negotiates contracts with the vendors?

A: Tractor Supply Company of Texas.

Q: Okay. And which entity determines the types, the brands, the amounts, the volume of inventory that the stores will have in their stores?
A: Tractor Supply Company of Texas.
Q: And who determines -- you mentioned earlier about sometimes the inventory might change in a particular store based on its geography, who decides those -- makes those decisions?
A: Tractor Supply Company of Texas.
Q: Okay. Who works on -- well, let me ask you this. Does Tractor Supply have any exclusive brands?
A: It does.
Q: Okay. If you had to give a ballpark number, like, a few, a lot? How many?
A: Many. Ten-plus.
Q: Okay.
THE COURT: Ten percent?
A: Oh, number of brands. Different brands, like ---
THE COURT: Oh, ten brands. Okay.
A: I, I would say maybe, 10 to 15.
Q: Okay. And who, who works on -- develops those exclusive brands?

A: Tractor Supply Company of Texas.
Q: And -- all right. And I, I know that there is a lot more detail under that, I just wanted to get the general categories and we can discuss those further later in the, in the case. One last ... And let me just clarify one more thing. When you say the answers to the questions about which entity performs certain procurement activities that you just listed, who within Tractor Supply of Texas performs those functions?
A: Who within Tractor Supply Company of Texas?
Q: Of Texas, yes.
A: The different departments that represent the procurement function operations.
Q: Okay.
A: The ---
Q: So, would it be any -- anyone that works in the Texas retail stores?
A: No.
Q: Okay.
(*Whispering*.)
Q: All right. And this may be clear in the record, it just wasn't clear to me, so I'm gonna ask you to clarify it for me, and I

apologize if it's not necessary. But you were asked some questions about testimony in your deposition that dealt with working with third parties predominantly in Asia to help source certain aspects of products. Can you just tell us a little bit more about that? How much is that done? There was a question about whether it was predominant or not?

A: Correct. And I went back and I tried to clarify what ---

Q: Right.

A: --- context that had been said in.

Q: Yes.

A: So we have vendors domestically and, you know, internationally. Only about -- I think it's about 14 percent of our business comes from overseas, as far as where we source our product from.

Q: Uh-huh.

A: And so -- and with that 14 percent, predominantly, those vendors would be in Asia.

Q: Okay. And the other, the other percentage that is left would be purchased where?

A: Domestically.

Q: Okay. So you got 14 overseas and 86-ish domestic?

A: Correct.

Q: It took me awhile but I did some math. All right. That's all I have for you. Ms. Wooten might have a few more.

MS. WOOTEN: Your Honor, just a few questions.

MS. MCKEOWN - RE-DIRECT EXAMINATION BY MS. WOOTEN:

Q: So, Ms. Geer asked you some additional questions about the purchasing function and the Texas employees. Under the restructuring, you agree that Tractor Supply Company transferred personnel and property associated with the Nashville Merchandising Operations to the Texas LP, correct?

A: Yes.

Q: Okay. And that the physical location and place of operation of the Nashville merchandising function will not change, correct?

A: Correct, it didn't change.

Q: The only change was to the legal employer of those particular individuals, correct?

A: For the procurement functions.

Q: Right. We're still talking about the procurement function. Okay.

And as part of the procurement function, once Texas overtook that function, the delivery and vendor terms did not change upon Texas taking that function, correct?

A: I think the, the vendor named changed as the agreements were now with Tractor Supply Company of Texas, but the terms as to which the vendor operated I don't believe changed.

Q: Okay. Pre and post restructuring?

A: Correct.

Q: Okay.

MS. WOOTEN: Okay. That's all, Your Honor.

MS. GEER: Your Honor, I know we're getting to a very gray area and don't want to go on further, but there's one other thing I would like to clarify based on -- solely on what Ms. Wooten just asked.

THE COURT: If it's all based on what she asked.

MS. GEER: Thank you, yeah.

THE COURT: And it's a new matter.

MS. MCKEOWN - RE-CROSS EXAMINATION BY MS. GEER:

Q: Ms. McKeown, I just want to clarify something, 'cause I, I think it's unclear. So, when people talk about things not changing once the restructure happens to the day-to-day activities of procurement, did the activities that the procurement team does change from 2001 until during the audit period?

A: Absolutely.

Q: Okay. And can you just clarify that for us and explain that a little bit?

A: Sure. If you're talking, if you're talking about just immediately aft- -- as you, you know, stamp the date and say this restructure is done, maybe not significantly at that point, but the purpose of this was to grow that. And one of the many purposes of, of the restructuring was to grow the procurement function, and so at that point in time, back in 2001, there were many -- maybe even a handful, 10-ish procurement-type individuals procuring product on behalf of the business. However, subsequent to that, we added inventory analysis and replenishment, we added product development, we added product sourcing, we -- Vendor Master Data, making sure that everything is setup accordingly. There were areas of procurement that we didn't have at that point and we grew it out. So it went from about 10 people to over 200 today, and at the time of the audit, probably, 130 team members that grew from the time that we restructured.

Q: Thank you. That's all I have.

THE COURT: Any questions regarding that?

MS. WOOTEN: All right. Your Honor, yes. Well, based on that and the questions that I asked and Ms. Geer asked, I have a few more questions about this particular restructure on Exhibit 14.

(Respondent's Exhibit Number 14 was referenced at this time.)

MS. MCKEOWN - FURTHER RE-DIRECT EXAMINATION BY MS. WOOTEN:

Q: You agree that Tractor Supply Company went through restructuring in 2001, correct?

A: Correct.

Q: Okay. And that TSC hired PwC to assist in that restructuring?

A: To consult, yes.

Q: Okay. And TSC was provided with advice and documents as part of that process?

A: Correct.

Q: And per the minutes that we just looked at, the Board of -- the Board minutes that have been -- already have been admitted into evidence, TSC Officers met to discuss that restructuring plan and the implementation of that restructuring plan, correct?

A: Correct.

Q: And those were based off of PwC's recommendations, correct?

A: Yes.

Q: Okay.

A: Let -- the minute -- I mean, the minutes, the conversation or the restructuring itself?

Q: Tractor Supply Company acted upon PW's [sic] recommendations regarding the restructuring, correct?

A: Correct.

Q: Okay. And Tractor Supply Company has kept a file -- or -- and maintained a file at their, their location with regard to this restructuring, correct?

A: Correct.

Q: And part of that file included the documents that were produced to the Department in discovery, correct?

A: Correct.

Q: Okay. So these documents were kept in the course of Tractor Supply's business records, correct?

A: They were kept in the records, yes.
Q: Okay. And this is an accurate reflection of the records in your business records?
A: It's an accurate reflection of the records that we kept.

MS. WOOTEN: Your Honor, at this time we would offer them as a business record of Tractor Supply Company. They were kept in the regularly conducted activity of their business, it's an accurate representation. We, again, would argue that these are -- it's a Tractor Supply -- the formatting is the same, it's -- appears to be other documents that are similar to this formatting, and it is in the first person. We understand pri- -- PricewaterhouseCooper's provided documents, we subpoenaed those documents, we didn't get this document with the PwC documents. So, again, we would argue -- we would suggest to the Court and offer it again as Respondent's Exhibit 14 because it is a part of Tractor Supply's business records, and it is a part of the restructuring process that is at issue in this case.

(Respondent's Exhibit Number 14 was offered into evidence.)

MS. GEER: Your Honor, it, it still is not a -- yes, it is in the records, but it's not a business record of Tractor Supply's. And if you look at the document itself, you will see that it is not a Trac- -- that that one page is not a Tractor Supply statement. If you read the introduction to the document, it refers -- which I think is clearly PwC, it actually refers, in general, to that page. I mean, I can pull it up if, if Your Honor would ---

THE COURT: I need to ---

MS. GEER: Yes.

THE COURT: --- see it.

MS. GEER: (To Mr. Streisel) pull that up.

THE COURT: Do I need this?

MS. GEER: Do we need -- what do we need to do to switch over?

MS. BUCKNER: I can find -- you guys want it? Okay.

MS. GEER: Yes, please.

(Whispering.)

MS. GEER: All right. So on the first -- oh, sorry, coming up, yet?

MS. BUCKNER: Y'all should be plugged in. I thought I've got it on right counsel, so.

MR. STREISEL: I'm plugged in. I don't know ...

MS. GEER: Oh, there we go. All right. So the first page is a memo to David Lewis of Tractor Supply from Kelly Smith and Mara Jolkovsky at PwC. And if you go to -- the first paragraph just talks about that it's a kick-off meeting for the restructure. And if you go to the second paragraph, it says; in addition to the brief summary of this restructuring ---

MS. WOOTEN: Okay.

MS. GEER: --- you will see below a proposed agenda for the kick-off meeting outlining tentative issues we would like to discuss and individuals that we would like to meet is attached. We would suggest that the brief summary of the restructuring circulated to the individuals with whom we are going to meet on Thursday, in order to give them the opportunity to begin identifying questions and concerns they have. And then, if you scroll down ...

So at the bottom of page two, you have a two in parenthesis, then we have a blue page, then we have the page that she wants -- that the Department is offering in, and if you look at the bottom of it, there's a three in parenthesis. So, I think this is all a part of

PwC's Memo and that they're referring to this summary to be distributed to Tractor Supply employees and managers, and whomever it's wanting them to share with so that they can discuss the restructure and kick-off. I think they've, they've done it on purpose for Tractor Supply to be able to use with their, with their people. So, I mean, I don't know why PwC didn't provide it, but she could have asked them -- followed up on the subpoena and asked them about this document. I don't -- I mean, I don't -- I'm not faulting her for that, I'm just saying there are ways we could've determined. And I think it's clear when you read it that it is a PwC document. So if it's being used as an admission of Tractor Supply, then I think that's a problem, because it's not an admission of Tractor Supply the party, it's something that was written by PwC.

MS. WOOTEN: Sure. We can go by this -- go through this line-by-line and I can ask the witness. But, the point that I believe Ms. Geer is making with regard to this argument -- with this document, I'm not suggesting that this was not a part of the full document, and I think I made that clear at the beginning of the hearing -- or the beginning of this. It is just a page that has been inserted in this particular ---

THE COURT: Uh-huh.

MS. WOOTEN: --- document. So I don't disagree that it is page number three in the document as we provided. But if you'll look at the second paragraph of this document -- and I don't have it on the screen, I think ---

MS. GEER: We can pull it.

MS. WOOTEN: Okay. Thank you.

It says; we would suggest that the brief summary of the restructuring, restructuring be circulated, and I believe that's what this is -- intends -- purports to be or what they're purporting it to be. It doesn't say who pre- -- who drafted it or who provided it.

THE COURT: That's my struggle, though. It doesn't say who ---

MS. WOOTEN: And, I mean, we can go through and I can ask -- again, first of all, it was produced by Tractor Supply in discovery. It is a part of Tractor Supply's business records of their restructuring. I mean, again, all provided by Tractor Supply. But we can go through line-by-line of this menu -- or of this memo and confirm that these things happened. But at the end of the day, I think the Department -- or the Department would submit to the Court that, again, Ms. Marjorie -- excuse me -- has confirmed a lot of the things already on this document. I mean, we've, we've gone through them several times, but it is all written in the first-person. It is Tractor Supply's documents. It is Tractor Supply's statement. It is their representation of what they intended to accomplish as part of this restructuring, and that is plainly in here where it says; our goal is not to do this, our goal is ---

THE COURT: But they ---

MS. WOOTEN: --- to do that.

THE COURT: My struggle is, if you're wanting me to admit it as an admission, if it indeed -- 'cause I'm not sure, when you say it's a summary of, if it's a summary written by Pricewaterhouse, then it would not necessarily be an admission by Tractor Supply, 'cause it's a summary. Now, admissions, if you go back under the Rules of Evidence and look at admissions, I mean, if you adopt the truth of it, then it would be admissible. But I have no problem -- I mean, we're, we're in re- -- re-cross, but if ---

MS. WOOTEN: Sure.

THE COURT: --- she did go into this. But, you know --well, she did re-cross, but a re- -- you're on re-re-direct. But I have no problem letting you, under the circumstances, go into the specifics ---

MS. WOOTEN: Okay.

THE COURT: --- with her.

MS. WOOTEN: All right. Your Honor ---

THE COURT: Line-by-line if you want to.

MS. WOOTEN: Okay.

THE COURT: It's just ---

MS. WOOTEN: All right.

THE COURT: --- admitting this document as an admission, I do have a problem with.

MS. WOOTEN: Okay.

Q: All right. Let's go by through -- go through this line-by-line.

THE COURT: You want us to switch to you?

MS. WOOTEN: Please. If, Ms. Buckner, if you could switch us?

MS. BUCKNER: Uh-huh.

Q: All right. Marjorie, let's go by -- go through this line-by-line.

All right. The first sentence says; in order to enhance the earnings of Tractor Supply Company, TSC, we are working with representatives of our accounting firm PricewaterhouseCoopers, LLP, brand PwC, to transform the legal structure of the company.

Does Tractor Supply agree with that statement?

A: Yeah, we were trying to grow our earnings.

Q: Okay.

A: I agree with this.

Q: Okay. Second sentence. Our primary goals are two-fold. First, to accomplish this restructuring in such a manner so as to have little or no impact on the day-to-day operations of Company personnel.

Do you agree with that state- -- or does Tractor Supply agree with that statement?

A: I don't know if I would agree that that was the goal of the restructuring from a primary, but I'm sure that we would've had a goal to make sure that it was -- it -- that it would not've disrupted the lives of, you know, our Company personnel.

Q: The next sentence; the second goal is to have the structure in place by July 1st of this year?

A: And, yes, I would -- I -- again, I wouldn't say that is a goal for restructuring, but it -- it's a, definitely, you know, a plan or -- I guess, it's -- I disagree with the wording, but I didn't write it at that time. I wasn't there at that time. But I would say, yes, they had a desire to put this in place by that time.

Q: The next sentence; the proposed structure is relatively straight forward and involves the formation of two new subsidiaries that will be wholly owned by TSC?

A: Correct.

Q: You agree -- Tractor Supply agrees with that statement?

A: I agree with that statement.

Q: Okay. A description of the proposed structure is as follows, do you agree that that's the, the statement?

(*Laughter*.)

Q: We're gonna go by this -- through this line-by-

line.
A: Yes, Tractor Supply agrees with -- that is the statement.
Q: All right. TSC will form a wholly owned Limited Liability Company in Michigan to own and operate all the stores located in that state?
A: I agree that that is the statement, yes.
Q: According ---
THE COURT: Well, now, what -- that's the statement or was that what Tractor Supply was intending to do?
A: And yes, that's what he -- that's, that's what we intended to do.
THE COURT: Okay.
Q: Accordingly, all of the assets and personnel associated with the Michigan store operations will be transferred to the new Limited Liability Company at the close of business on June 30th?
A: That is not what we did, because technically we didn't transfer the personnel to that entity.
Q: Did you transfer all of the assets?
A: The assets did go.
Q: Okay. So the only clarification you have with

regard to that sentence is the, the transferring of the personnel?

A: Yeah. The transferring of the personnel did not go into the Tractor Supply of Michigan's, I guess, EIN number where it will become the employer of.

Q: Do you have any other -- does Tractor Supply agree with all other components of that statement?

A: It looks -- that looks correct.

Q: Okay. All right. The next sentence; concurrent with the formation of the Michigan Limited Liability Company (hereinafter referred to as the "Michigan LLC") TSC will form a Texas Limited Partnership which will be jointly owned by TSC and the Michigan LLC as a general and Limited Partner respectively.

A: That is correct.

Q: Tractor Supply agrees with that statement?

A: Tractor Supply Company agrees with that statement.

Q: The Texas Limited Partnership will be formed for purposes of operating all store operations, as well as the Distribution Center located in Texas?

A: I agree with that statement.
Q: Does Tractor Supply agree with that statement?
A: Sorry.
Q: That's okay.
A: Tractor Supply Company agrees with that statement, plus, you know, the things that were not in that statement, like the procurement function. But, I agree with that -- those things -- or Tractor Supply Company agrees that the distribution center and the retail store operations were operating underneath, underneath this newly formed Trac- -- Texas Limited Partnership located in Texas.
Q: Accordingly, all of the assets and personnel associated with TSC's Texas store operations as well as TSC's Texas Distribution Center will be transferred to the Texas Limited Partnership hereinafter referred to as the Texas LP at the close of business on June 30th?
A: Correct. I -- TSC agrees with that statement.
Q: Thank you. In addition to the Texas store operations, TSC will transfer the personnel and property associated with the Nashville Merchandising Operations to the Texas LP?
A: TSC agrees with that statement.

Q: Note, the physical location and the place of operation of the Nashville merchandising function will not change?
A: TSC agrees with that statement.
Q: The only change will be the legal employer of these individuals?
A: I don't know if that's the only change, but it's definitely -- like, as far as not disrupting the impact for these team members or individuals performing this function, the legal employer changed.
Q: The Texas LP will assume responsibility -- well, let me go back to that last statement.
You agree with the -- let me go back to this -- the statement again. There may be other changes with regard to TSC, but the -- would you say that the primary change is that it will be the leg- -- the only -- the primary change is that the legal employer of these individuals is now Texas?
A: It's, it's a nuance, but I can't -- with the trademarks transfer, they're associated with the, kind of, the procurement and operations and that sort of thing. They moved to the Texas and -- or were transferred into the Texas

entity, the vendor agreements that, you know, are kind of associated with the procurement function are now in the name of Tractor Supply Company of Texas. The individuals are now working for the employer of Tractor Supply Company of Texas. There are other changes, but a big one would've been the fact that the, the changes, you know, for the legal entity -- or the, the employer of these individuals was going to Tractor Supply Company of Texas.

Q: The Texas LP will assume responsibility for buying all inventory for TSC stores?

A: TSC agrees with that statement.

Q: The Texas LP will be the legal buyer of record for all such inventory, however, the Texas LP will immediately resell the inventory to TSC at an appropriate markup?

A: TSC agrees with that statement, but Michigan would also need to be included in that.

Q: At what part of that sentence would Michigan need to be included?

A: However, the Texas LP will immediately resell the inventory to TSC and TSC of Michigan at an appropriate markup.

Q: Are there any other changes that you would make

-- that Tractor Supply would make to that statement?
A: No.
Q: Delivery terms with vendors will not change?
A: TSC agrees with that statement, other than the name of who they're doing business with, which is now Tractor Supply Company of Texas.
Q: Our goal is not to change the method by which the impacted employees currently do business?
A: TSC agrees with that statement.
Q: To the extent that it is impossible, we intend to make this restructuring transparent to our employees and customers?
A: TSC agrees with that statement.
Q: While we realize that there will be certain necessary changes to operations, again, our overriding goal is to keep these to a minimum?
A: TSC agrees with that statement.
Q: A meeting has been scheduled with representatives of PwC on Thursday, May 17th, to review the actions necessary to accomplish this restructuring and identify, to the extent possible, the issues that will need to be addressed?
A: I guess that happened. Again, based on this,

it appears that that was the intent, so. TSC agrees with that statement.

Q: I would ask that you begin considering any questions or concerns that you may have so that we can begin addressing these as soon as possible.

A: TSC agrees with that statement.

Q: Thank you.

MS. GEER: Nothing further, Your Honor.

THE COURT: All right. You may step down. Apparently, you're gonna be back, but. It's 12:46 by my computer. Why don't we just be back at 2:00, is that good enough?

MS. WOOTEN: That's fine with the Department, Your Honor.

MS. GEER: That works.

MS. WOOTEN: Thank you.

THE COURT: Okay. Thank y'all.

(Off the record from 12:48 p.m. until 2:02 p.m.)

THE COURT: Ms. Wooten?

MS. GEER: Your Honor, just -- we're having an issue connecting to the internet right now. So just for purposes of being able to pull up exhibits and stuff, if you could give us one minute?

THE COURT: Okay.

(*Whispering*.)

THE COURT: Go on. Are y'all connected?

MS. GEER: It looks like it -- no.

(Whispering.)

MS. GEER: Although, we might be close to at least one computer, and it's the more important computer, so. Oh, there it goes.

THE COURT: Mr. Von Lehe, your computer's already online, right?

(*Laughter*.)

MR. VON LEHE: Yes, Your Honor, thank you. It is indeed. At least, I hope so.

(*Whispering*.)

THE COURT: (Whispering) Katie, do you think we should give it over?

Does our computer person need to come down?

MS. GEER: No, I think, I think I might've just gotten it on mine. Hold on one second.

All right, Your Honor. We've got at least one up and running, and I think we'll be okay to get started.

THE COURT: All right.

MR. LUTHER: All right. At this time, the Department would call Orville Sharpe.

THE COURT: Okay.

OBJECTION:

MS. GEER: Your Honor, I hate to start off the afternoon after lunch with an objection, but Mr. Sharpe was not identified as a witness in the Department's Answers to Interrogatories. They did offer him as -- when Tractor sent a 30(b)(6) Notice, he was offered as a witness on behalf of the Department for purposes of the 30(b)(6) Notice, but he -- it was never -- he was never added as a witness on the -- in the Interrogatories as to what he would testify to. So, I'm okay with him discussing topics that he discussed in his 30(b)(6) Notice because he, he did those ---

MR. LUTHER: Yes, but ---

MS. GEER: --- but I, I would object to anything that goes beyond that scope.

MR. LUTHER: And that's fair. And she's correct. In the initial Interrogatory responses Mr. Sharpe was not identified as a fact witness because he did not participate in the audit. He was a designee in the 30(b)(6) deposition. The topics he's gonna cover today are the topics he covered in the deposition.

THE COURT: Good. Proceed ahead.

COURT REPORTER: Mr. Sharpe, if you'll raise your right hand.

MR. SHARPE: (Witness complies.)

COURT REPORTER: Do you swear to tell the truth, the whole truth and nothing but the truth, so help you God?

MR. SHARPE: I do.

COURT REPORTER: Thank you.

MR. SHARPE - DIRECT EXAMINATION BY MR. LUTHER:

Q: Good afternoon, Orv- -- Mr. Sharpe.

A: Good afternoon.

Q: Or as we learned at lunch, you go by Mike sometimes, right.

A: (Laughter.) Right.

Q: What is your role -- or who do you work for?

A: I work for the South Carolina Department of Revenue.

Q: Okay. And I want to get a little bit of background from ---

A: Okay.

Q: --- you before we get into that. Can you tell me just a little bit about your educational background?

A: I graduated in August of 1975 with a BS -- a major in accounting in the University of South Carolina. And then I worked for a bank as internal auditor for two and a half years. And then in April 1978 I started working for the South Carolina Department of Revenue and I've been there ever since, it'll soon be 45 years.

Q: And if you don't mind, just lean in a little bit to the mic ---

A: Okay.

Q: --- so we can hear you.

A: Okay.

Q: So, you have been at the Department of Revenue sin- -- Revenue since 1978?

A: April 1978.

Q: And what roles have you had during your time at DOR?

A: I started as a Sales and Use Tax Auditor, and I did that until the early 90's. And then I became a Multistate Corporate Income Tax Auditor.

Q: Do you have any specialized training?

A: I have a -- I'm a CPA, and I got my CPA in -- I think it was '95 or '96. No, I'm sorry, in the -- in early 90's.

Q: Okay. And do you maintain that license?

A: Yes, I do.
Q: So you have testing I gue- -- or training you have to go to throughout ---
A: Yeah, you have to take 40 CPE hours every year.
Q: Any other specialized training or certificates?
A: No.
Q: What is your current title?
A: I'm a -- we call it -- we -- the Corporate Multistate Section, we call the Foreign Audit Section, I'm a Foreign Audit Supervisor. I supervise six foreign auditors.
Q: And what are the responsibilities of the Foreign Audit Section?
A: I help select the audits that they audit, and I approve their audits. And I help in the training of the auditors and I perform various other administrative functions.
Q: How long have you been a supervisor?
A: April -- I'm sorry, not April, October, 1998. And by the way, in my deposition I think I said October, 1999, but it was actually April 19, 19- -- not 1998 or 1999, 2018.
Q: Thank you.
A: October of 2018 is when I became a Foreign Audit Supervisor.

Q: But since you came to the Department in '78, all of your roles have been in the audit capacity?
A: Correct.
Q: Okay. Actually, I heard earlier that Judge Anderson may be offering you for -- or people for promotions as part of his Order, so I don't know if this is a good time for you to put anything on the record about -- do you want to be the VP of tax anywhere?
A: No, sir.
Q: Okay.
A: I, I just, I just hope I can, I can -- my goal is to work 50 years at Department of Revenue, so I'm hoping my health will ---
THE COURT: Five more years?
A: 50 years.
THE COURT: I said, you've got five more years to go?
A: Five, five more years. I'm hoping my health will hold up, or -- of course, if I win the lottery, I'm gone.
(*Laughter*.)
Q: Let's hope you don't win it this afternoon.
What is your training experience in the

multistate taxation area?

A: When I started doing multistate tax auditors, it was basically on-the-job training with another auditor and/or other information I received from my supervisor, and information we received during auditor meetings. But I've also attended a good number of classes from the Interstate Tax Corporation and they deal with multi-stack -- multistate taxation. And also MTC has put on a -- two unitary combination classes for the Department of Revenue. One was -- I'm, I'm pretty sure it was in 2010 shortly after the *Media General* case, and then they did it again because we have so many new auditors and I think it was in 2019 when, when I attended that class. And, as I mentioned earlier, as a CPA you're required to take 40 hours of CPE every year and a lot of that deals with corporate income tax, but not so much with multistate taxation, which is fairly unique.

Q: You just used an acronym MTC. Can you explain what that is?

A: Multistate Tax Corporation, I believe. I just always call it the MTC.

Q: But -- okay. How many corporate tax audits do you think you've done in your entire career?

A: Over 1,000, I would guess.

Q: How many of those audits involved alternative apportionment?

A: I would say, maybe, about 15.

Q: Of those alternative apportionment audits, how many involved combined reporting?

A: I would say about ten.

Q: Okay. Is there anybody in audit that has done more combined reporting audits than you at the DOR?

A: I don't think, I don't think so.

Q: All right. I want to talk a little bit about allocation and apportionment.

A: Okay.

Q: Tell me in your words what allocation is?

A: Allocation is non-business income that's allocated away from the apportionable base, and it might -- and, and it includes real property gains and lo- -- and losses, which are statutor- -- statutorily defined in South Carolina as non-business income. But it would be things that don't really pertain to the taxpayer's business. It's, it's normally considered investments of their -- of their asset -- excess assets and receipts.

Q: What is apportionment?

A: Apportionment is the, the method we use to source the apportionable base to South Carolina.

Q: So what is the purpose of allocation and apportionment?

A: Determine how much net income the taxpayer should report in South Carolina.

Q: Are you familiar with Section 12-6-2320(A) of the South Carolina Code?

A: Yes.

Q: What does that Code section have to do with allocation and apportionment?

A: It, it basically says it's -- if the allocation and apporth- -- apportionment methods -- if the standard allocation and apportionment method does not fairly reflect the taxpayer's business in South Carolina, the, the taxpayer may request and the Department require an alternative apportionment method that is reasonable.

Q: And, and what is the standard method in South Carolina?

A: The standard method is either a sales or gross receipts method. If you're in the business of selling tangible personal property or manufacturing, then you're required to report on one factor, the sales factor. If you're in the business of providing a -- services, you're required to report on one factor, gross receipts. And so the, the numerator is the South Carolina sales and the denominator is the everywhere sales.

Q: Are you familiar with the *Media General* case?

A: Yes.

Q: Why, why -- for audit, why is *Media General* an important case?

A: Well, South Carolina was arguing in that case that under the other ---

OBJECTION:

MS. GEER: Your Honor, I would object to the extent that he's gonna testify about what the law is. I'm -- just because that's a question of law. I'm fine with him discussing how the Department applies it, but I just want to out that objection on record.

THE COURT: How about if you -- just where I've -- understand the proper ruling, do you object to him testifying about why *Media General* is important for the Department?

MS. GEER: Yeah, maybe, I missed -- why is -- as long, as long -- I mean, I don't mind him saying why he thinks it's important, so that ---

THE COURT: Yeah.

MS. GEER: --- question is not necessarily. But it sounded like what he was getting ready to say is what *Media General* did, that's was ---

THE COURT: Okay.

MS. GEER: --- made me object.

Q: Yeah. So, Mr. Sharpe, I'm just curious, as we're talking about this topic of alternative apportionment, why, especially from the audit perspective, what impact did *Media General* have on how you conduct audits of multistate corporations?

A: As a result of the *Media General* case, the ruling said that unitary combinations were a method that we could use when we require equitable apportionment.

MS. GEER: And again, Your Honor, he's saying it said --

THE COURT: Yeah.

MS. GEER: --- blah, blah, blah. That's the part

I'm objecting to, of him saying what the law it.

MR. LUTHER: I, I think he's allowed to testify from the perspective of the Department how they understand a Rule to be -- or what it ---

THE COURT: Well, why don't you just ---

MR. LUTHER: But I can ---

THE COURT: I'd like his testimony and, and ask the question again and let's get it out ---

MR. LUTHER: Sure.

THE COURT: --- where it's clear.

MR. LUTHER: Well, I -- let me just -- maybe, I'll do it a different way.

THE COURT: Okay.

Q: What is, what is a unitary business?

A: A uni- -- a unitary business a bus- ---

OBJECTION:

MS. GEER: Your Honor, I'm sorry. Objection if he's calling for a legal conclusion. If he's asking on a factual basis or how the Department applies it, I'm okay with it.

THE COURT: I assume everything he's asking is from the Department's standpoint, but -- (To Mr. Luther) do you have a response to that?

MR. LUTHER: Well, all right. I'll rephrase it a little bit differently, although I think we're gonna get back to the same point.

THE COURT: Okay.

Q: *Media General* -- let me ask this. When did Media -- when was *Media General* decided?

A: I -- in, in 2010. I'm not sure of the exact -- I think, the month, but I think -- I'm pretty sure it was 2010.

Q: Okay. And when you're auditing a multistate tac- -- a multistate corporation, do you ever consider whether it is a unitary business?

A: Yes.

Q: Okay. And when you're considering whether it's a unitary business, what does that mean in your mind?

A: It, it means that there is a flow, a flow of values among the unitary group that -- through functional inter- -- integration, economies of scale and centralization of management.

Q: Okay. And how does combined unitary reporting impact a unitary business, what relevance does it have to it?

A: It requires that the apportionable base ---

OBJECTION:

MS. GEER: Again, Your Honor, if it's his understanding of what the law requires, I'm good with it. If he's saying what the law does, that's the part I have a problem with.

THE COURT: Any response?

MR. LUTHER: I mean, I guess, you're gonna hear testimony all week about these cases, this statute, and how does the Department interpret and apply them. Those were the topics that were listed in his deposition.

MS. GEER: And, and I ---

MR. LUTHER: I assume that he's able to testify about how the Department understands the law that it's applying.

MS. GEER: I am totally fine with him saying how he understands the law. The way he's phrasing his answers are, this is what the law does, so if we want to have a running, you know ---

MR. LUTHER: I mean, I can rephrase it.

Q: Mr. Sharpe, what is your understanding of how combined unitary reporting should be used with a unitary business?

A: The apportionable base changes to include the federal taxable income for all -- the unitary group and the, and the apportionment ratio changes to include in the sales and everywhere factor, an elimination of all intercompany receipts.

Q: Okay. Are you familiar with the *CarMax* case?

A: Yes.

Q: Are you familiar with the *Rent-a-Center* case?

A: I'm more su- -- I'm more familiar with *CarMax*, because that was my -- that -- I was the auditor on that case.

Q: Okay. Again, from, from your perspective as the Department auditor, did *CarMax* or *Rent-a-Center* have any bearing on alternative apportionment as you apply it?

A: Yes. *CarMax*, especially.

Q: Did they involve combined reporting?

A: No.

Q: Are you familiar with Revenue Ruling 15-5?

A: Yes.

Q: And I may call it the 15-5, but you understand what I mean?

A: Yes.

Q: Okay. What is Revenue Ruling 15-5?

A: Revenue Ruling 15-5 is a policy document that came out as a result of taxpayers who wanted some guidance on, on how the -- South Carolina would utilize alternative apportionment, and specifically unitary combinations. It provides a recap of our, our statutory reporting method and if we -- if the taxpayer's business doesn't fairly operate in South Carolina, then it shows what it -- how you would compute a unitary combined return in South Carolina.

Q: Okay.

A: And it lists a lot of different factors that you may look for to determine if the taxpayer's reporting method fairly reflects their business operation in South Carolina.

Q: All right. You said it was issued to provide guidance to the public?

A: Exactly.

Q: I don't want to go into a lot of detail, but, just generally speaking, what sort of particular guidance does 15-5, 15-5 offer?

A: Well, it gives, I think, it's six reasons that, that might be considered for alternative apportionment, including unitary combinations. And it discusses some particular tax shifting strategies where the Department has required unitary combinations, and it gives a detailed write-up of, of specific items that, that spefic- -- specific things that you do to compute the taxpayer's net income -- South Carolina net income on -- unitary combination.

Q: Does 15-5 offer a definition that the Department is using for what constitutes a unitary business?

A: Yes.

Q: Does it provide -- I think you mentioned some of this, but just to clarify, does it provide some guidance on how combined reporting would be calculated?

A: Yes.

Q: Can you walk me through how an auditor would calculate the taxable income of the taxpayer in a situation where there asserting combined reporting?

A: Okay. Let me take a drink of water first.

Okay. You start with the federal taxable income for the unitary combined group, and then you, you modify that amount by the South Carolina modifications. And the South Carolina modifications are ad-backs or subtractions from the federal taxable income for items in the Internal Revenue Code that South Carolina has not adopted. You come up with the reconciled federal taxable income, and then you apply the everywhere non-business allocations to that amount, which can be a positive or a negative, to come up with the unitary apportionable income, and then you multiply the unitary apportionable income by the unitary combined ratio to come up with the South Carolina net income before direct allocations, and then you'll apply South Carolina direct allocations, which again, can be a positive or a negative, to come up with the South Carolina net income. And the apportionable base where unitary combination does not include any intercompany receipts or deductions in the, as I indicated previously, the South Carolina numerator and the everywhere denominator does not include any intercompany receipts.

THE COURT: So it's simple?

(Laughter.)

A: It's pretty simple once you've done it a hund- -- a thousand times.

THE COURT: Well, maybe for you (laughter).

Q: Now, I know why you had to take some water before you answered.

Are you familiar with the terms qualitative analysis and quantitative analysis?

A: Yes.
Q: Tell me, what is qualitative analysis?
A: Qualitative analysis is -- and this is in regard -- I'm assuming it's in regard to an alternative apportionment method that ---
Q: Yeah.
A: --- we proposed. Qualitative analysis is basically a summary of the taxpayer's business. It's, it's just a nar- -- it's a narrative form and you talk about the taxpayer's business within and without South Carolina, and you talk about their entities that are filing in South Carolina, the entities that aren't filing, and you talk about the intercompany transactions. And you will actually list a summary of their intercompany agreements and if they have a 482 or a transfer pricing study you'll the summary of that. And then you'll try to connect all the dots and explain why you think that the statutory -- or the standard apportionate -- apportionment method of the -- of taxpayer does not fairly reflect their business activity in South Carolina, and then you describe the alternative method that you propose and you provide statutory support for your adjustment.

Q: What is a quantitative analysis?
A: Quantitative analysis is more of a mathematical computation where you compare the entities reporting in South Carolina and the not -- entities not reporting into -- in South Carolina. So, you compute these various, what -- we call them distortion ratios, so you can compare the entities filing in South Carolina -- the ones -- and the entities who are, are not filing in South Carolina. These are generally the entities who receive all the income, or the entities not filing in South Carolina. And some of these ratios are -- and there's a bunch that you could use, net taxable or federal taxable income return on receipts, federal taxable income return on income, federal taxable income return on payroll, federal taxable income on assets and gross profit margin, etcetera. There's a, there's a ton that you can possible use.
Q: Okay. When an auditor finishes an audit, do they provide a write-up or an explanation of their findings and conclusions ---
A: Yes. So ---
Q: --- to the taxpayer?

A: They -- we, we always send the taxpayer a preliminary draft of, of our, our potential adjustments. We call it preliminary and it's potential -- to give the taxpayer time to review what our potential adjustments are and, and the time frame is usually a month, and then they respond back and we discuss what, what their potential adjustments are. And then, after that point we, we finalize the audit and submit a, a dra- -- of the final audit to the taxpayer after it's been written up and reviewed by -- and signed off by the supervisor.

Q: Is that done in every audit, like, not just including alternative apportionment audits ---

A: Every ---

Q: --- as you just described?

A: Every audit.

Q: Okay. And has that been a process for as long as you've been at DOR?

A: As long as I can remember, yes.

Q: Is there any significant difference between the write-up and the explanation you just described and the qualitative analysis you described a minute ago?

A: No. No, they're the same thing.

Q: Were you involved in this audit of Tractor Supply Company?

A: No.

Q: Have you reviewed the audit since it was completed?

A: Yes.

Q: Are you generally familiar with the issues raised in the audit?

A: Yes.

Q: What is your understanding of what the taxpayer's business activity is in South Carolina?

A: Their -- I think their South Carolina and everywhere business activity is selling at retail -- at their retail locations within and without South Carolina.

Q: Okay. When the Department required combined reporting in this case, how did it utilize the sales factor when it apportioned income?

A: Can you repeat that question?

Q: Yeah. Are you familiar with how the Department, in this audit, utilized the sales factor?

A: Yes.

Q: And how did they, how did they use that when they were apportioning income for Tractor Supply Company?

A: Well, you're talking about in the audit, not in ---

Q: Yes.

A: --- it's file? Okay. So -- well, on a -- under a unitary combined basis, the sales ratio in the numerator, in the denominator includes -- for the sales ratio it only includes the sales for the South Carolina locations here in South Carolina, and it doesn't include any intercompany receipts, and the denominator -- or the everywhere sales includes the sales in the whole -- for the whole enter- -- for the whole unitary enterprise less any intercompany receipts.

Q: And I want to make sure I'm clear. Is that the same process you used for Tractor Supply in this audit, that same formula you just described?

A: Yes.

Q: Okay. Whose income was apportioned in the Tractor Supply audit?

A: The income was apportioned is the income for the unitary group after eliminations of intercompany transactions.

Q: And explain to me why you would use the income of the unitary group?

A: In this situation when, when the taxpayer's shifting income from the South Carolina entity that's filing, that's the only way -- I believe, the only way you can determine their business activity in South Carolina is to take the complete base after you eliminate all the intercompany, intercompany receipts and deductions and then multiply that times the unitary -- the unitary combined apportionment ratio which, of course, in the numerator for South Carolina, it only includes the South Carolina activity, so you're only taxing the South Carolina activity.

Q: So -- and that was kind of my next question. When you include the combined income of the unitary group in the denominator, how does that affect the apportionment ratio?

A: It -- the apportionment ratio usually goes down because they -- the every -- the denominator will be increased by all those other receipts for the other locations that are not in --

included for the separate entity reporting of Tractor Supply.

Q: All right. I want to ask you about the procurement sales -- the receipts from the procurement sales between TSC of Texas and Tractor Supply and TSC of Michigan. Are you familiar with those receipts?

A: Yes.

Q: Okay. Did the Department ever consider adding those procurement sales into the denominator of the sales factor?

A: No, because that would violate the whole unitary combined filing principle, which the meth- -- the purpose of the unitary combined apportionment method is to eliminate all intercompany receipts and in the -- and deductions from the apportionable base and eliminate all intercompany receipts from the numerator and denominator. In this situation, that's the only way you can determine the true South Carolina net, net income.

Q: All right. But I'm trying to understand, if you're trying to represent all of the business activities of the unitary group, then why wouldn't you include the procurement sales in

the denominator in addition to the retail sales?
A: Well, that would be ridiculous as I indicated before, because it violates the whole unitary combined apportionment method. That's the purpose of the unitary combined method is to determine the true income of South Carolina. If you include that in there, you're gonna, you're gonna distort the South Carolina net income by increasing the denominator and thereby reducing this -- the apportionment ratio.
Q: So did the, did the Department ever perform any analysis to see how much income would be apportioned to the State if the procurement sales had been included in the denominator?
A: No, it wasn't necessary for the reason I just, I just discussed.
Q: Okay. Mr. Sharpe -- well, hold on just a second. I may ...
Mr. Sharpe, that's all I've got for you. You can answer any questions from ---
A: Okay.
Q: --- the other party.

MR. SHARPE - CROSS EXAMINATION BY MS. GEER:

Q: Good afternoon ---
A: Hey.
Q: --- Mr. Sharpe, how are you?
A: Fine; how are you doing?
Q: Good. I'll get situated here. So you said -- I believe you said you were not involved in this audit in any way, is that correct?
A: Correct. Except, you know, just reviewing it and being deposed ---
Q: Okay.
A: --- etcetera.
Q: Had you heard anything about this particular audit until this litigation?
A: I probably heard people talking about it, but I didn't really know the, the facts ---
Q: Okay.
A: --- of the ---
Q: All right.
A: --- the case.
Q: And you mentioned -- I think I might've misheard something, but you mentioned something about ten com- -- that you had performed ten combined unitary reporting audits?
A: Well, I ---
Q: Did I hear that right?

A: 10 to 15, something like that.
Q: 10 to 15. But then you said something about performing thousands of combined unitary -- what -- yeah, I think I missed something on there. What was the ---
A: You ---
Q: --- thousands ---
A: He said -- he asked me ---
Q: --- you're referring to?
A: --- how many corporate income tax audits I have -- that I had -- I conducted, and I said probably over 1,000.
Q: Okay. So 1,000 audits, but only ten involving combined unitary reporting?
A: Right.
Q: Okay.
A: 10 ---
Q: Thank you.
A: --- to 15 is what, is what I would ---
Q: 10 to 15.
A: --- guess.
Q: Yes. Thank you.
A: Is what I would guess.
Q: Okay. And you discussed the quantitative analysis ---

A: Right.

Q: --- portion, and you talked about it being a mathematical computation and the di- -- there are some distortion ratios where you can compare different figures.

A: Correct.

Q: Are you aware that those were not used in this case?

A: Yes.

Q: Okay. So we didn't have any quantitative analysis performed in this, this audit?

A: Not that I'm aware of.

Q: Okay. All right. And then, I think I heard this -- I think I heard you say that the business activity in South Carolina of the taxpayer is selling retail within and without South Carolina, did I hear that right?

A: I'm not sure. But I meant that the business -- the retail business activity of, of the taxpayer, I think they own, they own some disregarded entities that also had sales outside of South Carolina, so yes, that would've been correct, because the taxpayer had disregarded entities. I think pretense [sic] was one of them and they had locations within and outside of South Carolina. So, yes, the taxpayer would've been -- be selling at retail within and without South Carolina.

Q: Okay. But what, what -- maybe I'm -- I probably did not articulate my question well. What are the taxpayer's business activities in South Carolina, only in South Carolina?

A: Only in South Carolina?

Q: Yes.

A: Selling at, at retail.

Q: And you talked a little bit about the difference between -- I remember you talked about separate entity reporting and combined unitary reporting?

A: Right.

Q: Those are, those are two filing methods, correct?

A: Correct.

Q: Okay. And you understand that South Carolina has chosen separate entity filing as its filing method in South Carolina, correct?

A: It's the standard reporting method, yes.

Q: And are you aware that many of South Carolina's neighboring states are also separate entity reporting states?

A: Yes. I think most of the southeastern states are separate entity reporting states. But most of the states in the United States are, are unitary combined states.

Q: Yep. Are you aware that the South Carolina Department of Commerce touts South Carolina as being a separate entity state?

A: I, I remember reading that on the reds -- on the website, but it says, generally, from what I read, indicating that if unitary -- if a force unitary -- to me it indicates that -- I think it says, generally, so it leaves open the fact that if the taxpayer is shifting income from one entity to the next, an alternative method including a unitary combination may be applied. But it doesn't say -- it says generally.

Q: Right. Well, are you -- so, so generally, the Department of Commerce, you're saying, is touting that South Carolina is a separate entity state?

A: Right.

OBJECTION:

MR. LUTHER: Your Honor, I'm gonna object. These are not questions that were asked and they're not within the scope of the topics that Mr. Sharpe was identified as in his deposition, so if we're gonna limit his testimony to the topics, then I think the cross actually has to be limited to the same scope.

THE COURT: Well, she could open -- she could also be opening the door ---

MS. GEER: We ---

THE COURT: --- for you to -- on re-direct. I mean, it goes two ways.

MR. LUTHER: I understand.

THE COURT: Okay. Any response to that?

MS. GEER: I mean, he talked about that he -- the differences -- you know, separate entity reporting versus combined unitary reporting, I think I'm entitled to explore his understanding of it.

THE COURT: I'll let you go into it.

MS. GEER: Okay.

Q: And are you aware that South Carolina and its other neighboring states like to tout that separate reporting -- their state is separate reporting for economic development reasons?

OBJECTION:

MR. LUTHER: Objection. That calls for speculation.

THE COURT: Yeah, I ---

MS. GEER: I can ask him if he's aware of it, if he doesn't -- if he's not aware of it, he can say he's not aware of it.

THE COURT: Is it relevant? I mean, I ...

MS. GEER: I, I think it's of interest as to why the State -- our legislature has made a decision to have separate entity reporting as its chosen filing method.

MR. LUTHER: I think it's double speculation. We're speculating about whether they tout it, and now we're speculating about the intent of the General Assembly in each state.

THE COURT: Yeah, I ... I'm gonna su- -- I'm gonna let you respond.

MS. GEER: Let me ref- -- let me rephrase it ---

THE COURT: Okay.

MS. GEER: --- and see if I ---

THE COURT: All right.

MS. GEER: --- address any issues. I probably won't (laughter). I'm gonna try.

Q: Are you aware -- do you know one way or the other, from your own knowledge based on your many years, I think we -- I think I heard you say 50, almost 50?

A: 50's my goal.

THE COURT: 40 ---

Q: Trying to get to 50.

A: 50's my goal.

Q: Trying to get ---

THE COURT: 45, right now.

MS. GEER: 45, right now.

Q: So, 45 ---

THE COURT: Or 44.

Q: --- years since you've been involved in, in audits, and in -- I'm sure you've had lots of training on separate entity versus combined reporting and the Revenue Ruling of when to apply combined reporting when we're in a separate entity state. So, I think you've established that you're knowledgeable about those issues, would you agree?

A: Yes.

Q: Okay. And so in -- based on that knowledge and experience, are you aware of whether South Carolina is a separate entity state that one of the considerations is economic development reasons?

A: For South Carolina only?

Q: Yeah. Yes.

A: Yes. As I indicated, I'm aware of -- that they say that they're, generally ---
Q: Right.
A: --- a separate enti- -- endi- -- entity state.
Q: Right.
A: But that leaves the opening, opening for alternative apportionment when the taxpayer is shifting money from one entity to another entity, so that the method they report to South Carolina does not fairly reflect their activity in South Carolina.
Q: Right. And so, the reason to tout it on your website for South Carolina would be you're, you're wanting to encourage businesses, hey, we're -- South -- we're South Carolina, we're a separate entity state. It may not always be imposed, is what you're saying, but the reason to tout it is, we're wanting to let businesses that are interested in coming to South Carolina know that in South Carolina most of the time, or generally, I think you said, we're a separate entity state?
A: Right. If they ---

OBJECTION:

MR. LUTHER: And I'm gonna object again. It's a long compound question, number one. Number two, she said your website, and I think she means ---

MS. GEER: I, I did not mean ---

MR. LUTHER: --- the Department of Commerce.

MS. GEER: Yes. Please ---

THE COURT: You know, that was ---

MR. LUTHER: And I think -- and I, again, would lodge the objection, the Department of Commerce and the State are not necessarily one and the same.

THE COURT: Right. He cannot testify about the reasoning for the Department of Commerce's website, unless she can lay a foundation that he knows about the Department of Commerce's website.

MS. GEER: I think he already testified that he's aware of the website and, and knew that it was on the website.

THE COURT: Well, I'm talking about he'd have to testify that he knows the reasons behind why they put ---

MS. GEER: Okay.

THE COURT: --- what they do on the website.

Q: Are you aware of the reasons why the Department

of Commerce would tout separate entity reporting on their website?
A: I can, I can guess, but I'm, I'm not aware of the reasons.
Q: Okay. All right. And then, you talked about the statute, the Alternative Apportionment Statute 12-6-2320. Do you agree that under the Alternative Apportionment Statute it can only be used when the standard method of apportionment does not fairly represent the taxpayer's business activity in the State?
A: Can you repeat that question again?
Q: Yeah. Do you agree that the Alternative Apportionment Statute can only be used when the standard method of apportionment does not fairly represent the taxpayer's business activity in the State?
A: Yes, I agree with that.
Q: Okay. And does it also -- does the alternative method chosen also have to be reasonable?
A: Yes.
Q: Okay. All right. So let's go -- those were two, two parts there. I'm gonna go back to step one.

Step one is to determine whether the

standard method fairly represents the taxpayer's business activity. If it does fairly represent the taxpayer's business activity in South Carolina, then the analysis would end and you would not invoke alternative apportionment, correct?

A: Correct.

Q: So you, you mentioned earlier that the retail activity of the taxpayer -- of Tractor Supply or TSC as we've been referring to it today, is the retail stores. How did -- you've rev- -- you've reviewed the audit report, correct? How did the audit report measure those business activities?

A: I'm not sure I followed your question.

Q: Okay. So the standard apportionment statute, one of the things you're trying to figure out in step one, is whether the standard apportionment method fairly represents the taxpayer's business act- -- activities in South Carolina, right?

A: Correct.

Q: Okay. And so you've told me that the taxpayer's business activities in South Carolina are the retail stores?

A: Correct.

Q: Okay. So if you're trying to figure out if it's fair, like, how did the audit report attempt to measure that activity, that business activity, that was in South Carolina?

A: Oh, okay. Well, by the fact that, that all -- most of all the income is shifted from, from Tractor Supply Company to the procurement portion of Texas, so that's how you, you measure it.

Q: Okay. So you're -- I think we're talking about two different things, maybe. You're talking about the income, and I want to talk about the business activities.

A: But that is the business activity. The business activity for -- is on -- the whole enterprise only has one business activity.

Q: Uh-huh.

A: That includes Tractor Supply of Texas, that includes Michigan ---

Q: Okay.

A: --- and that includes Texas. They only have one, one business, that's selling at retail. Procurement is not a business of any of these entities, it's just a cost center that they're, they're marking up and charging to the entity in South Carolina. There's only one, one business activity, that's selling at retail, and that's how they did it. They -- they're trying to look at what is this company's doing, they're only selling at retail, how do we determine what, what the South Carolina activity is? You have to eliminate those transactions to the procurement entity, because they are not selling at retail in South Carolina.

Q: Okay. So, you're saying that you, you don't respect that Tractor Supply Texas is a separate entity?

A: That's not what, that's not what I said. I said their business activity.

Q: Okay.

A: They only have one business activity. In South Carolina, their only business activity according to their 10-K is selling at retail. They say nothing about a unit that generates income via a procurement fee. There's nothing in their, their 10-K that reflects that income.

Q: Okay. Well, let me, let me make sure I, I understand. So you don't dispute that

procurement activities are taking place?
A: No.
Q: Okay. So, you agree that employees of Tractor Supply Texas -- I don't know if you were in here when Margie McKeown testified earlier and talked about different procurement activities?
A: Yeah, I think I was in here.
Q: Okay. I think you were, too. So, you know, the buying, the development of products, all those types of things, you don't dispute that someone is doing those within ----
A: Yeah, it's just the cost ---
Q: --- Tractor Supply of Texas?
A: It's the cost for, for the whole enterprise.
Q: Okay.
A: It's the -- I don't see how, how it would be able ---
Q: So you ---
A: --- to generate all this huge profit, but it's just a cost center.
Q: Okay. So, you are viewing the activities that are performed by the procurement team in Texas, you don't view those as business activities, you view those as a cost?
A: I've -- no, I, I -- as a cost, right.

Q: Okay.

THE COURT: So I can understand your testimony. Are you saying that their selling at retail -- they being Tractor Supply, selling at retail in South Carolina, but your -- or the Department's position was that they were also making profits on the procurement?

A: Well, what I'm saying is that the -- they -- based on separate entity reporting, Texas makes a 9.7 percent markup.

THE COURT: Okay.

A: But in reality, that's not their real income, 'cause that procurement entity actually earns zero income because it's a cost center, it's -- all it is a cost center. If you look at their 10-K, they only report their, their sales from retail sales, it says nothing about some procurement entity that's earning this huge amount of profits so much that the entity reporting in South Carolina does not reflect their true activity in South Carolina, because all their income -- or most of the income has been shifted to this entity reporting in Texas.

THE COURT: So you -- your position is, it's been shifted to Texas via the 9.7 percent?

A: Yes. Yes, sir.
THE COURT: All right. Okay.
Q: In cases where a taxpayer has intercompany transactions ---
A: Right.
Q: --- is your opinion that distortion exists regardless of whether those transactions are priced at arm's length?
A: (No audible response.)
Q: In other words, let me ask you another way so it's maybe a little clearer.
If an intercompany transaction involves a charge that is determined to be at arm's length, does that change your opinion about whether there's income shifting?
A: It might, but it depends on the circumstances.
Q: Okay. Well, let's say, in this particular case, that -- let's say you got -- you picked your transfer pricing expert that you trusted and that transfer pricing expert said, Orville, these are arm's length rates between procurement and Tractor Supply. Would that impact your decision? And if not, tell me what ---
A: Well, at our, at our level, we -- really,

really wouldn't look at the transfer -- we -- the transfer pricing -- the auditors or the supervisors, we look at the, the general operations to determine what they're doing, we don't deal with the transfer pricing. When it goes to appeals or litigation, that's the time that they hire these experts to come forward and explain why the, the intercompany -- the transfer pricing is not correct or is correct.

Q: Okay.

A: And I think in this ca- -- this situation, we're gonna probably have to do one of the experts who are gonna, like ---

Q: Talk about that later?

A: Yeah.

Q: Yeah.

A: That's something we don't deal with at the audit level, because you know how cheap the State is. You -- I mean, if you ever worked, worked with the che- -- with the State, but we can't afford those experts. We're lucky to get the auditors that we have based on the salary that, that we pay. If we wanted to have a team that did -- at the audit level, did these transfer pricing studies, we just can't afford it, because you have to buy the software and the comparables and most of these people who I've seen in these trials are basically PhD's, so they -- they're probably making like 10 times more in- -- than the lowly auditors and the audit supervisors are making. So South Carolina hasn't invested in, in hiring these experts, mainly because we can't get them. We don't pay as -- the State doesn't pay enough.

Q: So at the audit level, you're not, you're not -- it's not relevant to you whether the charges at arm's length or not?

A: Well, I can usually -- I usually have an opinion one way or the other where I think they're, they're relevant, but I never comment on that because I'm not a expert in it.

Q: Okay. Well, let me ask, let me ask a different question.

So, if Tractor Supply, instead of paying Tractor Supply of Texas, had used a third party -- I don't know if you heard the testimony earlier today that they had used some other distributors for procurement, third parties, for certain procurement activities prior to this restructure. So, if they had paid -- if they had not done the restructure and they had just strictly gone with third parties and paid a third party for the procurement function, would you call that a shifting of income, for them to pay money to the third party?

A: Well, how much are they paying to the third party?

Q: Whatever the third party charges them.

A: Well, well -- no, I wouldn't call that a shifting, but I can say this, they wouldn't pay the 9.7 percent markup, 'cause they wouldn't be in business very long if they did.

Q: All right. Well, what I'm trying to get is just the, the basic fact of, if a taxpayer pays a third party it's totally unrelated, there's no question that they're unrelated ---

A: Right.

Q: --- if they pay them for that -- for a procurement function and then that cost that they paid goes onto their return as a deduction, does the Department have any complaint with that, whether income shifting or improper deduction or anything else?

A: No.

Q: Okay. And to follow that a step further, I'm assuming that in that situation, you also -- the Department also would not claim, based solely on that payment to the third party, that Tractor Supply's business activity in this state was not fairly represented?

A: It depended if that was the only ---

Q: And I, I am limiting it just to that one factor ---

A: Oh, yeah. Right.

Q: --- so you don't have to worry about anything else.

A: Right.

Q: So you would agree that ---

A: Yes.

Q: --- in that situation the Department would not claim that there was ---

A: Right.

Q: Let me just finish, just, just so we got ---

A: I'm sorry.

Q: --- a clean record.

A: I know, you told me -- you know what, you told me that in the deposition to quit ---

Q: I know.

A: --- to quit cutting you off.

(*Laughter.*)

Q: It's okay. It's okay.

All right. So, in the situation where Tractor Supply pays a third party for the procurement functions, the Department would not take the position that Tractor Supply's business activity in South Carolina was not fairly represented by the standard apportionment method?

A: Yes, if that was the only transaction we're talking about.

Q: Okay. Thank you. And you talked about Revenue Ruling 15-5. Do you agree that under Revenue Ruling 15-5, combined reporting is not automatic for a unitary business?

A: Correct.

Q: Okay.

(*Whispering*.)

Q: So back to the Alternative Apportionment Statute. So we've talked about step one, and looking to see if the taxpayer's business activity is fairly reflected in South Carolina. And if it's not, then the language of the Statute is, the taxpayer may petition for, or the Department may require an alternative method. So, would you agree that it is optional as to whether the Department would impose an alternative method?

A: Can you read it again ---

Q: Yeah.

A: --- and let me, let me listen?

Q: Yes. All right. It says, if the allocation apportionment provisions -- I'm gonna skip some language to get to the, the gist of it, but let me know if you want the full ...

If the allocation apportionment provisions of -- do not fairly represent the extent of the taxpayer's business activity in the State, and I'm just gonna focus on the Department's part, the Department may require an alternative method. So, do you agree that the Department may require, indicates that that is optional? The Department -- it doesn't say, must require, the Department has the option to determine whether or not they are going to invoke an alternative method?

A: Yes. And -- but, but if the taxpayer's reporting method doesn't fairly reflect their activity, I'm sure we're not just gonna say, oh, well, go ahead and keep fli- -- filing the way you are and don't fairly report your receipts to South Carolina, don't fairly pay your taxes to South Carolina. There must be a -- something -- another type of adjustment that we made ---

Q: Okay.

A: --- to cure the, the fact that they aren't fairly reflecting their activity in South Carolina. I mean, you've got to do something if you don't do a unitary combination, or ---

Q: Okay.

A: --- an alternative apportionment to, to reflect their -- you might do an add-back or you -- there might be a separate accounting of their operation.

Q: Okay.

A: No -- well, that -- those are all alternative apportionments, but you got to do something else. You're not just gonna say, taxpayer, continue not to fairly report your income in South Carolina.

Q: Okay. So, so if it's not fairly reflected, then the Department's policy would be to invoke some type of apportion- -- alternative apportionment method?

A: Or some -- something else within our Code

Section that would, would allow us to reflect their, their business activity in South Carolina. We aren't just gonna say, taxpayer, continue to not fairly report your income in South Carolina for year after year, after year, after year.
Q: And then, when you get down to the step two in trying to figure out the methods, so would you agree with me that A(4) is the method that the Department chose in this audit?
A: Yes.
Q: And A(4) says the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.
A: Right.
Q: My understanding is that, you believe that equitable and the reasonable, from up top, where we say if the business activity isn't fairly represented then the Department can invoke another method if it's reasonable, and then this language of equitable, that you use those terms synonymously?
A: Yes.
Q: And so there's nothing -- no extra analysis in your mind or the Department's policy that would

be applied to determine whether the ---

A: That's the only thing we have to determine based on Rev- -- Revenue 15-5 and the *CarMax* case.

Q: Okay. So you're not, you're not imposing any separate or different tests for equitable, you do view those as synony- -- synonymous and you were looking at the same thing?

A: I think reasonable is, is, if not exactly the same thing, very similar to equitable.

Q: Okay. And in this case, would you agree that both parties are applying the standard apportionment method of the sales factor?

A: Well ---

Q: And both used the sales factor?

A: When you say both parties?

Q: Sorry. Would you agree that Tractor Supply and the Department -- so Tractor Supply did separate entity reporting ---

A: Uh-huh.

Q: The Department did combined unitary reporting ---

A: Right.

Q: --- but they both used the sales factor or the standard apportionment method that they

applied?
A: The apportionment method was the, the sales ratio, the -- right.
Q: Thank you.
MS. GEER: Your Honor, could I have one minute?
THE COURT: Sure.
(*Whispering*.)
Q: Mr. Sharpe, I appreciate it. Those are all the questions I have.
A: Thank you.
MR. LUTHER: Nothing further from the Department, Your Honor.
THE COURT: Okay. You may step down.
MR. SHARPE: Thank you.
THE COURT: Any more bullets?
MS. WOOTEN: I'm sorry?
MR. LUTHER: Any more bullets.
MS. WOOTEN: Oh, bullets. One more today.
THE COURT: Okay.
MS. WOOTEN: Your Honor, the Department calls Steven Riggs to the stand.
COURT REPORTER: If you'll raise your right hand for me.
MR. RIGGS: (Witness complies.)
COURT REPORTER: Do you swear to tell the truth, the

whole truth and nothing but the truth, so help you God?

MR. RIGGS: Yes, I do.

COURT REPORTER: Thank you.

MR. RIGGS - DIRECT EXAMINATION BY MS. WOOTEN:

Q: Mr. Riggs, could you please state your full name for the record?

A: Steven Dwayne Riggs.

Q: And where are you currently employed?

A: SCDOR, the Department of Revenue, South Carolina.

Q: How long have you been employed with the Department?

A: June of 2010, which is about 13 -- 12 and a half, 13 years.

Q: And you're here to testify on behalf of the Department today?

A: Yes.

Q: Okay. In what are of the Department do you currently work?

A: Audit support.

Q: Okay. And is that your title?

A: My title is Audit Selection Analyst.

Q: Okay. And could you describe to the Court what an Audit Selection Analyst does?

A: Part of my duties is to be, what they call, a power user for our -- the system that we use throughout the Department. I also help with audit selection for the Corporate Income Tax Section. Usually, issues in the system, I would help them with that, things of that nature.

Q: All right. So let's jump back to -- I believe you said 2010, when you first started working at the Department?

A: (No audible response.) (Nods head.)

Q: All right. So let's walk through your employment history and some of the duties with each job that you held at the Department. What was your first position at the Department?

A: My first was Revenue Officer from June 2010 to, roughly, about September of '12.

Q: Okay. And what did you do as a Revenue Officer for the Department?

A: We collected on assessments. You serve rules and revocations to businesses, help them do payment plans, you run, like -- you work the fair for people's retail licenses and things like that.

Q: I'm sorry, the failure?

A: Like, the fair. Like, the State Fair.
Q: The fair, okay.
A: You'd run out there and collect their money and help them get -- and their retail license, certain things like that.
Q: All right. After the Revenue Officer position, what position did you move to at the Department?
A: I went to Domestic Audit from September of '12 to January of '16.
Q: Okay. And what is Domestic Audit?
A: It's just like sales and use tax, anything that's local to where your office was located. So, I was based out of Charleston at the time, so I would work a lot of sales and use tax, liquor by the drink, manufacturing, ST-10s, things like that in just the local area of the office.
Q: And when you say, within the local area of your office, are you talking about the taxpayer's physical location?
A: Yes.
Q: Okay. And in those particular instances, do -- did -- were the taxpayers also operating in other states besides South Carolina?

A: No.
Q: So, the manufacturers were only operating in South Carolina?
A: Well, for new -- like the buildings themselves. So technically, what you would do with the manufacturing audit, from what I can remember, you would essentially go out and issue an ST-10 that they may've submitted and you would help them get the ball rolling in starting up that manufacturing location. So, while it could've been a company that was outside, you were only dealing with that specific location in the vicinity of, of the office who you work -- you got assigned from.
Q: All right. And just for the record, you said ST-10. What is an ST-10?
A: It's just a form of license that the manufacturer probably would submit to DOR. They would assign it to an auditor and then you would go and discuss, you know, what was needed to get the operations running, what were the operations in general, and then they could get exemptions for certain things throughout the whole building.
Q: All right. So after Domestic Audit, where did

you move next in the Department?
A: After Domestic I went to Foreign Audit.
Q: Okay. When did you move to Foreign Audit?
A: That was January of '16.
Q: Okay. And how long were you in Foreign Audit?
A: I was there, I think, about three and a half, so it went to the end of September of '19.
Q: Okay. And you left that position to go to your current position ---
A: Yes.
Q: --- correct?
A: Okay. All right. So let's jump back and talk about what, what is Foreign Audit?
A: Foreign Audit is just -- it usually consists of our C-corps -- corporate income tax audits, sometimes nexus -- we have a whole separate nexus section, but essentially, we deal with C-corp returns and then we would review those.
Q: Okay. And can you describe some of your responsibilities and duties as a Foreign Auditor in this section?
A: Essentially, reviewing C-corporation returns, assigning -- getting assigned audits, working the audits, contacting taxpayers and discussing issues.

Q: And during your time as a Foreign Auditor, approximately, how many audits did you work on?
A: I think it was roughly about 30.
Q: 30 audits?
A: About 30 to 35, I do believe.
Q: Okay. And can you just generally describe the types of taxpayers that were involved in the audits? Again, nothing specific, just the general industry that those taxpayers were involved in?
A: Usually, like, retailers, service providers, a little bit of manufacturers, but, you know, typically it would be a retailer or service provider, something along those lines.
Q: Okay. And in those 30 audit -- approximately, 30 to 35 audits, can you describe the types of issues that you generally encountered in those particular audits?
A: Typically, it can be anything from sourcing for apportionment -- I believe there were a few unitary combinations that we did. It could deal with license fee adjustments, or maybe credits that were taken. Typically, anything that would fall in with the State, South Carolina 1120.

Q: And so, going back to these 30 to 35 audits that you've done in your capacity as a Foreign Auditor, what was your role during those 30 audits?

A: It, it would depend. So at the beginning, I actually came to Columbia everyday for the first year. So, essentially, I was gonna be a supporting auditor essentially and I would go with other more experienced auditors, say, for a group audit. So I was either coming to the office here in Columbia from Charleston everyday, or I was actually on-site with another auditor reviewing returns.

Q: Okay. And just, again to jump back. Where were you physically located when you were a Foreign Auditor? Which offi- -- which Department office?

A: So, technically, I would've been in Columbia for the whole first year, and then after that I would've been relocated to Charleston ---

Q: Okay.

A: --- and then we would travel, obviously, so --

Q: Okay.

A: --- you know.

Q: I just wanted to clarify that. You had mentioned you were going back and forth between the Columbia --

A: Right.

Q: --- office and another office, but you didn't say which office that was.

A: Right. Right.

Q: All right. So, of these 30 audits you -- I believe your testimony was that there's, that there's lead auditors and then there -- you paired up with a more experienced auditor in some. Can you describe the -- within those 30 audits, when you were paired up with someone versus when you were the lead auditor?

A: Okay. So, essentially, if -- when you're pairing up with an auditor, especially at the beginning, you're essentially kind of learning on-the-job training. So you're, you're going through the returns with the -- what would be the lead auditor. So as a supporting auditor, you would be learning from them, learning about the returns, maybe, certain issues that are changing throughout all the different audits that you're going on with a lead auditor. And then as being the lead auditor itself, that's when you would kind of take more control of the flow of the audit, I would say. So you're contacting the taxpayer, typically, scheduling the appointments, when to come out at that point, on-site, maybe the information you're requesting from the taxpayer before you get to the location, you know, the discussions between the taxpayer and the DOR would be with the lead auditor directly until you got to the end and the audit was considered submitted and approved.

Q: In the 30 to 35 audits that we've been discussing, how many of those audits were you a supporting auditor?

A: I would guess, about half. So the whole, probably, the whole first year, at least. And then, there were also times even -- after even the first year and a half you may go on a group audit and not technically be the lead auditor. You would actually still go with audit- -- auditors and they would be working it and you would be there to be this extra set of eyes. You can hear the conversation that's going on and then discuss, still among both auditors -- well, sometimes three.

Q: Okay. So if you were a supporting auditor for half the time, about -- approximately 15, that would leave 15 audits in which you were the lead auditor, correct?

A: Roughly, yes.

Q: Okay. Other than working with more experienced auditors, did you receive any other kind of training at the Department when you became a Foreign Auditor?

A: So, typically, at the beginning it would be a lot of articles on, I call it continuing education, so other, maybe, newer instances of issues that the auditors were seeing, they would kind of pass those around new auditors, especially 'cause we needed to have exposure to that. There were, there were two training sessions, specifically. One was actually in August of '19, so that was right before I left. I think it was a month before I had left the, the group. And then the other one was actually -- I think, it was three and a half to four days, the fall or winter before, so that would've been, like in 2018, and that was the ITC. The summer one from '19 would've been the MTC, which is actually what -- the one we spoke about.

Q: Okay. You mentioned the ITC training, do you know what the ITC stands for?
A: I believe it's the Interstate Tax Commission, I think is how they pronounce it.
Q: All right. Are you -- and you are -- are you still a Foreign Auditor?
A: No.
Q: Okay. When did you leave?
A: I left -- it would've been October of '19.
Q: Okay. And why did you leave the foreign audit position?
A: A couple different factors. So, I wanted to get off the road, they were still traveling, you know, twice a month back then. I had a younger daughter so I was trying to be home for her every day. It was probably a -- it -- well, it was a new position in general, so it was -- nobody had even had it yet. It was really focused on the electronic side, the system side of things, so that was something I was already pretty good at from doing the audits, even dating back to the domestic when the system first was created for us. So, it kind of seemed like the right fit and the right move all at the same time so I, I just took it.

Q: Okay. And again, what position did you move to when you left Foreign Audit?

A: Audit Selection Analyst.

Q: And that is the position you're currently in?

A: Yes.

Q: Okay. All right. So, let's, let's turn more towards the taxpayer and the audit in this, in this case.

Are you familiar with the taxpayer?

A: Yes.

Q: Okay. And what's the nature of your involvement with the taxpayer?

A: I would've been the lead auditor.

Q: Okay. And what years did this audit cover?

A: That would've -- 12/31/2014 through 12/31/2016.

Q: Okay. And are you familiar with the term FY, or fiscal year?

A: Yes.

Q: Okay. And what does that mean?

A: Fiscal year is technically, I guess, the filing period for the, the corporation. So, it's not necessarily a calendar year. So, typically, taxpayers can go from March to March or June, September or December, so it's not necessarily a calendar year, it's just when their filing period begins and ends.

Q: Okay. And is that usual or unusual for a corporate ---

A: It's usual.

Q: --- tax year.

Q: Okay. Let me finish.

A: Sorry.

Q: All right. In South Carolina, what is the due date for a corporate income tax return?

A: Typically, it's the 15th day, three months after the original due date, normally.

Q: Okay. And does South Carolina permit taxpayers to file an extension -- corporate taxpayers to file an extension request?

A: Yes.

Q: Okay. And if an extension is granted for that corporate taxpayer, when would their return be due?

A: It would be six months after the three months of the due date. So, technically, about nine months later.

Q: Okay. So let's, let's look at this from one of the years in question in this case. Let's start with 2014.

For the 2014 tax return, when would it

have been due under the, the normal filing date?

A: It, it would've been March 15th of 2015, depending on when that day fell on. So, I'm assuming, if it was a Friday, it would've been due then.

Q: Okay. And if the taxpayer had gran- -- or requested and been granted an extension for that particular return -- again, the 2014 return, when would it have been due?

A: That would've been in September of '15.

Q: Okay. If you will flip to Joint Exhibit 9. I'm gonna hand it to you.

(Joint Exhibit Number 9 was introduced into the record at this time.)

Q: All right. If you'll flip to Exhibit 9, and could you identify that for us? Joint Exhibit 9. Could you identify that for the Court, please?

A: Yeah. It looks like a Tractor Supply, South Carolina state return, 2014 period.

Q: Okay. And do you know what date Tractor Supply filed that return?

A: I think it was September 2nd of 2015, I believe.

Q: Okay. All right. All right. So let's, let's talk -- step back just a second and talk about corporate income tax, generally.

In your role and experience as an auditor, what is the first step in determining whether a taxpayer is subject to tax in South Carolina, income tax?

A: Typically, you'd see if they had any operations within South Carolina. I think it's 12-6-530 requires any corporation that does business in the State has to file a tax return.

Q: And did you determine Tractor Supply Company was doing business in South Carolina?

A: Yes.

Q: Okay. And how did you determine they were doing business?

A: So, initially, we would've seen that they filed state rev- -- state returns. We would've done a -- did a Google search of, were there stores in South Carolina. The SEC website shows their 10-K, it kind of explains their background and what they do, in general. So we knew that they were already filing state returns on top of that, so.

Q: And where did you find this information that you just described?

A: So the state returns would've been filed in our system, so we have access to that for the returns themselves for South Carolina. A Google search helps you just generally see that -- the company itself. And then, the SEC website obviously has the 10-K information.

Q: Okay. And the Google information and the 10-K that you were just talking about, is that public information?

A: Yes.

Q: Okay. So once you determined that Tractor Supply Company is doing business in South Carolina, what did you do to determine what their principle business is?

A: So, essentially, you know it's retail sales obviously because they have stores. You're reading through the 10-K to understand how they're operating, in terms of what is the company, what do they do. So just based off of that up front, we knew they were doing store sales, which would've been retail sales in general. So that's what we -- we knew they were operating as in South Carolina.

Q: And why is it necessary for the Department to ter- -- to determine what a taxpayer's principle activity -- business activity is in South Carolina?

A: You need to know how, how they're operating in the State so that you know how to apportion their income.

Q: And why is that important to know -- or -- with reference to how to apportion their income?

A: So you need to know how to apportion their income based on the business activity in the State. Being a retailer, they would've followed the sales, the sales factor. I -- offhand, I think it's 12-6-2280, I believe it's at, that talks about retailers and manufacturers must use the sales factor for South Carolina sales over everywhere sales. So, knowing that they were a retailer, looking at the returns you could see that that was the factor they were using in terms of apportionment.

Q: And so you say it's, it's necessary for certain types of businesses, so retailers, manufacturers use sales factor. What is the other type of industry that would use a different ratio other than sales factor?

A: It could be -- well, it's anything other than that for the most part. So service provider, for example, they would use gross receipts ---
Q: Okay.
A: --- and not retail sales.
Q: But the Department did not use gross receipts in this case?
A: No.
Q: All right. All right. So dialing back to apportioning income to South Carolina. How does a taxpayer apportion its income to South Carolina?
A: So, I guess, in general, for -- similar to this case, for a retail sale, they would go South Carolina sales as a numerator, and that would be over the denominator, which would be their everywhere sales. So on a single-entity basis it would just be the sales that they had for the -- that single corporation.
Q: All right. And so, that is for the sales factor. How about their taxable income in South Carolina -- again, generally, how -- what is the process of determining the South Carolina taxable income?
A: It's -- basically, would be the federal taxable

info from the federal return, which is typically on 30, that becomes line one on our state return. Then you would have your South Carolina modifications, it's gonna be Schedule A, Schedule B, you would run through that, and then you would have the apportionment amount based on the sales and you would apply to the number. And then, if they had South Carolina NOL, you'd subtract that.

COURT REPORTER: Say that one more time, I'm sorry.

A: The South Carolina ---

COURT REPORTER: Slow down.

A: --- NOL, Net Operating Loss, you could apply that and then you would come to the South Carolina ...

Q: Okay. In your experience with the Department, what are the two basic methods states use to determine the amount of income that's apportioned to that particular state?

A: It would be single entity and unitary.

Q: Okay. So you said single entity, is there another name for that reporting method?

A: I guess, the statutory ...

Q: Separate entity?

A: Separate entity.

Q: Okay.
A: Yeah.
Q: So, let's look at separate entity reporting. What is separate entity reporting?
A: So, separate entity reporting would be one individual taxpayer filing on a single return, one-to-one on their own.
Q: And in comparison to combined unitary reporting?
A: So combined unitary reporting would be typically everybody in a unitary group all combined into one return, including FTI, apportionment, minus the eliminations, so it would be all of them combined into one -- on one return.
Q: Okay. All right. So, let's, let's turn to the actual audit in this case. Were you -- what was your role in this case, were you a supporting auditor or a lead auditor?
A: I would've been a lead auditor.
Q: Okay. Were you the only auditor involved in this claim?
A: No.
Q: Okay. Who else was involved?
A: Rob King.

Q: Okay. And who is Rob King?
A: Now, he is the Foreign Audit Manager.
Q: Okay. What was Mr. King's title and position at the time of this audit?
A: He would've been a -- an auditor, Foreign Auditor.
Q: Okay. And as the supporting auditor, what was Mr. King's responsibilities?
A: In this particular audit?
Q: Yes.
A: He, he contacted the taxpayer. He scheduled the appointment. And he also sent the appointment letter, which was also essentially the first IDR information request to the taxpayer.
Q: All right. And for the record, what is IDR?
A: It's just an information request that we would send, it's just the acronym for it. So it's ---
Q: Okay. So I, Information; D?
A: I don't know what the acronym ---
Q: Document?
A: --- actually stands for? Yeah, Document Request.
Q: And R, Request?

A: Right.
Q: Okay. All right. So, again, we're just gonna talk about this generally for now. But if you will look at Joint Exhibits 12, 13, 14, and 15. And if you could start with Joint Exhibit 12, and we'll wait until you get there.

(Joint Exhibit Number 12 was introduced into the record at this time.)

A: Yep.
Q: Okay. Can you identify this exhibit for the Court?
A: This would be the Appointment Letter/initial IDR.
Q: Okay. And what is the purpose of this document?
A: Typically, it's to send to the taxpayer after they have agreed to the time to meet. It also requests -- or it shows the items that we are requesting to review on the site once we show.
Q: And so the taxpayer know -- or is -- knows to have these documents available prior to you arriving on audit?
A: Yes.
Q: Okay. All right. If you'll flip to Exhibit 13, and could you describe for the Court what

Exhi- -- Joint Exhibit 13 is?

A: So, 13 looks like it's the work papers for all three periods in the audit. So it would be '14, '15 and it looks like '16 as well.

(Joint Exhibit Number 13 was introduced into the record at this time.)

Q: And what are corporate working papers?

A: It -- typically, it shows the -- any of the adjustments that you would've made for each particular audit period. So our audits run working papers per year, so that doesn't come out as one working paper for all three, you have to have individual working papers, so. It would show the adjustments broken down for each period.

Q: Okay. All right. And we'll go to Exhibit 14 -- Joint Exhibit 14. And could you identify and describe, just generally, again -- we're gonna get into this in more detail, but just generally, what this document is?

A: This is the Explanation of Assessments Letter that is usually sent out with the audit packet once the audit itself has been submitted and approved. And it brief- -- briefly explains the adjustments and the reasonings behind it, to the audit.

(Joint Exhibit Number 14 was introduced into the record at this time.)

Q: Okay. And if you'll look at Exhibit 15. And if you could identify and describe that document for the Court?

A: 15 is the Proposed Assessment Letter that goes along with the audit packet and it, kind of, essentially is the breakdown -- not the breakdown, but the overall amount of the adjustment for all three periods total. Also, behind it is the Waiver of Restrictions Form that usually comes with the packet and the instructions for that are on the last page.

(Joint Exhibit Number 15 was introduced into the record at this time.)

Q: Okay. And do these exhibits, specifically, 13, 14 and 15, contain your audit report and work papers for this particular taxpayer?

(Joint Exhibit Numbers 13 and 14 were referenced at this time.)

A: Yes.

Q: Okay. And did you provide all of this information to the taxpayer?

A: Yes.

Q: Okay. All right. Again, generally, what are the findings of your report? And we're gonna go through this in detail, but just to set the picture, what are your findings?

A: The findings were, we decided that there was distortion in their income based on the business activity in South Carolina and due to that, we were recommending a unitary combined adjustment.

Q: Okay. And just for the record, what was the apportionment method that you recommended, specifically?

A: Unitary combined.

Q: Combined, okay. All right. Based on your audit examination and findings, who did you determine is the unitary group?

A: It would've been the three affiliates on the federal consolidated return, which would've been Tractor Supply Company, Tractor Supply Company of Texas, and the Tractor Supply Company of Michigan.

Q: All right. Going back to -- so, let's start going into your proposed assessment and audit work papers in detail.

Let's start with the first. Who is the

taxpayer in this case?

A: Tractor Supply Company.

Q: Okay. And why does the Department consider them to be the taxpayer?

A: They were already filing the returns and based on the same code as earlier, they were required to file in South Carolina based on business activity.

Q: Okay. Where did you conduct the audit examination in this case?

A: It was on-site in Brentwood, Tennessee.

Q: And that is Tractor Supply's Headquarters?

A: Yeah.

Q: All right. Prior to going to the on-site audit in Tennessee, did you do anything to prepare for the audit?

A: I reviewed the South Carolina state corporate returns.

Q: For what years?

A: For -- I believe, it was the three years.

Q: The three years at audit in this ---

A: In the audit, the audit period.

Q: Okay. All right. If you'll just briefly turn to Joint Exhibits 9 through 11. And could you verify that those returns are the returns that you looked at, the South Carolina returns for the years at issue?

(Joint Exhibit Number 9 was referenced at this time.)

(Joint Exhibit Numbers 10 and 11 were introduced into the record at this time.)

A: It appears to be so, yeah.

Q: Okay. So after reviewing those returns, what did you find or conclude?

THE COURT: All right. I think now might be a good time to take a break.

MS. WOOTEN: Okay.

THE COURT: Let's take a short ---

MS. WOOTEN: Sure.

THE COURT: --- five-minute, ten-minute break. Which one y'all want?

MS. WOOTEN: Ten-minute is fine, if that -- or ---

THE COURT: Okay.

MS. WOOTEN: That's -- all right. Thank you.

(Off the record from 3:33 p.m until 3:45 p.m.)

THE COURT: Proceed.

MS. WOOTEN: Proceed?

THE COURT: Uh-huh.

MS. WOOTEN: Thank you, Your Honor.

Q: So, before the break we were talking about Exhibits 9 through 11, and you identified those

as the South Carolina returns of Tractor Supply Company filed for the audit period, correct?
A: Yes.
Q: Okay. All right. So you -- and, I believe your testimony was that you reviewed those prior to the on-site audit?
A: Yes.
Q: That's correct? Okay. Did you review anything else prior to the audit -- on-site audit in Tennessee?
A: I believe I read the -- probably, the business section of the 10-K, which is kind of a little bit of an idea of the, the company in general, the business side.
Q: All right. So, we go to -- now you're going to the on-site, and while you were there did you review any documents?
A: Yes.
Q: Okay. Can you tell me the documents that you reviewed during the audit examination that, that week in Tennessee?
A: So, I looked at the state returns again, the federal consolidated returns, the apportionment information that was submitted, there were memos. I think, there were brief summaries of

their 482 Study. I think we got the licensing agreements up front, Revenue Ruling 15-5, let's see ... We received the 482 after that, still on-site, just later on in the week. (Whispering) What else was there?

There was inventory agreement. We did look at older audits -- Excels from the prior to audit. I had my own version of the Excel that I looked at. I think we probably looked through the 10-K deeper. On-site there was, there was an IDR-2 that I sent, that's when we got the 482, was from the IDR-2, which also included explanations of some of the other agreements, so the shared service agreement, the administrative chair agreement, those were explained in that IDR, what their responses from Matt Appelman.

Q: When you say they were explained in that, who explained what?

A: I believe Matt Appelman sent the response to the IDR-2, and that's when he included the memos for a second time. The 482 was on -- attached to that. I believe the inventory agreement might've been on IDR-2. And then, within it were responses to the questions of maybe what the agreement was. Actually, probably two of the agreements were responded to that way.

Q: All right. And just to clarify for the record, who is Matt Appelman?

A: He was actually somebody that was helping us while we were on-site, outside of Marjorie.

Q: Okay. Who was he employed by?

A: Tractor Supply Company.

Q: Okay. All right. And going back to the federal consolidated returns, you also -- you mentioned that you reviewed those returns. Did you review any accompanying documents to those returns?

A: Say that one more time?

Q: Did you review any, like, attachments to the actual consolidated return?

A: It came with, with the white pages. The back of ---

Q: What are the white pages?

A: It's just the back of the documentation that usually coincides with the lines on the federal return. So, when you get to the back it'll, it'll essentially break down the combined column, what eliminations there were, and then all three in this case, that were included in the federal return, plus the breakdown of the line items that go into that, as well. So, it's essentially a larger backup of the federal consolidated return.

Q: Okay. All right. And after you reviewed these documents, what did you do next?

A: Once we reviewed that, especially the white papers, and you could see that there were intercompany, obviously with eliminations, we were looking through the memos, all the information that we had received up-front, just reviewing through that. We started to see similarities, I guess, in what Rob had done when he audited them, the -- well, not the first time, I guess, but prior.

Q: Okay. And just for the record, who, who was Rob?

A: Rob King.

Q: Okay. And he was the auditor with you on-site?

A: Yes.

Q: Okay. And when you say prior audit, describe what you mean by that?

A: So, he did a prior audit from 2008 through 2010 -- 2008 through 2010 of the taxpayer.

Q: Okay. And what was the result of Mr. King's audit?

A: His was a unitary combined adjustment.

Q: Okay. So, after you began seeing those circumstances or facts that you believe were similar, what did you do next?

A: Once we started to see that, I think that was when he pulled his Excel that he had worked on initially, and it had a lot of the descriptions of the companies that were still there. We were starting to, I guess, discover that it was essentially -- they were pretty much operating the same way, so at that point we wanted to look at 15-5 since we were assuming they were going to be unitary, and we wanted to make sure that we were on the right track with how we were going to apply if that was the way we were gonna run.

Q: After reviewing the prior audit report of Mr. King, did you review any additional returns by the taxpayer?

A: We did.

Q: Okay. And what were those returns?

A: We looked at both 2012 and 2013 South Carolina returns.

Q: Okay. And why did you look at those returns?

A: So, I believe when he did his adjustment, I think they settled with the state. So, we wanted to see, did they continue to file as unitary based on a settlement or did they keep filing separate, and how they were filing after that initial, I guess, settlement.

Q: Okay. And for tax year 2012, what did you find?

A: They filed a unitary combined return in South Carolina for 2012.

Q: Okay. Did you make any -- were there any adjustments made to that return by the Department?

A: Not that I know of.

Q: Okay. When you reviewed the 2013 return by that taxpayer in South Carolina, what did you find?

A: They had reverted back to filing separate entity with Tractor Supply Company.

Q: Okay. What adjustments, if any, did the Department make to the taxpayer's 2013 returns?

A: We, we didn't make any.

Q: Okay. And why didn't the Department make any adjustments to that 2013 return?

A: That -- at that point it would've been out of statute, so we wouldn't've been able to go back.

Q: Okay. All right. So we've talked about the documents, what you began to see. At -- what happened at that point during the audit, once you've reviewed the initial set of documents, you began seeing circumstances from Rob's prior audit, you reviewed additional documentation, what happened next?

A: So, at that point, I think we -- initially, we decided that we were gonna do a unitary adjustment based on the transactions, similar circumstances. We also -- I forgot to mention, we did received a Word document that had a brief, like, explanation of each entity within the group. That actually also helped apply and it showed that they had common ownership among certain entities, which a lot of them were, if I remember, the company dis- -- disregarded into TSC, which kind of coincided with the federal consolidated return since there was only the three entities on that. So, because of that and all those circumstances, and we were doing unitary, we wanted to run 15-5 and follow it the way that South Carolina interpreted it.

So, at that point, I'm sure I sent it to the taxpayer stating, hey, this is what we're looking at. And I think, at that point, while we were applying it and working through the Revenue Ruling, we were trying to set up, like, an exit interview -- or exit meeting, or whatnot.

Q: And what's the purpose of the exit meeting?

A: Just to discuss any -- maybe, adjustments you already had planned that -- based on what you saw, kind of, to discuss which direction you thought you might be working in. Typically, we -- when we're doing something like that with an adjustment, you would like to give them some sort of documentation or, you know, some sort of idea of what you were going to do instead of, maybe, just dropping it on them later on.

Q: I'm gonna hand you what's been marked as Department's Exhib- -- or Respondent's Exhibit 22.

Do you recognize this document?

(Respondent's Exhibit Number 22 was introduced into the record at this time.)

A: Yes.
Q: What is it?
A: This is the Word document I was just talking about that we received once we got to the location for the review, and it just has the explanations of the entities that were included, including the disregarded.
Q: Okay. And did you use the information in this document as part of your audit examination?
A: Yes.
Q: And did you rely on the information in this document?
A: Yes.
Q: Okay.
MS. WOOTEN: Your Honor, at this time, the Department would offer Respondent's Exhibit 22 into evidence.
MS. GEER: No objection.
THE COURT: It's admitted.
(Respondent's Exhibit Number 22 was admitted into evidence.)
MS. WOOTEN: Okay. Thank you.
Q: All right. We'll come back to that, to that document in just a minute.
All right. You also testified earlier

that you reviewed the taxpayer's federal consolidated returns. Does South Carolina have a consolidated return?

A: Yes.

Q: Okay. Is that the same as a federal consolidated return?

A: No.

Q: Okay. And how are they different?

A: So a federal consolidated return typically is every entity within their corporation which includes and shows their eliminations. And then on the front page it's a -- like the white papers to a Federal 1120, it would have the combined information all through the, the first page that works and breaks itself down, so that's for federal. And then, South Carolina essentially, what we use our consolidated return for is essentially administrative ease. So, each taxpayer is still filing their own particular return, but it's still consolidated into one return so they can file one return with all of them included, but they are still separate. They still have their own enforcement rates, their own FDI and everything working through.

Q: All right. So, let's go back and talk about this document, the -- Respondent's Exhibit 22, the description of the entities provided by the taxpayer during the audit.
Why did you use this information as part of your audit write-up and papers?
A: Well, we felt this helped show that there were a lot of disregarded entities for tax purpose and to TSC, which kind of coincided with the federal return itself, only showing TSC, TSC Texas and Michigan. It also kind of shows and breaks down, like, the percentage of ownership in between the three. And it also kind of shows that they're working as a unitary aspect with common ownership.
Q: And why is common ownership important to your audit findings, findings?
A: Well, for us, to have common ownership, is showing that they're dependent upon each other and certain functions of, maybe, how they're operating, so in a group. So, the fact that there's common ownership, you're showing that it's essentially one group of entities working together to make retail sales. So this kind of helped reinstate that and back that up, showing

that there was common ownership among the entities.

Q: Okay. And just for the record -- I'm not sure who said this so, just for the record, for my purposes. For purposes of this audit, which Tractor Supply entities filed tax returns in South Carolina?

A: Just Tractor Supply Company.

Q: Okay. Did Tractor Supply Texas file a tax return in South Carolina?

A: No.

Q: Okay. Did Tractor Supply Michigan file a tax return in South Carolina?

A: No.

Q: Okay. All right. Earlier you were talking about some of the documents you reviewed, and you stated that you reviewed 482, I believe you said, memos, is that correct?

A: Yes.

Q: Okay. If you'll flip to Joint Exhibit 21. There should be three pages of Joint Exhibit 21, is that correct?

(Joint Exhibit Number 21 was introduced into the record at this time.)

A: Yes.

Q: Okay. Did you review all three of those pages as part of your audit?

A: Yes.

Q: Okay. If you'll identify those for the Court, please?

A: They're the Memos that we received, initially. Also I believe with the IDR-2, I think we got them a second time. Essentially, they're the same document just with the updated years on them. I think the numbers are all the same.

Q: Okay. And what do these Memos mescribe?

A: Essentially, what it talks about is -- it's like a summary of the 482, so it kind of breaks down the rate that they would be using as a markup in terms of a range and what they might decide. Also the same thing for profitability I think is in here. Let me make sure it's the same one.

So, essentially, in the first paragraph it talks about for the licensing fee of what the 482 would summarize -- or what this summarizes of the 482 and what the profitability range would be depending on what they chose. And then, by the end, it shows that all three discussed -- well, Texas waiving the fee for

the license trademarks.
Q: Is a 482 memo different than a 482 study?
A: Yes.
Q: Okay. Were you provided with the 482 Study?
A: Yes.
Q: Okay. How were those different?
A: This, this is essentially a summary, whereas the 482 Study would be the whole review.
Q: Okay. All right. And finally, you mentioned the intercompany agreements as something that you reviewed. Which intercompany agreements did you specifically review as part of your audit?
A: So, I believe we received the licensing agreements and inventory procurement agreements, and then just the responses about the shared service agreement and the administrative agreement.
Q: All right. And to clarify, when you say you just received the responses, did you ever receive the actual master shared services agreement or the administrative agreement as part of the audit?
A: No.
Q: Okay. What did you receive with regard to

those particular intercompany transactions?

A: So we, we received a description of what was included in the agreements, essentially, and the e-mail as a response to IDR-2.

Q: Okay. If you'll flip to Joint Exhibit 16. And can you identify and describe Joint Exhibit 16 to the, the Court?

A: That's the response to IDR-2 from the taxpayer.

(Joint Exhibit Number 16 was introduced into the record at this time.)

Q: Okay. So you received this response from the taxpayer, but you did not receive the actual agreement?

A: Correct.

Q: All right. And what does this document describe?

A: Essentially, it tells you what's comprising of those two agreements at the top, so number one and two. Number one would be the breakdown, I guess, of the Master Shared Services, which is gonna be the leasing of the employees to Michigan. And then, second is, actually, the administrative services agreement between the shared overhead costs between all three, and I think that's based on how TSC is covering the overhead upfront for the other two, and then they would pay them back based on the annual amount from the year before.

Q: Okay. So, now, going back to the taxpayer's retail operations in South Carolina, how many Tractor Supply stores were in South Carolina during the audit period?

A: I believe 42.

Q: Okay. So based on your understanding of the documents that you reviewed and their operations in the State including their federal and state tax returns, what did you determine with regard to their filed South Carolina returns for the audit period?

A: We found that -- we thought the way that they were filed didn't reasonably show the sales within South Carolina. We thought it was being distorted based on intercompany transactions. So based on that, we were going to do a unitary combined adjustment.

Q: Okay. And how in -- and based on your documents in your review, what is your understanding of how the taxpayer shifts income from the retail operations in South Carolina to the entities that do not file in South

Carolina?

A: So the main one would be the procurement function. So what -- essentially what happens is, they have agreements in place to where Texas owns the trademarks and allows those to be used among TSC and Michigan, in response to that, without charging a fee for that, they will be the sole supplier of product to sell to the other two. So, essentially, instead of getting -- instead of paying a fee for the trademark they are going to buy everything from them for the procurement function to sell in stores for retail sales.

Q: All right. And what other intercompany transactions did we talk -- did you look at?

A: Another one would've been the, the leasing of the employees to Michigan, the fact that Michigan was relying on TSC to supply employees for them, TSC was getting back income for that plus a markup for the leasing of the employees to Michigan. Then, you had the shared -- so the master shared service agreement, which was the same thing, and the administrative service agreement, that was actually the overhead costs, which was among all three, whereas TSC

I believe was covering it, essentially. And then once that was due, then they would actually pay them back based on what the annual was the year before.

Q: All right. You testified earlier that you reviewed the transfer pricing study in this case, correct?

A: Uh-huh. Yes.

Q: All right. Let's get this one out of the way. You are not a transfer pricing expert, correct?

A: Correct.

Q: Okay. Why do you -- or why did you review the 482 Study for this particular taxpayer and audit period, understanding that you are not an expert in 482 Studies?

A: We usually looked at the 482 Study to understand what the transactions were, maybe, how they, how they worked, the operations of them in between. So it gave us an idea of what the transactions were and how they were occurring within the group themselves.

Q: All right.

MS. WOOTEN: I'm sorry, Your Honor. If you'll bear with me just a moment.

Q: All right. So then, I'm gonna go back and ask you some very specific questions about those intercompany transactions. You reviewed the documents, you have a general idea of what's going on, so let's break those down one by one.

Let's talk about the leasing of employees. You stated that that's Michigan, leases employees from TSC the parent company, correct?

A: Yes.

Q: Okay. And there is a markup -- small markup paid to TSC, correct?

A: Correct.

Q: Okay. Why is that relevant in your audit determination, understanding that TSC is the parent company and the taxpayer in this case?

A: I, I think it showed that they were still connected, they were still dependent upon those employees from TSC while also TSC was dependent on receiving that income plus the markup from Michigan. The fact that they were dependent on each other to, one, have the income, plus have employees to operate to get retail sales, I thought that kind of showed that they were together in unitary -- as part of the group.

Q: Okay. All right. So let's go to the next one. The next one is the administrative services agreement. I don't want to testify -- or speak for you. I think you testified for it. But just, generally, describe that -- just -- transaction again?

A: So the administrative services group, essentially, showed that TSC is supplying, I believe it's like payroll, the accounting, marketing, other services like that, to the other two entities and covering that cost up-front so that they wouldn't have to deal with it, wouldn't have to worry about it. And then in return, those two would pay TSC back, so therefore depending on them to supply that for them and to just pay them back for it. And I think that was based on what the amount was for the year before.

Q: All right. So similar to the leasing of employees that we just talked about, why is the administrative services transaction important to your audit examination in your report?

A: I, I think it's -- showed the same thing, that they were still depending on TSC to supply that for them. They wouldn't -- if they had to do it on their own it would've been completely different, because then they wouldn't've had, they wouldn't've had the fee that was going to TSC, but TSC wouldn't be dealing with them directly. So, I mean, by doing it this way it's showing that they're unitary in the group, as in, the other two entities that are helping out with procurement and the income that they're receiving, now they're applying that with them and they're just generally working together to make sure that they can continue to grow and have retail sales in general.

Q: All right. Now let's turn to a procurement transaction.

We've described that, I think, for the Court, but just generally, tell us your understanding about it so that I can ask the same question. What's your understanding of the procurement intercompany transaction?

A: My understanding is that Texas owns the trademarks and the procurement functions, so instead of charging the fee for the trademark, they're essentially going to charge for the procurement of the sales to the other two entities plus the markup on that. So, essentially, by letting them use the trademarks and not charging for that, they're making sure that they -- all the sales purchases from TSC to Michigan are coming from Texas directly and that they're all still self-contained.

Q: Okay. And again, similarly, why is that important to your audit report and conclusions?

A: I, I believe that's showing that the sales from TSC -- purchases, I'm sorry, they're, they're sending the income from TSC for the purchases to Texas, which would be sales outside of South Carolina to the other Company, but also keeping that in-house inside their self-contained group. So, essentially, Texas is getting all those sales for intercompany and South Carolina's not seeing that income. So, essentially, that's built into itself, contained.

Q: All right. So based on these intercompany transactions and the information that you learned during the audit from TSC, what proposed adjustments did you make to the taxpayer's Return?

A: We -- the adjustment we ended up doing the unitary combined.

Q: Okay. And again, what kind of analysis did you conduct to reach that conclusion?

A: So we based it on, what was the business activity in South Carolina. We knew with the intercompany transactions that they were going to be in a unitary group, so at that point we had to determine what we thought was the most fair or, you know, what do we think fairly represented what they did in South Carolina, and if they were unitary we were gonna by run by 15-5, how are we going to apply that to make sure that it was inline with the unitary group being a retailer, how is 15-5 going to guide us to accomplish that adjustment, essentially.

Q: Okay. And as part of your analysis, did you determine or understand whether or not Tractor Supply Company had any third party transactions outside of the group, other than the retail stores and the sales to the retail customers at the retail stores, so not looking at that third party transaction, did Tractor Supply Company engage in any other transactions with third parties outside of vendors and customers at the retail stores?

A: No.

Q: Okay. What did you conclude in your audit report regarding the taxpayer's South Carolina taxable income with regard to the statutory filing method?

A: Say, say it one more time?

Q: Sure. What did you conclude in your audit report?

MS. WOOTEN: (To Ms. Gamble) and if you'll pull up 14? I think Joint Exhibit 14.

Q: What did you conclude in your audit report regarding how the taxpayer filed their Returns and the taxable income stated using the Statutory filing method?

A: Well, we thought that the standard method wasn't fairly showing the unitary group's income or apportionment properly, so based on that, we were following 15-5.

Q: Okay. And is all the analysis that we just talked about, is that contained in your audit report under Joint Exhibit 14?

(Joint Exhibit Number 14 was referenced at this time.)

A: It -- yes.

Q: Okay. All right. And let's just run through some facts or some, some -- yeah, some facts for Tractor Supply Company based on your audit examination.

All right. Based on your audit, did you find that Tractor Supply of Texas provides any procurement services to an unrelated entity?
A: No.
Q: Okay. And based on your audit, do any of the Tractor Supply distribution entities provide those services to an unrelated entity?
A: No.
Q: Okay. And based on your audit, did Tractor Supply Company the parent, provide management services to any unrelated entity?
A: No.
Q: Okay. And based on your audit, what is Tractor Supply Company's primary source or stream of income on its federal consolidated return?
A: Retail sales.
Q: Okay. All right. You testified earlier that you, in your audit examination, found that the taxpayer operates within a unitary group, is that correct?
A: Yes.
Q: Okay. And what entities did you include in the group?
A: The three from the federal consolidated return, so TSC, TSC Texas and TSC Michigan.

Q: Okay. And what guidance did you rely on to determine whether or not a taxpayer operates -- this particular taxpayer operated within a unitary business?

A: 15-5.

Q: Okay. And how did you reach the conclusion that the taxpayer operates within a unitary business?

A: Ba- -- based on intercompany transactions that we reviewed and, you know, falling in line -- following 15-5 it, it helped kind of explain it for us.

Q: And why is it important to your audit examination and report whether the taxpayer operates within a unitary business?

A: I think it's important to know that they're running in a unitary business, because then we know what their actual activity is, what -- what's their, their business activity to come to their income. So as a unitary business and dealing with retail sales, that's their final game plan, essentially, would be to have retail sales. So running in a unitary group, we would know that the apportionment would still probably use sales factor, but also have to follow 15-5 to make sure that the calculations were proper, intercompany was eliminated, things like that.

Q: Before you started the audit, did you decide the result of it and what the examination would be?

A: No.

Q: Okay. At what point during the audit did you determine -- or did you consider combined unitary reporting as an alternative apportionment method?

A: I think it was probably when we got the memos, which were -- they were summarizing the 482. We began looking through the licensing agreements, we were seeing similar instances through the prior audit. Looking through the white pages, you could see shared, shared service eliminations between companies. So the line items were there, you know, just the general idea of how they were operating, plus Rob King knowing the history of what he knew when he did the initial audit, we were seeing similarities. So just based on what we had received, the intercompany that we'd already been looking at, so.

Q: All right. You mentioned Mr. King's audit. I'm gonna hand you what's been marked as Respondent's Exhibit 18. Are you familiar with this document?

(Respondent's Exhibit Number 18 was introduced into the record at this time.)

A: It looked -- well, it looks like different documents, to be honest with you. This first page has a period of '08 through '10, third page of it shows '14 through '16. So I don't know if it's the same complete document.

Q: Do you recall being asked about this document in your deposition?

A: Yes.

Q: Okay. And Ms. Geer asked you several questions about it?

A: Yes.

Q: Okay. And it relates to Mr. King's prior audit, correct?

A: Yes.

Q: And you reviewed his prior audit once you were on-site at Tractor Supply Company, correct?

A: His work papers, or his Excel, I should say, his Excel file. 'Cause ---

Q: Okay.

A: --- they, they were done different back then, so we didn't have the newer way, so.

Q: Okay. And again, what was the purpose of looking at Mr. King's prior audit work papers?

A: So he had brief explanations of the entities that were in his group at the time. So when he saw the instances, he went back and he said, let's look through what my initial one had on it, because it had explanations in here -- which they should be here if this is the document, for specific entities, and it was a way of us kind of comparing and seeing if they were still doing the same thing with those entities, or if there were new entities, or how they were operating now as opposed to then, was it going to be different, was it going to be similar. So we had to know, since he recognized certain instances anyway, we wanted to compare and see, are they doing the same exact thing or is it different.

Q: And the result of Mr. King's audit was combined unitary reporting, correct?

A: Yes.

Q: Okay.

MS. GEER: And I'm sorry, I, I missed that question.

Just if you ---

MS. WOOTEN: The conclusi- -- I think I might have to read it, but the conclusion of Mr. King's audit was for combined unitary reporting.

THE COURT: Close.

MS. WOOTEN: Close? Is that close?

THE COURT: The results of it.

MS. WOOTEN: I was wing- -- I was winging that one.

(*Laughter*.)

THE COURT: It started with the result.

MS. WOOTEN: Okay. The result of Mr. King's audit was, was combined unitary reporting.

THE COURT: That's it. Ding, ding, ding.

(*Laughter*.)

MS. WOOTEN: I told you I was winging it. All right. At this time, Your Honor, the Department would offer Respondent's Exhibit 18.

(Respondent's Exhibit Number 18 was offered into evidence at this time.)

MS. GEER: No objection, Your Honor.

THE COURT: Okay. It's ---

MS. WOOTEN: Thank you.

THE COURT: --- admitted.

(Respondent's Exhibit Number 18 was admitted into evidence.)

Q: And just for the record, let's talk about this for a second.
Did you reach the same conclusion as Mr. King in his prior audit under Respondent's Exhibit 22?

(Respondent's Exhibit Number 22 was referenced at this time.)

A: They weren't exactly the same. So I think his prior audit didn't include Michigan, if I remember correctly. His prior audit was done before 15-5 so, you know, it was going to be different, if I knew that or not. You know, when we were looking at it, it was going to be different anyway. But I mean, essentially, we both ended up in a unitary combined adjustment, so I could say yes and no, I guess.
Q: Okay. And just to clarify, the result of Mr. King's audit and the result of your audit was combined unitary reporting?
A: Correct.
Q: The difference was Mr. King did not include the Michigan entity in the unitary group, you included Michigan in the unitary group in this audit?
A: Right.

Q: Okay. Just making sure. All right. So as a result of your audit examination, you testified that you were impose -- the Department imposed combined unitary reporting. What authority did you rely on to oppose -- impose an alternative method in this case?
A: It -- I guess, it would've been best -- based on 2320(A)(4) once we decided unitary and we thought the apportionment wasn't being fairly applied. So then, we went to 15-5 and began to follow that Revenue Rule.
Q: Okay. Did you rely -- or did the Department -- did you, in your audit, rely in -- rely on any case law?
A: I think *Media General* kind of ties in with 15-5, so essentially, due to fif- -- due to *Media General*, 15-5 was released and that's why we ...
Q: In your experience as an auditor, does the Department impose combined unitary reporting on every unitary business?
A: No.
Q: Okay. And why not?
A: I think all the facts are, are different per each taxpayer. So, you can't always just apply

it to a unitary group based on certain instances, so each audit's going to be different, each review's different, so you can't automatically just apply it to a unitary group even though they might be doing different things.

Q: Revenue Ruling 15-5, Joint Exhibit 17 for the, for the record, discusses business structures or strategies that may create stu- -- state tax benefits. Are you aware of 15-5 and the discussion of that topic?

(Joint Exhibit Number 17 was introduced into the record at this time.)

A: What was that again?

Q: The business structures or strategies discussed in 15-5 that may create state tax benefits?

A: Is that the six factors?

MS. WOOTEN: (To Ms. Gamble) if you'll pull up 7. (Whispering.)

Q: Okay.

OBJECTION:

MS. GEER: I'm gonna object to leading here.

THE COURT: All right.

Q: All right. Mr. King [sic], in looking at 15-5 and your consideration of it, does 15-5 discuss any business structures or strategies that may create state tax benefits?

A: So, I guess, persons in companies, management companies I believe -- well, it says east and west, those were the instances I'm sure they were running into at the time of 15-5.

Q: Okay. So in your particular audit, did you find any of those features or structures with Tractor Supply Company?

A: I -- yeah. We -- I mean, the management company considered TSC, procurement companies which would be Texas, but those are instances listed on 15-5.

Q: Okay. And in your experience as an auditor, what is the significance of purchasing or management companies?

A: Essentially, for a purchasing company that's not filing in South Carolina, it would be a way of shifting income based on a purchase from an outside entity of South Carolina, outside. But from your -- inside your same group, you're shifting your income away from the South Carolina filer to a company that's not filing in the State.

Q: And in your experience, does the Department automatically impose combined unitary reporting for a taxpayer that has any of the types of business structures described in 15-5?

A: Automatically, no.

Q: And why not?

A: I just think it just depends on the circumstances of the transaction.

Q: And in your experience, does the Department impose combined unitary reporting as an alternative method for every taxpayer that operates -- or is part of a unitary group?

A: No.

Q: Okay. Does 15-5 provide any guidance related to a taxpayer's reliance on I.R.C. Section 482 or transfer pricing studies?

A: I think it -- it, essentially, explains that it -- not that it can't be reliable but it, it doesn't affect -- I'm not sure of the wording in it, but it's not -- well, it's not determinative of an apportionment ratio for South Carolina strictly based on what a 482 says or how it explains the transaction.

Q: All right. And finally, does Revenue Ruling 15-5 provide any guidance on how to calculate the combined unitary income in South Carolina?

A: Yes.
Q: Okay. And did you follow that approach in this case?
A: Yes.
Q: All right. Let's walk through your work papers for the Court and describe that.
Do you recall how many steps there are in 15-5 when it discusses how to calculate the taxpayer's combined unitary income?
A: Exact steps? I -- there's probably like six to eight, maybe.
Q: Okay. All right. Let's start with step one. Let me know when you get there.
A: That's all right. I think I'm on it.
Q: Okay. For the record, this is Joint Exhibit 17, which is 15-5. What page number are you on in 15-5?
A: I was on page six.

(Joint Exhibit Number 17 was referenced at this time.)

Q: Okay. All right. Step one of 15-5 is -- tell me what the step one of 15-5 is?
A: All right. So step one of 15-5, you're gonna do your federal taxable income for the unitary group, which is typically line 30 on the

federal consolidated return, while also subtracting, subtracting eliminations from the total.

Q: All right. So if you could, if you could describe the two documents on the slide, it's titled step one, line 30, federal consolidated return?

(Respondent's Exhibit Number 31 was introduced into the record at this time.)

A: Okay. So, the left side is actually the working paper. So, I guess, this red box is the -- discussing the federal taxable income amount, which is also, like I said, on line 30, which in this case is the 575 in this example. That would be minus the eliminations on top.

Q: All right. So just so the record's clear, on the left side of the page, who's document is that?

A: That would be the South Carolina work paper in this case for 2016.

Q: Okay. And who prepared the document on the left side of the page?

A: I did.

Q: Okay. As the Auditor for Tractor Supply Company?

A: Yes.
Q: All right. Now, let's look at the right side of the page. What document is that?
A: That's the federal consolidated return, page one ---
Q: Okay.
A: --- 1120.
Q: For?
A: Tractor Supply Company and subs.
Q: All right. All right. So let's go to slide two. Step two under 15-5 is what?
A: So this is gonna be the combined unitary income. The red box actually is the combined income before the elimination. In this instance, when you're working with the eliminations being taken out for South Carolina unitary income, it's gonna work from left to right. So, essentially, the first line from my work papers -- actually, the furthest column to the right on the bottom which shows that the elimination was taken from the combined column on the left.
Q: All right. Now, if we'll go to step three. What is step three?
A: So, step three is essentially what I just said

with the eliminations, that's gonna show the combined eliminations through the whole unitary group line-by-line.

Q: All right. And we'll go to step four. What is step four?

A: Step four on the left and the right. So the left side is gonna be the summary, essentially, of line-by-line through one through 15. The right side is actually just to sho- -- like, a small breakdown showing what the modifications were, so addition and subtractions from the South Carolina state return.

In this case, they matched. So we gave them credit for the addition and subtraction on the South Carolina return for that period.

Q: All right. And if we'll go to step five. Can you, can you describe what step five is? And I think this one's gonna be a two-part -- step five, this particular slide describes the numerator. So if you could describe that for the Court, please?

A: Okay. The left side is the South Carolina state return that was filed by the taxpayer. The red box shows the South Carolina sales, which in this case, matches the 160,942,647.

The right side is the work paper side of it, so it's showing that we gave them credit for South Carolina sales, so that, that figure would match the state return.

Q: All right.

MS. WOOTEN: (To Ms. Gamble) If you'll advance to the next slide.

Q: And if you could describe slide -- step five, single sales factor denominator?

A: So the denominator in this case on the right side is still the work paper, it's broken down by each entity. Also the adjustments on the second-to-last column is actually going to coincide with eliminations that were taken on the federal return. So, essentially, the way that the right side of this works with work papers, is those adjustments work right to left. So the everywhere sales adjusted does have the eliminations included, so those are the -- the confirmed numbers would be the right -- the red box on the right side. And then, on the left side, each line item that's added in, and it's described at the bottom of the work paper -- actually, it's added and then included into that, so that's where you would run into the work paper.

Q: All right.

MS. WOOTEN: (To Ms. Gamble) If you will advance to the next one.

Q: So we'll go to step six. And describe step six for us.

A: This is just for amounts that were directly allocated to South Carolina strictly based off the state return. They didn't have anything on the Schedule above it. And then, line two is actually blank, as well, so we didn't have to add anything within the work paper for that.

MS. WOOTEN: All right. If you'll advance to step seven.

Q: If you could describe step seven for us?

A: Step seven in this case is gonna be, just, any sort of South Carolina net operating loss carried forward that they may've had, whether it was within the year carried forward, in general, they did not have that either on the state return, therefore it's a zero on the right side, which is the South Carolina working paper.

Q: All right.

MS. WOOTEN: And if you advance to step eight.

Q: If you could describe step eight for the Court, please?
A: Step eight is the credit carry over that they had. And actually they accrued that credit during the period and it essentially gave them credit for the 22,646 on the work paper, just to show that they had the credit before ...
Q: All right. So now we've gone through this -- the eight step process under 15-5.
MS. WOOTEN: (To Ms. Gamble) If you will advance to the last.
Q: All right. If you will describe the -- what is being shown on this particular slide?
A: Okay. So the right side, I guess, is the Department Determination and the way that they've added that up, the tax, kind of, like the interest. The left side appears to be an Excel essentially adding and giving credit, it looks like maybe for tax reported, that way it comes to the balance for each year, and then it's added up at the bottom.
Q: Okay. And under that Excel, is that figure, the total figure, how does that relate to the figure on the Department Determination?
A: That -- it's just the total tax for all three

years combined.

Q: Is it the same number on both sides?

A: Yes.

Q: All right. Thank you. All right.

MS. WOOTEN: (To Ms. Gamble) If you will advance a bit to the work papers. All right. I think it's 14 -- 13. If you'll up 13 for me?

MS. GAMBLE: Sure.

MS. WOOTEN: Yeah. Joint -- well, 14 and pull up 15. Let's try 13. Okay.

Q: Under -- we're looking at Joint Exhibit 13, and you testified earlier that these are your corporate working papers, correct?

(Joint Exhibit Number 13 was referenced at this time.)

A: Yeah.

Q: Okay. On this page, it appears that there are penalties stated on this particular page. Is that correct?

A: No.

Q: Okay. Can you explain to the Court why penalties are on the corporate working papers?

A: So that's actually -- I don't know, it's essentially a system error. So what happens is, is when you run and create work papers for each individual period within our audits for corporate, it automatically starts to apply a penalty from the system. Typically, whenever this happens, we have to explain, hey, these penalties aren't really real. If you go to the proposed assessment letter itself it will show that the penalty is actually zero. But it's not something that we've ever been able to get the system -- IT to essentially fix or wipe out, or somehow get it to apply it properly.

Q: Okay. So for the record, you did not apply penalties in -- as part of your audit?

A: No.

Q: All right.

MS. WOOTEN: And if you will pull up 15 -- Joint Exhibit 15? All right.

(Joint Exhibit Number 15 was referenced at this time.)

Q: Do you recognize Joint Exhibit 15?

A: Yes.

Q: Okay. And what is it describing with regard to penalties?

A: It shows a zero.

Q: Okay. The -- was this document provided to the taxpayer?

A: Yes.
Q: Okay. All right. Was interest added as part of the proposed assessment?
A: Yes.
Q: Okay. And why was interest added?
A: I believe it's, it's statutory. It's a -- we can't adjust it on our end, at all.
Q: Okay. All right. I'm gonna remind you of 12-54-240, we refer to that as the prohibit- -- Prohibition Statute -- or, sorry, Disclosure Statute. So I'm reminding you of the Disclosure Statute first before I ask you these questions.
Turning back to your experience with the Department and unitary adjustments, in your experience, have taxpayer's petitioned the Department to use combined reporting as an alternative method when filing its South Carolina income tax returns?
A: Yes.
Q: Okay. And does the Department grant those petitions?
A: Sometimes.
Q: Okay. And why would they grant them sometimes?
A: I think it would be based on the circumstances

of the taxpayer.

Q: Okay. And in your experience as an auditor, have you made a unitary adjustment against a taxpayer at the conclusion of an audit examination where the tax liability resulted in a refund for that particular audit period?

A: Yes.

Q: Okay. Did the taxpayer -- as part of the situation we're just talking about, did the taxpayer request the unitary adjustment or did you recommend the unitary adjustment at the conclusion of your audit examination?

A: It -- we recommended it at the end of our audit examination.

Q: Okay. And again, without divulging any names or specifics on the return, what industry did that particular taxpayer operate in?

A: It was retail sales.

Q: Okay.

MS. WOOTEN: Thank you, Your Honor. One -- I take that back. The Department would offer Respondent's Exhibit 31 into evidence. It is the calculation that Mr. Riggs just described as part of his audit examination.

(Respondent's Exhibit Number 31 was offered into

evidence.)

MS. GEER: No objection.

THE COURT: It's admitted.

(Respondent's Exhibit Number 31 was admitted into evidence.)

MS. WOOTEN: Thank you.

THE COURT: How long is your cross gonna be, whoever's gonna do it?

MS. GEER: I'm trying to think how long we -- how long we've been going since the last break? I would guess -- and it kind of depends, but at least half an hour, maybe ---

THE COURT: Okay.

MS. GEER: --- 45 minutes ---

THE COURT: Well, let's just take a ---

MS. GEER: --- to an hour.

THE COURT: Let's just take a quick break then.

MS. GEER: Okay.

(Off the record from 4:38 p.m until 4:44 p.m.)

THE COURT: All right. We have honed down your cross-examination?

MS. GEER: I hope so. I hope. Okay.

(*Whispering.*)

MS. GEER: It's a little warm in here. Anybody else? (To Ms. Wooten) Were you thinking that?

MS. WOOTEN: Yes.

THE COURT: Yeah. 'Cause certain people are talking a lot.

(*Laughter.*)

MS. GEER: I'm contributing is what you're saying? All right.

MR. RIGGS - CROSS EXAMINATION BY MS. GEER:

Q: Mr. Riggs, we've met before. Good to see you again.

A: Yes.

Q: So in your earlier testimony, if I heard you right, you were a Foreign Auditor at the Department for about three and a half years ---

A: Yeah.

Q: --- is that right? Okay. And during that time you performed about 30 audits total, half and half, as between lead and supporting?

A: Yeah, roughly. Roughly.

Q: And September of 2019 I think is when you became a -- an Audit Selection Analyst, is that right?

A: Right around the end -- maybe -- might've been maybe the first of October.

Q: Okay. And so, am I understanding correctly

that you don't do any more foreign audits anymore, you're strictly doing this new position?
A: Yes.
Q: Okay. And if I recall correctly, this Tractor Supply audit might've been one of the first few audits that you worked on as lead, am I remembering that right?
A: I -- yeah, probably. It had to have been within, you know, maybe the first five-ish.
Q: Okay. All right. So you understand that some states have separate entity reporting as their required filing methods, and some states have combined unitary reporting as their required filing method?
A: Yes.
Q: Okay. And you know that South Carolina has chosen separate entity filing as their filing method?
A: Yes.
Q: And you agree that the stan- -- sorry. You agree that the Alternative Apportionment Statute can only be used when the standard method of apportionment does not fairly represent a taxpayer's business activity in the

state and the alternative method is reasonable?

A: Correct.

Q: And if you choose (A)(4), any other method, it also has to be equitable?

A: Yes.

Q: All right. So if you determined based on your analysis that the standard method does fairly represent the taxpayer's business activity, then the analysis ends and you cannot invoke alternative apportionment?

A: Correct.

Q: All right. And I think you agreed that Tractor Supply's business activity in South Carolina is the sales in the retail stores in South Carolina?

A: Yes.

Q: Now, what evaluation did you do during the audit to try to measure Tractor Supply's retail stores' business activities in South Carolina?

A: So, it was strictly based on the sales that they had that they were showing on the state return, would've been the initial review, considering it was the sales factor for retail. The state return, we would review that first, and the worked our way in to that for the review.

Q: Okay. So you looked at the, the income that was showing -- that was being reported by TSC on their return as filed?

A: Yes.

Q: And so did you agree that that measurement did represent their business activities in the State?

A: I think we agreed that the sales factor was the proper sales factor and that what they stated on the return was from South Carolina sales.

Q: Okay. But when you're trying to measure -- are, are you, are you agreeing that that measurement, the sales factor that was used by Tractor Supply, fairly represented the taxpayer's business activity in the State?

A: For their South Carolina sales on the numerator.

Q: And I'm not just talking about for the -- determining the sales factor, I'm talking about your attempting to measure what the taxpayer's business activities are in the State.

A: Right. So, I mean, essentially -- initially, when we reviewed that, we would go off the state return 'cause that's what they filed.

After that, once we began to see intercompany, we thought there was distortion in the income -- unitary group, then we would look at them as a whole, and then we would start to determine the sales factor for the -- for that point -- at that point.

Q: Okay. So what you're saying is, at some point, you determined that it was a unitary business and so you believed you did not need to look at what was being reported on the return, the as-filed method, but you needed to look at the unitary group to determine the taxpayer's business activity in South Carolina?

A: Yeah -- I guess, yes and no, 'cause we did look at the state return and we actually used their South Carolina sales. But once it got to the point of unitary and unitary adjustment, then we would look at the whole group. So, essentially, I guess, it's yes and no.

Q: All right. And you've used the word, distortion. Do you mean that to be synonymous with the taxpayer's business activity not being fairly represented in South Carolina?

A: Yes.

Q: Okay. And I think you believe that any amount of, what you see as distortion, even if it was one percent distortion, that that would be sufficient to invoke the Alternative Apportionment Statute?

OBJECTION:

MS. WOOTEN: Assuming facts not in the record, Your Honor. I believe she said she's -- he stated one percent.

THE COURT: I think she said he believed.

MS. GEER: Yeah.

MS. WOOTEN: He believed. I don't think there's been any testimony about what he believes about one percent.

MS. GEER: I'm not saying he stated it now ---

MS. WOOTEN: Okay.

MS. GEER: --- I'm saying it's my understanding that that's what he thinks.

Q: Let me ask you that, so ---

THE COURT: Yeah. If you just rephrase that, you're gonna get there.

Q: Do you think that any amount of distortion, even one percent, is sufficient to invoke the Alternative Apportionment Statute?

A: Yes.

Q: Okay. So if it's distortion, it's distortion,

no matter what level?
A: That's -- yeah.
Q: And did you make any attempt in this case to quantify the amount of distortion that there was?
A: No.
Q: Okay. And that's because you didn't think it was relevant. If it was any, it was enough to invoke the Statute, so you didn't need to determine it?
A: Correct.
Q: Okay. All right. And in cases where a taxpayer has intercompany transactions or related party transactions, is it your opinion that distortion exists regardless of whether the transactions are priced at arm's length?
A: No. I think it just depends on the transaction itself. It doesn't have to -- I don't -- you know, if it's arm's length, it's still a transaction that's occurring.
THE COURT: So, I can be clear, if it's a arm's length transaction, you believe it still could be distortion?
A: It -- in this case, yes, because it's still happening -- the transaction's still occurring

between related entities self-contained within the group itself, the unitary group.

THE COURT: All right.

Q: So -- and just to make sure I'm understanding, you, you think that there are cases where even if it's at arm's length price, it still can be distorted?

A: Yes.

Q: All right. And I think you said that you did not attempt to evaluate or determine whether the procurement charge was an arm's length charge?

A: Well, I read the 482, but I can't tell if that's a yes or no. I can't, I can't gauge that. I can just read it and understand it, and it was a transaction.

Q: But you didn't attempt to do your own analysis on that point?

A: No.

Q: And I think you said you earlier you didn't -- you don't have 482 expertise, is that correct?

A: Correct.

Q: And did I understand your testimony right that, the two main things that you think show distortion here are the existence of a unitary business along with the existence of intercompany transactions?

A: It -- yes. It was essentially the intercompany transactions were -- we thought was distorting the income of the group in South Carolina based on the, the business activity.

Q: Okay. So, let me ask you about a -- relate -- a third party transaction versus a related party transaction. So if Tractor Supply had paid the procurement charge to a third party that was not related in any way, you wouldn't've had an issue with that payment, correct?

A: No.

Q: And so, if Tractor Supply had paid that third party, Tractor Supply could've claimed a deduction on it's South Carolina tax return for those expenses, and you're saying the Department would not try to argue, based solely on that third party transaction, that the taxpayer's business activities weren't fairly represented in South Carolina?

A: Based solely on that one transaction ---

Q: Right.

A: --- right.

Q: Right.
A: To me, the income would not have been staying within the group's income, it would've been leaving, going to a third party.
Q: And so, is that the key for you, is that it's because a South Carolina taxpayer is paying money to a non-filing related entity?
A: I think following 15-5, that shows to me that there was distortion by shifting that money out of South Carolina, but then following with 15-5, it does explain that it's a unitary group and the rest of the transactions all show that, as well. So, the procurement transaction itself is really the shifting of the income out of the State, but at the same time, 15-5 is explaining the unitary group that falls in line with that ---
Q: Uh-huh.
A: --- with the other transactions that are occurring.
Q: So if, for example, Tractor Supply decided tomorrow that they were tired of providing -- Tractor Supply of Texas was tired of providing the procurement activities or it was, they didn't have enough employees or something along

those lines, and Tractor Supply went out on the open market and said, we got to find somebody, and they found a third party, and let's just assume that they are performing the exact same functions as what Tractor Supply of Texas was performing ---

A: Uh-huh.

Q: What is your position there as to whether at that point the Trac- -- Tractor Supply's business activities would be fair -- could be fairly represented in South Carolina?

A: I think that's the same example. So, if it's going to a third party, they're not keeping that income from the sales ---

Q: Okay.

A: --- within their, their own unitary group. So all the sales that they're using -- they're purchasing from Texas for ---

Q: Right.

A: --- that income is staying within TSC on a unitary aspect, 'cause they're all in the same group ---

Q: Right.

A: Whereas in your example, if TSC Texas is now anything else, ABC Texas outside of that group

---

Q: Uh-huh.

A: --- and all that income's going to them ---

Q: Yep.

A: --- that does -- that all of a sudden changes that whole transaction in general. Now, there might be other instances here or there that might happen and occur, but the majority -- or all of the sales at that point, if now the ABC group was now the sole seller of merchandise, that changes the whole aspect of that group in general, plus the audit itself, so.

Q: Okay. So, I guess, help me understand. It seems to me that with the third party situation, the reason that you're comfortable with it is that it's an arm's length transaction. You know it's an arm's length transaction because it's with a third party, is that right?

A: I mean, I guess, if it's a -- there's a 482 and all that kind of thing.

Q: No, no. I'm talking about a third party transaction. Like, is the reason you're comfortable with it happening with, with -- the reason you believe that the standard method

fairly represents a taxpayer's business activity in South Carolina when they're paying it to a third party ---
A: Uh-huh.
Q: --- versus paying it to a related entity, is it because it's a third party, so you can feel some comfort level that it's arm's length?
A: No, I think it's just, in general, is that the income is now leaving the company as a whole. So, whether there's a markup included, whether there's just straight purchases that they're making, the company is now losing that money, whereas right now it's staying within itself ---
Q: Well, it's leaving the company either way. It's leaving Tractor Supply Company either way. You're saying that because it's staying with a member of the group, that's the problem?
A: Right, because it's still the same group that has a federal consolidated return that has their total unitary income on that. So, if that income disappears and goes to a third party, depending on that transaction and their agreements and guidelines, that federal consolidated return changes.

Q: But in my example, no more money is leaving Tractor Supply Company as an individual entity under either scenario, would you agree with that? Either way they're paying for ---

A: If it's the same exact information just not going within the group it's going outside the group, right.

Q: Right. So let me, let me make sure, 'cause I don't think I -- I don't think I asked my question very clearly.

A: All right.

Q: In either scenario Tractor Supply Company is sending -- let's just say it was $1,000 -- is sending $1,000 outside of its entity to procure that function?

A: Right.

Q: Okay. All right. Y'all tal- -- you talked about Revenue Ruling 15-5, and you said -- I think you agreed that combined reporting is not automatic for a unitary business?

A: Right.

Q: Okay. And you talked about that 15-5 sets forth six factors that the Department considers?

A: Right.

Q: Okay. And did you receive any specific training on how to apply these six factors, or was it on-the-job training?
A: It would've been on-the-job training.
Q: All right. So, for the -- the first factor is amounts paid to related parties for goods and services or goods and services provided without payment. Tell me what you're looking for there?
A: That, essentially, I think fell in line with the procurement company, with Texas.
Q: I'm sorry. I -- it's not your fault, I just -- I got distracted and I couldn't hear what you were saying. Do you mind starting over?
A: Sure. That it's -- for me it coincides with Texas, Tec- -- Tractor Supply of Texas, their procurement, the trademark ownership, not charging for that, but also being the sole contributor for merchandise to the stores which includes Michigan and TSC. So, to me the related entities purchases, services, sales.
Q: So, let me back up and just not talk about Tractor. When you -- this factor itself, like, just in general, amounts paid to related parties for goods and services or goods and

services provided without payment, are you just looking to see whether it's paid or not paid or, what does this factor mean in general?
A: In general, I think it's just saying, are there intercompany transactions ---
Q: Okay. So ---
A: --- occurring?
Q: --- just are there -- do they exist?
A: They just are occurring.
Q: Okay.
A: To related parties.
Q: And so, here -- I think in the audit you were only looking at the procurement charge, is that correct?
A: In terms of?
Q: In terms of your finding that there was distortion?
A: Essentially, it was the -- procurement was the largest -- like, the big one.
Q: Okay. And when you applied this factor to this case, you looked at the procurement charge and you were just saying, under this factor it exists? Like, that was all you looked at for factor one?
A: Well, and it, it would've been transactions in

general, so it would have also included the other agreements that were happening ---

Q: Okay.

A: --- so, you know, the management.

Q: To look at the existence of those?

A: Right. Just ---

Q: Okay.

A: --- and anything that was showing transaction that was intercompany within itself or related.

Q: All right. And then, the second one is profit margins associated with business activities. Tell me, in general, what it means, and then if you want to jump ahead, how it applied here.

A: So for me it was the profit margins in general for -- in this case, for me it was always what's the profit margin have to be in order for a transaction to occur, 'cause I think that was kind of what it went with with the agreement itself. So I always apply that, meaning, all right, well, is that included in the transaction, or what's the background of the transactions that are occurring. So, you know, does it have to be a certain profit margin for it to occur, things kind of like that.

Q: Wait, so -- okay. Does it have to be a certain profit margin? Tell, tell me how that one applies here and maybe I'll understand what you're saying.
A: So, for instance, like on the agreements for the memos, I think they talk about a markup, but they also have to make sure that there's a profit margin ---
Q: Okay.
A: --- available ---
Q: Right.
A: --- for it to occur, whether they charge the fee, or how much of a fee and whatnot.
Q: Okay. So in this particular case, the transfer pricing, it gave a range for what the procurement charge should be, and it also gave a range for what the expected profits of the retail stores would be if that profit was charged?
A: Right.
Q: So that's what you're referring to?
A: Yes.
Q: And did you look to see what the -- what that second part was, what the profit was of the retail stores?

A: Well, I've looked at the ratios that they gave. So they had -- they gave us the range itself and then they gave us the actual percentage that they chose ---
Q: Right, but did you ---
A: --- for them.
Q: --- yourself evaluate or look at what the return on sales or ---
A: No, I didn't.
Q: Okay.
A: No.
Q: You didn't look at that. All right.
All right. The third one is capital investments associated with business activities. Is this one you're familiar with?
A: Not terribly.
Q: Okay.
A: I didn't make an adjustment for it.
Q: Okay. Did you even apply it in this one?
A: No.
Q: Okay. Do you, do you know what it would mean in another -- just in general?
A: I never actually made an adjustment on it ---
Q: Okay.
A: --- so.

Q: So you don't know what this one ---
A: Typically, I wouldn't ---
Q: --- is looking for?
A: Yeah, I wouldn't really use it.
Q: Okay.
A: I never have used this, put it that way.
Q: Okay. All right. The fourth one is whether goods and services are provided to both related and unrelated parties on similar terms. Is this -- what does this one mean to you?
A: It's just asking if the same transactions were being offered to third parties or if a third party was being used for the transaction.
Q: Okay. And how did that apply here?
A: They, they didn't have third party transactions occurring within Texas and Michigan and TSC.
Q: All right. Number five, whether taxpayers in similar industries provide similar goods and services to unrelated parties under similar terms. What's that one looking at?
A: It's -- it sounds similar to the 482. So 482 kind of gives you the background of comparables, so that's probably applied through that based on the 482. You know, a specialist was, was reviewing that. For me, that

technically meant, did the 482 come with a complete review of the transaction itself. Sort of a backup to make sure that I could see what the overall idea of the transaction was.

Q: All right. I might not've followed you, so let me, let me ask a follow-up question.

So, are you saying that this one is looking at 482 considerations and trying to determine whether it's a arm's length charge?

A: I -- no, I think it -- it's technically -- for me it was saying, all right, well, there's comparables in a 482. But I'm reviewing the 482 just to see the background of the transaction itself. So, essentially, if I'm thinking about both of those at the same time, is it being offered to somebody else, is there something similar to that but it's not within the group, so there's really not, in this case, there's not because they're not doing third party or it's not within the group itself, or outside of the group.

Q: And so, how did that, how did that one weigh in this case?

A: It, it didn't weigh much. I mean, it -- if it's talking about comparables, there wasn't really a comparable, 'cause it was all self-contained within the unitary group for me.

Q: So to -- in your mind, this factor didn't give you any new information?

A: No.

Q: Okay. All right. Number six, whether the taxpayer would be willing to enter into a similar arrangement with an unrelated third party considering among other things, the relinquishment of control over the business. In general, and then in this case?

A: So in general, were they willing to use a third party, did they use a third party, would they want to? I guess, those are all the general kind of ideas of it.

Q: Yep.

A: And then, this -- in this case, they didn't, so. I mean, I can assume they would if they could, they would if they wanted to, but they didn't. So for me it was the fact that they, they didn't do it, so they didn't ---

Q: Okay.

A: --- do it.

Q: So the fact that they didn't do it, in your mind, meant that they were not willing to do it?

A: Yeah.

Q: Yeah. Okay. All right. Do you understand that the Department has 482 powers?

A: 482 powers, I'm not sure what you mean?

Q: They -- could the Department choose to deny part or all of a deduction if, for example, they determine that an intercompany charge was too high or too low?

A: I don't think that they could -- they would do that.

Q: So you don't think when you were an auditor that you had the ability to adjust a charge if you didn't think the charge was appropriate?

A: Not -- if we're talking about a 482, I'm not a expert on it, so I couldn't say yes or no on that.

Q: Okay.

A: Now, if you're saying just, in general ---

Q: Yes.

A: --- if I could do an add-back or I could do a subtraction, you know, something like that, that's something that usually would go above an auditor's, you know, correspondence really. So ---

Q: Okay.

A: --- that could be something that you could entertain and you could provide for your supervisor, and then they would have to say, okay, we can do that. That's not really an option as an auditor to make and send it through and be done. That has to go above them to make sure supervision, managers, anybody else has to be the one that really makes that decision, the auditor can't. So, could I say, hey, I think we could do this, what do you think? I can do that.

Q: Okay.

A: But it solely really wouldn't be my decision to begin with. So if that's in a conversation with a taxpayer and you -- and we're kind of talking about, and I said, look, I'll run it by them, let me run it by them if I think that's logical or something, that's a fix or whatnot.

Q: Right. And so, when you were a Foreign Auditor, if you had information or the taxpayer offered you information that indicated that the charge could be adjusted -- let's say it was ten percent and they -- you received information from some source that said that six

percent might be more appropriate ---
A: Uh-huh.
Q: You would then take that to your supervisor and see if that was something that could be worked out?
A: Sure. If, if that was a conversation that was had, yep.
Q: Okay. So the Department has the ability to do that, but what you're telling me is that -- did, did you ever do that?
A: No.
Q: Okay.
A: I didn't have that conversation for any sort of alternate adjustment.
Q: And let me make sure I'm clear. Did you ever do that for any taxpayer?
A: I think, honestly, that there might be one that I did do, that was brought up and we discussed it, and it was forwarded and the supervise said we can, we can do that.
Q: Okay. And how -- I'm just curious, how did that one come up? Like, what was the information -- not -- without saying a taxpayer name, just ---
A: Sure.

Q: --- what type of information made you consider it in that case?

A: We were talking about a royalty that had a fee on it, and instead of, you know, saying well, this needs to be added back, essentially, what they would do is -- well, they wanted to add it back, but then what we did was, you had to change the apportionment based on a royalty, 'cause it was strictly used for that ---

Q: Uh-huh.

A: --- they didn't do anything else other than that. So because of that, that was portrayed as, all right, well, is that something that we could just do as an add-back or essentially adjusting the apportionment for strictly royalties, and then I just forwarded that to the supervisor and they agreed and said that we could run it that way.

Q: Okay. All right. And just to close the loop on that, the Department did not consider doing that in this case?

A: It was never brought up, no.

Q: And in this case, did you -- did the Department ever attempt to assert nexus over TSC Texas in this case?

A: No.

Q: All right. And so, in the 30, approximately, 30-something audits that you've performed, was it pretty rare that the taxpayers in those audits operated out of a single entity?

A: No.

Q: So there were a lot that operated out of a single entity in those audits?

A: No. So, typically, you would -- a lot of audits you would get a Federal Consolidated Return as a backup and there would be multiple entities in them.

Q: Okay. That's my question.

A: Right.

Q: In most of those audits that you were doing, was the taxpayer -- did the taxpayer have subsidiaries?

A: Yes.

Q: Easier way to say it.

A: Yep.

Q: Okay. All of them, or?

A: That said -- well, yeah. I mean, the majority, I'd say.

Q: Yeah. And in those cases where there were subsidiaries, was it pretty common to have intercompany transactions between subsidiaries?

A: Sure. Probably, yeah.

Q: And, as compared to other companies that you've dealt with on audit, there may've been some differences between Tractor Supply's structure and other taxpayers, but nothing stood out to you as being unique, is that right?

A: Unique, in terms of all the audits that I've done, or unique in ---

Q: Yeah.

A: --- in general? Out of all of the audits that I've done, they're all so different anyway, it's hard to say that they pretty much weren't unique, 'cause they -- none of them were really the same.

Q: And based on the facts that you reviewed during the audit, you believed that Tractor Supply, TSC of Michigan, and TSC of Texas all had economic substance, correct?

A: Yes.

Q: All three entities had stores, they had employees, they had functions, they weren't empty companies doing nothing, correct?

A: Correct.

Q: Okay. And you assumed that Tractor Supply entities had a business purpose since they had stores they were operating and they were earning money, right?

A: True.

MS. GEER: I apologize, Your Honor, I'm just making sure I caught everything.

THE COURT: I'm learning that your handwriting looks like scribble.

MS. GEER: It does. Which probably doesn't help that it's upside down for you.

THE COURT: Yeah. Well, it's just scribble I can't read.

(*Laughter.*)

Q: You talked a little bit about the prior audit that was done before this one. Why was Michigan not included in -- so let me, let me back up.

The Department, in the prior audit, invoked alternative apportionment and did a combined reporting method, correct?

A: Yes.

Q: And they only included TSC of Texas and TSC, correct?

A: Yes.

Q: Why didn't they include Michigan?

A: I, I don't know. Or the only -- I mean, we didn't have 15-5 then, so that might've been a reason. But I didn't do that audit. The only thing I know about it is -- was basically the Excel worksheet that he had and the descriptions of the, of the Company's front them.

Q: Okay. So when you say, we didn't have 15-5 then, are you attempting to convey that you didn't have guidance that might've told you to include Michigan, or what are you -- what do you mean by that?

A: Well, with 15-5, we applied it here and we worked it exactly at -- the way it was portrayed and written. So, if it wasn't around back then, I can't really explain why they didn't include them, because I wasn't there.

Q: Fair enough. During your direct you pulled up a e-mail on the screen, I think it was Joint Exhibit 16, and it said -- let's see, I'm trying to read my scribble.

Oh, they sent you an e-mail that, I believe, had summaries of the agreements?

(Joint Exhibit Number 16 was referenced at this time.)

A: Uh-huh.

Q: Okay. And then you mentioned something about not looking at the actual agreements?

A: I didn't receive them, so ---

Q: Okay.

A: --- essentially, we questioned what they were from based on what the white papers were showing and transactions ---

Q: Right.

A: --- and we got the responses back in the e-mail ---

Q: Okay.

A: --- and not the agreements.

Q: And I'm assuming that what was provided in the e-mail was sufficient for your purposes, or I'm assuming you would've asked, asked for them again?

A: Yeah. It -- well, it answered the questions that we had ---

Q: Okay.

A: --- in the e-mail from it, so ---

Q: Okay.

A: --- he answered them directly in the e-mail ---

Q: Yep.

A: --- instead of just, here's the agreement (indicating).

Q: Okay. Now, the examples that are given in 15-5 that you mentioned that were in those footnotes, 13, 14 and 15 that talk about different business structures, is that language from any Statute?

A: Not that I know of.

Q: Any case?

A: I can't give you an exact case. I just know that those were probably examples that were given for 15-5 based on what they led up to writing 15-5.

Q: So you don't have personal knowledge about ---

A: I don't know.

Q: --- where those came from?

A: Right.

Q: Okay. But you do not know of any particular statute or case that those came from?

A: No. The only case I know that regards 15-5 that -- which those are in, is from *Media General*.

Q: Okay.

A: And then, probably any other case that it may discuss within 15-5 itself.

Q: Okay.

MS. GEER: Your Honor, if I could have three minutes I will be able to ---

THE COURT: Okay.

MS. GEER: --- wrap this up.

(*Whispering*.)

Q: All right. One last ... All right. So, you talked about the licensing ---

A: Uh-huh.

Q: --- agreement. And are you aware that PwC gave T- -- TSC -- that's a lot of initials -- a transfer pricing study that actually attempted to value what that charge should be for that licensing?

A: That, that was the 482?

Q: Yes.

A: Yeah.

Q: Okay. And it gave a range of, like, between 1.7 percent and 7.5 percent, does that sound familiar?

A: Yeah, yeah. I think so.

Q: Okay. All right. And so, I'm assuming that if Texas didn't waive the charge and actually charged the additional amount, the Department would say that money should not be being shifted out of TSC to TSC Texas, right?

A: Correct. It, it would've been another transaction.
Q: Okay. So y'all would not have been happy with that money going there. I was just trying to make sure I understood whether you were complaining about the fact that they didn't charge it, or if you -- my assumption would be, that you would complain if they had charged it?
A: Right. I think the idea behind it actually is the ---
Q: Yeah.
A: --- the fact that, because they're not charging it --
Q: Yep.
A: --- you have to buy everything from us. So, essentially, it's, it's kind of locked into the same transaction even though it's the IP plus the procurement. Not that that changes the transaction, it's just the background behind it.
Q: All right. This is not your fault at all, it's probably that it's late in the day, but I did not, I did not follow that at all. Can you tell ---
A: Okay.

Q: Can you explain it one more time?
A: I think -- the idea for me was that the IP, while they're not charging the fee for it ---
Q: Okay.
A: --- it's also saying that, you know, we have to be your sole supplier of goods for sale.
Q: And where are you getting that from?
A: I'm pretty sure that was in the agreement. So it's ---
Q: Okay.
A: It says we're not gonna charge you this to, to keep it in the margin, but we're also gonna be your sole ---
Q: Okay.
A: --- provider.
Q: Yep. And is there something about that -- what does -- what relevance does that fact have to your analysis?
A: I just think that was what the transaction is, and ---
Q: Okay.
A: --- I was just trying to compare it to what your example would be as if they charged the fee on top of that, it would just be creating more income for Texas.

Q: Okay. So what I'm trying to make sure I understand is, any complaint you have about the licensing fee not being charged, is there anything that your -- in your conclusions tied to a complaint about that, or not?
A: I don't think so.
Q: Okay.
A: I just think it's the transaction that's, that's occurring.
Q: Okay. All right. Thank you for your time, and I'm, I'm gonna turn you back over to Ms. Wooten.
THE COURT: You said the range in the four ---
MS. GEER: 482?
THE COURT: Yeah, four eight -- was it 1.7, to?
MS. GEER: Let me find back where I put that.
MR. STREISEL: 7 point ---
MS. GEER: 7.5.
THE COURT: 7.5? Okay.
MS. GEER: Yeah. 1.7 to 7.5.
THE COURT: Okay.
MS. GEER: Okay.
THE COURT: Re-direct?
MS. WOOTEN: Yes, Your Honor. If I may have 30 seconds?

THE COURT: Okay. I'll start counting.

MS. WOOTEN: Please.

(*Laughter.*)

MS. GEER: Do you promise?

MR. RIGGS - RE-DIRECT EXAMINATION BY MS. WOOTEN:

Q: Earlier in your -- Ms. Geer's questioning, she asked you about economic substance, do you recall that?

A: Yes.

Q: Okay. What does that term mean to you?

A: Just the fact that they have income coming in and that's their effort, is to have income coming into the company. Essentially, like she said, it's not just a shell of a company and they're not operating -- they're still in a return. To me, it still shows that they have income coming into the company or affiliates.

Q: All right. And are you aware of what the term means in the 482 Regulations?

A: I ---

Q: Are you familiar with that?

A: I'm not super familiar with it.

Q: Okay. That's because you're not a 482 expert, correct?

A: Correct.

Q: Okay. All right. And you -- in your work as an auditor -- or are you familiar with the *Jeffrey* case?

A: Yes.

Q: Okay. And are you familiar with the Department's application based on the result of the *Jeffrey* case?

A: Yes.

Q: Okay. And what is your understanding of how the Department applies the *Jeffrey* case?

A: *Jeffrey's* typically, for an intangible, usually trademark that's being -- like a trademark fee for a company that's not filing in South Carolina, but they are charging it to a sou- -- a South Carolina filer, therefore let's just say the South Carolina filer would take a deduction for a royalty fee or sometimes it's a management fee, a franchise fee, things like that, to a company that does not file in the State solely for a trademark or a non-tangible service item, trademark, whatnot.

Q: And in that situation, would the Department make any adjustments for that transaction?

A: Typically, if they weren't filing, I, I believe they would just assert nexus on them and use

Jeffrey as the, the backup for that. Other than that, somebody could -- I guess, if they agreed to it and the State was, was accepting to that, they could do an add-back for the amount of the fee that they paid out on a federal return, but that still, that still has to be approved above an audit level -- or an auditor level, so.

Q: So looking at this case, if Texas had charged the, the licensing fee to the South Carolina company, what would the Department have done in that situation?

A: I, I think they still would've done unitary.

OBJECTION:

MS. GEER: Your Honor, I object based on speculation.

MS. WOOTEN: Your Honor, he's an auditor with the Department. He has reviewed Tractor Supply's information. Ms. Geer asked questions about ---

THE COURT: No, you said what -- you didn't ask what he would've done. I think you asked ---

MS. WOOTEN: Oh, okay.

THE COURT: --- what the Department would've ---

Q: What would ---

MS. WOOTEN: Thank you for that clarification.

THE COURT: Not a problem.

Q: In that parti- -- in the instance I was just talking about, if Texas had charged Tractor Supply Company for the licensing fee and you discovered that in this particular audit, what would you have done and what adjustments would you have made?

A: I would've still done unitary adjustment, just because the fee itself, the new fee that was being charged, it would've been an example of another transaction that was occurring, so it doesn't change the fact that the sales were still happening between the other affiliates. It doesn't change the fact that they were a unitary group. It just would be another transaction that the South Carolina filer would be paying out for a royalty fee, management fee, however it would be worded on a, on a federal return.

Q: All right. So let's take the unitary nature out of that example, so it just Texas licensing trademarks to Tractor Supply Company. Just looking at that transaction, if that is the only transaction that you are looking at, what adjustment would you make?

A: If they were strictly doing a license fee -- or a -- say a trademark fee or a license fee, if that's what we're saying ---

Q: Yes.

A: --- the same thing? Essentially, they would have nexus in South Carolina based on *Jeffrey*.

Q: Who would have nexus in South Carolina?

A: The ownership of the trademark and charging the fee, which, I guess, would be Texas in the example.

Q: Thank you.

THE COURT: Anything new?

MS. GEER: Nothing further, Your Honor.

THE COURT: Okay. You may step down. Call your next witness.

(*Laughter*.)

THE COURT: I'm just joking.

MR. LUTHER: It's probably only -- it'll only be about four hours, and I think we can do that.

MS. WOOTEN: I mean, I'm here if you'll be here.

THE COURT: Huh?

MS. WOOTEN: I said I'll be here if you're here.

THE COURT: Yeah.

MS. WOOTEN: Your Honor, at this time, we would ask to recess for the day ---

THE COURT: Okay.

MS. WOOTEN: --- and call -- and begin our -- I believe we'll be calling expert witnesses, which will probably be lengthy, so we would request to start tomorrow.

THE COURT: Okay. And who are you calling?

MS. WOOTEN: We will be calling our account- ---

THE COURT: Or, how many?

MS. WOOTEN: Two.

THE COURT: Two? Okay.

MS. WOOTEN: Hopefully, we can get through two tomorrow.

THE COURT: Okay. All right. I'll see y'all, what time?

MS. WOOTEN: Bry- -- Bryson and I ---

MS. GEER: I mean, I would prefer to start at the same time. I just -- there's a lot of stuff that goes into getting us all prepared and over here in the mornings.

THE COURT: Okay.

MS. WOOTEN: All right. 10:00.

THE COURT: All right. Well ---

MS. GEER: If that suits the Court?

THE COURT: It suits me if we're gonna get done, you know ---

MS. GEER: I, I can't ---

THE COURT: --- tomorrow.

MS. WOOTEN: That -- so that's my question is, maybe we can make adjustments later on in the week, but if we sti- ---

MS. GEER: Let's see how tomorrow goes.

MS. WOOTEN: Our goal is to get this done ---

MS. GEER: Yeah, absolutely.

MS. WOOTEN: --- by Friday.

MS. GEER: Ours too.

THE COURT: Okay.

MS. WOOTEN: And so, if we see that that's going to be an issue, we would request the Court to start or finish late, etcetera.

THE COURT: All right. I'll probably go with early, if that's okay with y'all.

MS. WOOTEN: Okay.

THE COURT: I mean, I get before 8:00, so. Or at least most days.

MS. WOOTEN: Okay.

THE COURT: But I can also go late, too.

MS. GEER: Okay. Well, let's see how we do tomorrow.

THE COURT: All right. The one thing ---

MS. GEER: Let's see ---

THE COURT: --- I will tell y'all is I've got to go over to the General Assembly on Wednesday at 1:30, so on Wednesday I want to take a lunch break around 1:00 to 2:00. It's on my budget, so I'm sorry, y'all.

(*Laughter.*)

MS. GEER: We understand.

MS. WOOTEN: Understand.

MR. LUTHER: Take as much time as you need.

(*Laughter.*)

THE COURT: If it wasn't for those trips, y'all wouldn't be sitting in comfortable seats.

(*Laughter.*)

THE COURT: Okay. Thank you for your time.

MS. WOOTEN: Thank you.

MS. GEER: Thank you, Your Honor.

THE COURT: Tomorrow at 10:00.

(DAY ONE of the hearing adjourned at 5:33 p.m.)

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DAY TWO - TUESDAY, JANUARY 24, 2023

THE COURT: All right. Who's on base?

MS. WOOTEN: I am, Your Honor.

THE COURT: Yeah.

MS. WOOTEN: One housekeeping matter. Yesterday, we offered Joint Exhibits 1 through 53, which were admitted. We gave an electronic copy to the court reporter, and then we have an electronic copy for the Court now.

THE COURT: Thank you.

MS. WOOTEN: May I approach?

THE COURT: Yeah.

MS. WOOTEN: Thank you.

The Department calls Mr. Akash Sehgal.

THE COURT: Mr. what?

MS. WOOTEN: Akash.

THE COURT: Okay.

MS. WOOTEN: Sehgal. Am I pronouncing that correctly?

MR. SEHGAL: Say-gul.

MS. WOOTEN: Say-gul.

MR. SEHGAL: Yep.

COURT REPORTER: If you'll raise your right hand for me.

MR. SEHGAL: (Witness complies.)

COURT REPORTER: Do you swear to tell the truth, the whole truth and nothing but the truth, so help you God?

MR. SEHGAL: Yes.

COURT REPORTER: Thank you.

AKASH SEHGAL, having been duly sworn, testifies as follows:

MR. SEHGAL - DIRECT EXAMINATION BY MS. WOOTEN:

Q: Good morning. Could you please state your full name for the record?

A: It's Akash Deep Sehgal.

Q: And, Mr. Sehgal, what do you do for a living?

A: I am a tax partner at an accounting firm in Los Angeles.

Q: And what is the name of that accounting firm?

A: It's called GHJ.

Q: Okay. And what does GHJ stand for?

A: That's Green Hasson Janks.

Q: All right. The Department of Revenue hired you to serve as an expert witness in this dispute with Tractor Supply, is that correct?

A: Yes, that's correct.

Q: Okay. And what were you asked to do?

A: I was asked to review documents and make -- help the Department make some determinations around -- based on my experience, whether or not certain state income tax provisions and rules were followed and what, what my ex- -- what my, you know, conclusions were after I reviewed these documents.

Q: Okay. All right. Before we get into your opinions, let's review your qualifications.

MS. WOOTEN: Ms. Buckner, can we have the computer, please?

MS. BUCKNER: Uh-huh.

Q: All right. Let's start with your undergraduate education and then move forward with your professional career.

A: Sure.

Q: Okay. Where did you go to college?

A: I went to California State University Pomona.

Q: Okay. And what was your major?

A: Accounting.

Q: Okay. And what did you -- what degree did you receive?

A: I received a B.S. in accounting.

Q: Okay. And after your educational experience, what did you professionally?

A: So, I started my career at Arthur Andersen in 1997 and I was with Arthur Andersen until 1998.

Q: Okay. And if you could, just briefly described for the Court your responsibilities or duties while you were at Arthur Andersen?
A: So, while I was with Arthur Andersen, I was a part of the federal income tax practice, but I also did a lot of state and local tax work. So, I would prepare tax returns, both federal and state returns. I would help with sales and use tax issues for clients. I would help with state income tax, nexus determinations and apportionment determinations.
Q: Okay. And after you left Arthur Andersen, where did you go?
A: So, I joined PricewaterhouseCoopers, PwC, and I was with PwC from February of '97 until February of 2012.
Q: Okay. And if you could, if you could describe your roles and responsibilities at PwC during that time frame.
A: So, while I was with PwC, I was part of the state income -- state and local tax practice, but my primary focus was on state income tax. So, while I was in the Los Angeles office, I -- you know, that early in my career I was spending a lot of time on researching state

income tax issues, apportionment, combined reporting, separate reporting. So, it was a lot of research and writing of memos during that time. And then, in March of 2006 I moved to the Seattle office because the firm asked me to lead the state income tax practice in the Pacific Northwest, which I did from March of 2006 until February of 2012.

Q: All right. And, and just backing up. You said that you were a SALT advisor. What does that mean, and who were you advising?

A: So, most of my clients were large multi-na- -- multinational companies, Fortune 500, Fortune 1,000. Many of them operated on a multistate basis, so they would have operations, whether it was retail, manufacturing, technology, they would have operations in pretty much every single state. My primary focus at that time was, because I had spent most of my career in California up to that point, I was advising a lot of clients in the Pacific Northwest on California income tax issues because for most of the clients in the Pacific Northwest, California was their biggest market state.

Q: All right. And after you left PwC, where did you go next?

A: So, I had an opportunity to join my current firm, Green Hasson Janks to, to actually start and grow the state in- -- the state and local practice. At that time, GHJ did not have a state and local tax resource, did not have a state and local practice, but given the firm was growing substantially, they wanted to grow the state and local practice. So, I joined the firm in August of 2012 to lead and grow the state income -- state and local practice, which includes state income tax, sales and use tax, property tax, etcetera.

Q: Okay. And let me go back to PwC for ---

A: Sure.

Q: --- just a second. As part of your practice in the SALT area and advising clients, did you ever have an occasion to review or be a part of transfer pricing issues or discussions?

A: Yes. While I was with PwC, I was part of their state tax restructuring group. And so, I helped the client -- I helped clients look at their entire structure and help the -- you know, help them structure things in such a way to minimize state taxes or, essentially, reduce the burden of state taxes on their structure. And as part of that, transfer pricing was a significant part of those projects. So, I had a chance at that time to review probably a hundred plus transfer pricing reports and had many in depth conversations with our transfer pricing specialist on, you know, comparables, what it meant from a pricing structure, etcetera.

Q: Okay. And are you a transfer pricing expert?

A: No.

Q: Okay. And are you here to give any kind of opinion from an expert -- or an expert opinion on the 482 Study in this matter?

A: No.

Q: Okay. All right. Moving back to Green Hasson Janks, GHJ, you previously -- you've stated you previously led the SALT practice. Can you explain how that is different or related to what you were doing at PwC?

A: So, it's pretty similar in terms of the day-to-day type work. It's a lot of state income tax, sales and use tax consulting with clients. So, we -- you know, I would advi- -- I advised clients on, you know, how to file in states, depending on whether states are combined reporting states or separate reporting states. We do a lot of apportionment analysis for clients, especially, in California where there are some very unique, specific industry rules around apportionment. So, probably, the main difference between what I did at PwC and what I do at GHJ is, I don't -- we don't do as much restructuring work as I did at PwC. So it's more on the day-to-day consulting side as opposed to these large restructuring projects.

Q: Okay. And as part of your SALT practice, State And Local Tax, have you authored any articles or spoken either at the legislature or any kind of trade groups or organizations related to the topics we've just been discussing?

A: Yeah. I mean, I've spent pretty much my entire career speaking at many organizations and industry groups, State Society of CPA Conferences, etcetera. And many of those topics include apportionment, they include combined reporting and separate reporting and understanding the differences between the various states and, and their rules. I've written articles for the LA Business Journal on combined reporting and, and -- or, sorry, on apportionment methods. And I've spoken at the Council of State Tax. I've spoken at Tax Executive Institute. So, it's something that I do as a regular part of my practice.

Q: Okay. And how long have you been doing that? You say it's a regular part of your practice, but if you could, you know, put a year number on how long you've been ---

A: I would say, I started doing it on a significant basis when I moved to the Seattle office, because at that point in my career, I was at the manager level and, you know, had the confidence and experience to start speaking at various conference and industry groups.

Q: And remind me, did you move to the Seattle office in 2006?

A: 2006. Correct.

Q: So, since 2006 to present, you've been a frequent speaker at various trade groups and organizations?

A: That's correct.

Q: Okay. All right. All right. In your current capacity, do you prepare tax returns?

A: I don't prepare tax returns in my current role, but I review several hundred tax returns during the year.

Q: Okay. And can you just describe that process and what you mean by reviewing the tax returns?

A: Yeah. So, as is the case at most accounting firms, we have staff-level and senior-level individuals. Those with generally from one year to four or five years of experience that do all of the preparation work of tax returns for clients. And that includes federal tax returns. It includes state income tax returns. It includes international forms, etcetera. And once those returns are prepared by the preparer, they go, generally, to what we call a detailed reviewer, which is a manager level or a senior manager level, and they'll do a detailed review of those tax returns. Once the returns are reviewed in detail, they then go to a partner or somebody at that level to do a top-level review and sign the returns. So, in my current role, I do top-level review of returns and I sign most, if not all, of the returns that I review.

Q: What do you consider your expertise that is relevant to this dispute with Tractor Supply?

A: So, I would say it's my experience with state income tax filing methods. So combined reporting, separate reporting. It's -- my experience in California and a lot of states that have a combined reporting regulations and com- -- and mandatory combined reporting. And I would also say that, I have a significant of experience in apportionment issues. So, how to file -- how to prepare returns and research apportionment methods for clients, depending on what type of industry they're in.

So, my two biggest areas of expertise, I would say are combined reporting, apportionment, and then, just general multistate income tax consulting.

Q: Okay. We're going to break down that in just a minute, but let me start with the multistate tax.

Is -- when you say multistate tax, is there a difference between state and local tax and federal practice and multistate tax. And if there is, can you tell us the difference and what area you were focused on?

A: So, federal ta- -- there -- there's a clear difference between Federal Tax and state income tax. Multistate income tax and state income tax are the same thing. So, from a federal standpoint, you know, most, if not all companies file a federal tax return. So, that's done generally by the federal income tax group. From a state and local standpoint, many of our clients -- or many of my clients also filed on a multistate basis. So, they have nexus or they -- they're doing business on a multistate basis, and so a lot of my clients throughout my entire career, may file in several states or all, you know, 45 states that have an income tax.

Q: Okay. And you mentioned that you were an accountant, you're in the accounting area. Are there different areas or specialities within the accounting practice?

A: Yeah. I mean, I -- there's, you know, the two biggest areas, there's the accounting and assurance practice, which it's a practice that does review and audit -- they review and audit financial statements for clients. That's a separate part of our firm. That -- I'm not part of that firm. And then there's the tax side, which is federal tax, international tax,

state and local tax, etcetera.
Q: Okay. All right. And if you will look on the screen, we have Joint Exhibit 24. Can you identify this for the Court, please?
A: Oh, this here. Oh, this is my resume.
(Joint Exhibit Number 24 was introduced into the record at this time.)
Q: Okay.
A: Or CV.
Q: Does your CV list all the professional experience that we just discussed?
A: Yes.
Q: Okay. Is there anything that's on -- that is not included on your CV that you think is relevant and you haven't discussed?
A: No.
Q: Okay. All right. Let's just talk, generally, the process that you go through in formulating your opinion in matters.
To start with, you were retained by the Department of Revenue, correct?
A: Correct.
Q: And are you being compensated for your testimony today?
A: Yes.

Q: Okay. Did anyone at your firm tell you what your opinion should be?

A: No.

Q: Okay. And did anyone at the Department limit your ability to review documents or research?

A: No.

Q: Okay. And were you provided all of the information that you requested from the Department?

A: Yes.

Q: All right. Generally, how do you approach -- or what is your process in formulating your opinion in cases or matters?

A: Yeah. So, I -- you know, it -- it's heavily driven off the facts. So, the first thing I will do for most of my clients is start off with a discussion with the company. So, it's either somebody at the -- in the tax group for the company, depending on the size of the company. It may be the CFO, it may be the controller, it may be the CEO. And what I'm trying to get a sense of is, where does the company operate, where do they have employees, where do they have property, what type of business are they in, how do they generate revenue from various operations? So, the first -- my first step is always, generally, a discussion with clients on their business and how they operate, where they operate, etcetera. So, that's the first step.

Once I get -- once I have those discussions, I will look at documents. So, oftentimes I will look at, you know, a payroll reports. I'll look at their balance sheet. I'll look at their income statements, so I have a better since of how they're generating revenue. If they have parent/subsidiary relationships, I will review their financial statements to get a sense of where revenues is generated in the company, so which entities are generating revenue. And then, once I -- once I've gathered all of the facts, I will -- you know, and have a sense of where the company's operating, I will generally sit down and start looking at the various rules in states around, you know -- because a lot of times clients will come to me and ask me, how should I be filing in these various states. So, once I get all of the facts and do my fact gathering, I will sit down and look at the rules, and sit down with the client and help them make some determinations in terms of how they file in a multistate business.

Q: And for purposes of this matter, could you describe the information that you reviewed as it pertains to Tractor Supply?

A: Sure. So, I reviewed the 10-K. I reviewed the intercompany agreements between the various Tractor Supply companies. I reviewed the pro- -- the 2014 through 2016 federal returns. I reviewed seve- -- a couple of the state income tax returns that were filed. I reviewed the South Carolina returns. I reviewed some memorandums that were prepared by PwC and some other firms that were in there. So, pretty much those documents.

Q: Okay. And did you review any accounting records?

A: I reviewed the trial balance, as well as the financial statements that were in the 10-K.

Q: Okay.

OFFER AS EXPERT:

MS. WOOTEN: Your Honor, at this time, the Department would move to recognize Mr. Sehgal as an expert witness in the area of state income tax accounting, including apportionment methods and multistate businesses.

MR. STREISEL: No objection.

THE COURT: He is so qualified.

MS. WOOTEN: Thank you.

Q: All right. Before we get into your, your opinions in this matter, what is your understanding of the Taxpayer's position?

A: So, my understanding is that the taxpayer's position is that the -- their state -- South Carolina returns for the audit period 2014 through 2016 fairly represent their business activity in South Carolina.

Q: And based on your review, what is the Department's position in this ---

A: The Department's position is that an alternative apportionment method more fair -- or fairly represents the taxpayer's business activity in the State and that separate entity reporting does not fairly represent the business activity in the State.

Q: And we will get in your opinions in detail, but at a high level, do you have any opinions in this matter?

A: I do. I have three opinions. The first is, based on my experience and working with a number of clients that have similar characteristics as Tractor Supply Company, my opinion is that there are several facts and characteristics in this case that suggest that there is unitary relationship between the various companies.

Q: Okay. And do you have a second opinion?

A: My second opinion is that there's a significant amount of functional inter- -- interdependence and dependency between the various companies. There's functional integration, there's interdependency in terms of a significant amount of intercompany transactions between the various companies. And -- so, that's my second opinion.

Q: Okay.

THE COURT: Well, that sounds like that would be a component of the first opinion.

A: That factors into the com- -- to the first opinion.

THE COURT: Okay.

Q: And do you have any other opinions in this matter?

A: Yes. My third opinion is that combined unitary apport- -- combined unitary reporting appears to be a reasonable method in this case.

Q: Okay. All right. So, just to clarify, we talked a little bit earlier about accounting and that there were different sides of accounting. Are you planning to testify that the numbers on the return mathematically are incorrect?

A: No.

Q: Okay. Can you explain your opinions related to that statement?

A: Yes. So, as -- you know, for me to understand the mathematical side of the tax returns, I would need much more information from the company, in terms of in-depth, like, you know, certain accounts, and -- I've reviewed the trial balance, but generally, when we're preparing tax returns we will ask for detailed information on each account within the trial balance to really understand what that means for the tax return. So, looking at the mathematical component is only one component of preparing tax returns. And so, it's not -- I don't have enough information to make that determination.

Q: All right. You testified earlier that you have researched reporting methods, including combined unitary reporting, correct?

A: Correct.

Q: And as part of your research and experience, you're also familiar with apportionment methods.

A: Yes.

Q: Okay. Are those concepts related or intertwined?

A: They are intertwined because once you make a determination on the reporting method in the state, it's important to understand how that factors into the apportionment calculations. So, as an example, if you file on a combined unitary basis in a state, when you're preparing the apportionment, often times the apportionment regulations in the state will specifically say that you're -- the computation of the apportionment factor is -- it's -- is dependent upon how you're reporting income from a -- from the tax base standpoint. So, how do you calculate income? What's included in the sales revenue in the state, what's included in property, what's included in payroll. So, oftentimes, there's a direct correlation between how you compute an apportionment factor for a company, compared to how that company is filing in that state ---

Q: Okay.

A: --- from a reporting standpoint.

Q: Going back to some of the, the information that you've reviewed in this case, did you review the taxpayer's 10-Ks?

A: Yes.

Q: Okay. Why did you review the 10-Ks?

A: I reviewed it to get an understanding of the taxpayer's business. Often times, a 10-K will provide a pretty solid amount of information on the company, what it does, the various subsidiaries, how it generates revenue. It allows me to get a really good understanding of the taxpayer's business that I sometimes cannot get just by reviewing the tax returns.

Q: And after reviewing the 10-Ks, what did you observe is the taxpayer's business activity in South Carolina?

A: So, the taxpayer operates, I think, it's 42 retail stores in South Carolina.

Q: Okay. And what is your understanding of how

Tractor Supply Company, the group and it's subsidiaries, conduct its business activity across the United States?

A: It's pretty similar on a state-by-state basis. So, the company has retail stores in a number of states across the country and, you know -- so I didn't observe much of a difference in how the -- where the -- the company's operations on a multistate basis outside of the Tractor Supply Texas and Tractor Supply Michigan operations.

Q: Okay. All right. Earlier you testified that your first opinion and, maybe, your sub-opinion relates to the unitary concept or the unitary business. Is unitary -- or unitary business commonly used by accountants in -- or others in your profession?

A: Yes. It's used heavily by tax professionals and accountants, particularly, when we're advising clients on how, how they should be filing on a multistate basis.

Q: All right. And how is that term commonly defined in your profession?

A: So, unitary is commonly defined as -- there are several unitary tests. Some are, what we call objective tests, and that -- an objective test example would be more than 50 percent voting stock ownership. So, that's a clear objective test. There are also what we call subjective tests. There's a concept called unity of use, unity of operations, and then through judicial and policy determinations in various states, there's a fourth test, which we call contribution independency.

Q: All right. So, let's go back and talk about those individually. Let's talk about unity of operations. Can you describe what you mean by that?

A: So, unity of operations typically will include -- so, there's common accounting systems, there's common research and development operations, there's common marketing between the various companies, so when you look at the operational side of a company's business, often times, there are common characteristics of operations amongst various entities within a unitary group.

Q: Okay. And with that backdrop of understanding what unity of operations is, have you reviewed Tractor Supply's documents with that goal in mind, in viewing it in light of unity of operations?

A: Yes.

Q: Okay. And what did you find?

A: So, I found that, first of all, there's a heavy reliance on unity of operations amongst the various entities. And an example of that would be administrative and management functions. So, you know, the current situa- -- under the facts, Tractor Supply Corporation the parent, is providing significant amount of back of- -- back -- significant amount of operations to the various Tractor Supply subsidiaries. And that includes accounting, it includes marketing, it includes back office support, payroll, etcetera.

Q: Okay. And why are those services important from an accountant's perspective.

A: They're important because when I'm making a determination around unitary filings, that factors heavily in whether or not I think the company meets the unity of operations test. It's also important to understand from a reporting standpoint, in terms of how intercompany transactions are booked, where revenue is being reported, etcetera.

Q: All right. You also described something called unity of use. And can you describe to the Court what you mean by that?

A: Yeah. So, unity of use is typically around the concept called centralized management. So, when you look at executives of the company, when you look at board of directors, there's generally a common -- there's, there's a common theme amongst various entities that are part of the unitary group. So, an example of that would be a situation where an executive of one company is an executive of another company and that executive is making decisions, whether it's operational or investment decisions, on behalf of various companies within the group.

Q: Okay. And again, turning back to the facts of this case, did you find any of those factors or facts present in your review of the documents?

A: Yes. In particular, the review of the intercompany agreements.

Q: Okay. And can you describe what you found and observed?

A: So, what I observed was that executives of Tractor Supply Cooperation the parent, were also officers or executives of Tractor Supply Texas and Tractor Supply Michigan.

Q: All right. You also discussed a contribution of dependency test. Can you describe for the Court what you mean by that?

A: Yeah. So, typically, contribution and dependency test is that there's a significant amount of dependency amongst various entities of a unitary group. So, an example of that would be, when one company is relying heavily on services that are provided by other company, or alternatively, when one company is generating a significant amount of revenue through related party transactions. So, when there's a, when there's a significant amount of dependency amongst the various groups in order for those groups to, to operate, that is a sign that a company -- or a group of companies have a strong contribution and dependency upon each other.

Q: Okay. And similar to the other tests that we just talked about, and from your review of Tractor Supply's documents, what did you observe with that particular test, the contribution of dependency?

A: Yeah. So, I observed that there were -- there, there was a significant amount of interdependency amongst the various entities and an example of that would be the procurement function and that -- the fact that Tractor Supply Texas generates a significant amount of income from intercompany transactions with Tractor Supply Company, and it's providing a significant service to Tractor Supply Company.
Q: Do factors related to dependency, profitability or economies of scale, is that a relevant factor or test when discussing unitary concepts?
A: Yeah. You know, I sort of lump that into the contribution and dependency test. But functional integration between companies is a significant part of a unitary determination. And what I mean by that is, when companies are heavily integrated together, when they're relying on each other for services and when there's economies of scale between companies because they're using similar accounting systems, they're using similar payroll systems, that again, points to the fact that under the concept of fundal- -- functional integration

and contributions and dependency that a unitary -- that unitary characteristics exist.

Q: All right. All right. Your second, I guess, sub-opinion is the interdependency and dependency upon the -- the entities in the group. Is there anything that you haven't discussed already related to that specific opinion?

A: I think I've covered it in the, in the functional integration dependency discussion.

Q: I'm going to have you look at something on the screen. And I'll hand you a copy of it as well. It's been identified as Respondent's Exhibit 32.

(Respondent's Exhibit Number 32 was introduced into the record at this time.)

MS. WOOTEN: Would the Court like a copy?

THE COURT: Yeah.

MS. BUCKNER: Thank you.

THE COURT: Just while I look, were these also in the flash drive?

MS. WOOTEN: These are not because they haven't been admitted yet.

THE COURT: Oh, okay.

MS. WOOTEN: Or consented to. At the conclusion of the trial, I plan to provide all of the exhibits that have been admitted during the trial at the end of the trial, once we know which ones have been ---

THE COURT: Okay.

MS. WOOTEN: But these have not been consented to.

THE COURT: All right. I just wanted to know.

Q: All right. Do you recognize the PowerPoint that's displayed?

A: Yes.

Q: Okay. What is the purpose of the PowerPoint?

A: The purpose of the PowerPoint was for me to show, number one, my understanding of the various operations and transactions between the related companies in that group.

Q: Okay. And what information did you use for outlining your opinions in this matter?

A: So, I used the 10-K. I used the intercompany agreements. I used the various memos that were provided, that were prepared by PwC and others. I reviewed the tax returns, the federal tax returns and the state tax returns. And I reviewed the accounting records and the trial balances.

Q: Did you use any information that was not provided to you as part of this litigation?

A: No.

Q: Okay. All right. All right.

MS. WOOTEN: (To Ms. Gamble) If you'll just go to slide two.

Q: All right. If you could describe slide one for the Court, please?

A: Yeah. So, slide one is showing, really the three main Companies that are part of this discussion, Tractor Supply Company, so the parent, Tractor Supply Company of Texas and Tractor Supply Company Michigan, and the arrows pointing both ways are showing that there is a significant amount of interdependency between the various Companies in this group.

Q: All right. So, in your review of the documents, let's go through these one by -- the companies one by one. What did you observe as important functions or services of Tractor Supply Company, the parent?

A: So, Tractor Supply Company, the parent, is the operator of the retail stores on a multistate basis. Tractor Supply Company of -- the parent purchases a significant amount, if not all, of their inventory from Tractor Supply Company of

Texas. Tractor Supply Company the parent leases emplo- -- Michigan -- employees to Tractor Supply Company of Michigan, and then Tractor Supply Company, the parent, provides administrative and management services to both Tractor Supply Company of Texas and Tractor Supply Company of Michigan.

Q: And did you observe for, specifically, for Tractor Supply Company any relation or facts related to the officers within that group?

A: Yes.

Q: I'm sorry, within that entity.

A: In -- for -- in terms of reviewing the intercompany agreements, I noted that there were several -- at least, in terms of the agreements that were provided, that there was common executives between Tractor Supply Company, the parent, Tractor Supply Company of Texas, and Tractor Supply Company of Michigan.

Q: Okay. All right. Let's move to Tractor Supply Company of Michigan. Based on your review of the documents, what did you observe about the functions or services of this particular entity?

A: So, Tractor Supply Company of Michigan operates the Michigan retail stores. Tractor Supply Company of Michigan pays an administrative and management fee to Tractor Supply Company for the back office support and management services. And then, Tractor Supply Company of Michigan leases employees from Tractor Supply Company that are located in Michigan.

Q: Okay. Now, moving to Tractor Supply Texas. Based on your review of the documents, what did you observe were the services or functions provided by the Texas entity?

A: So, Tractor Supply Company of Texas operates the Texas retail stores. It provides a procurement service in purchasing and sale of inventory to Tractor Supply Company of Texas -- oh, sorry, Tractor Supply Company, the parent, as well as Tractor Supply Company of Michigan. It pays an administrative and management fee to Tractor Supply Company, the parent, for back office support. It, it also holds the marketing intangibles for the company, so trademark and trade name. And it operates a distribution center, there's several mixing centers, as well. And it also holds the Tennessee -- I believe it's the storage support team in Tennessee.

Q: And in your review of the documents, did you make any observations with regard to the revenue received by Texas from those intercompany transactions?

A: Yeah. I -- in my review, it appeared that approximately 82 percent of the revenue generated by Texas was from intercompany transactions to the parent and Michigan.

MS. WOOTEN: (To Ms. Gamble) If you'll advance for the next slide.

Q: All right. If you will look at what's been la- -- it's not labeled slide three, but it should be slide three. The prior slide should've been labeled slide two. And looking at slide three, does this information describe the testimony you just gave?

A: Yes.

Q: Okay. All right. So, we've been talking a lot about these entities and their functions. How does the taxpayer organize or assign these functions throughout the group?

A: So ---

Q: Is there a document that the, the taxpayer uses to assign these functions?

A: So, those would typically be intercompany agreements, right. So, the intercompany agreements show which company, you know, sho- -- clearly show that the Texas entity is purchasing and providing the procurement service to the parent. There is the Administrative and Management Service Agreement. There's the -- an agreement showing the lease of -- leasing of employees to Michigan. So, there were several intercompany agreements that clearly showed the delineation between the various Tractor Supply group and function they had for the group.

Q: Okay. And you stated earlier that you had reviewed those agreement, correct?

A: Correct.

Q: Okay. From an accounting perspective, how does the taxpayer document or account for these intercompany transactions in their books and records?

A: Yeah. So, it's typically done through journal entries. So, in reviewing the accounting records and the trial balance, I can clearly see that these transactions were documented through, through journal entries.

Q: And what is a journal entry?
A: A journal entry is typically an entry that you make to record a certain transaction in your financial statements.
Q: Okay. All right.
MS. WOOTEN: (To Ms. Gamble) If you'll advance to the next slide.
THE COURT: Can I ask you a question while you're on the ---
A: Sure.
THE COURT: I'm just looking at that slide. If you could back up to it. And this may be something from ignorance because I'm not an accountant, but why would Michigan be -- need to be in this cabal? Because it seems like from the South Carolina perspective of trying to compute this, it -- you could cull Michigan out. So what are they offering that requires them to be part of he unitary business?
A: So, I think it's two-fold. One, when you're looking at unitary, it's important to look at it from the entire group's perspective. And so, when you look at Michigan, Michigan -- and you look at the unitary factors, like contribution and dependency, unity of use,

etcetera, Michigan is leasing employees from the parent, so there's a clear interdependency in terms of being able to have employees who are operating within the retail store. And then, they're also relying heavily on the parent with respect to management fees and administrative fees and etcetera. So, often times when we're looking at this concept of unitary and trying to determine whether or not a unitary group exists, it's important that we look at all members of the group as opposed to just one specific member ---

THE COURT: Well, I get that.

A: Yeah.

THE COURT: It reflects the unitary business.

A: Sure.

THE COURT: I'm asking from a calculating of the taxes standpoint. So ---

A: Yeah. I think Michigan is definitely a smaller portion of the tax, but it's still, you know, a relevant part of the unitary determination.

THE COURT: Okay. Go ahead.

MS. WOOTEN: All right. (To Ms. Gamble) If you'll advance to the next slide.

Q: All right. If you will look at what's been displayed on slide 3.

Can you describe the information on this particular slide?

A: Yes. So, what this is showing is the intercompany transaction between Michigan and the parent for the leasing of the Michigan employees. So for the parent, TSC, we're showing shared service income. So this is the charge that they are -- this is the amount that they are charging to Michigan for the use of the employees. And then, there's also a payroll expense, which is the actual expense -- the payroll expense for those particular employees. And the difference between the shared service income, in this particular situation, and the payroll expense is generally going to be the markup on those -- the leasing of those employees.

Q: And how is the information on this slide relevant -- or, you know, relevant to your opinion?

A: So, this -- again, this is showing that there's a clear dependency between the parent and Michigan for the leasing of the employees. And it also shows that there's a significant elimination in the consolidated financials for this transaction.

Q: And what do you mean by elimination in the transact- -- in the financials?

A: Yeah. So, when you're preparing financial statements for a combined or consolidated group, or a group of companies, in order to accurately reflect the income of the group, it's important that any intercompany transactions are eliminated so as not to create artificial income from a financial statement standpoint.

Q: All right. The slide we were just reviewing was related to 2014. Did you review the other two years in the audit period?

A: Yes.

Q: Okay.

MS. WOOTEN: (To Ms. Gamble) The next slide, please.

Q: All right. And what did you find for 2015 with regard to the employee leasing?

A: Exact same situation as 2014. There's shared service income, and then there's the intercompany payroll expense. And then, there's an elimination for the transaction in the, in the consolidated trial balance.

MS. WOOTEN: (To Ms. Gamble) And if you'll advance to the next slide.

Q: So, that was '14 and '15. Now, we're looking at '16. What did you find with regard to tax year 2016?

A: Same thing for 2016. There's share service income, there's intercompany payroll expense, and then there's an elimination for the transaction in the consolidated trial balance.

Q: Okay. And you testified earlier that you've reviewed the actual intercompany agreements. Do you recall the signatures on those agreements, generally speaking?

A: Yes.

Q: Okay. Based on your observations, what significance, or any -- does it have any significance to you and your opinion about who signed those -- that particular agreement?

A: It does, because when I'm looking at unitary characteristics one of the things I'm focused on are situations where you have common officers between the company, who are making decisions for the benefit of several companies within the combined group. And I noted that the officers of -- the officers that signed the intercompany agreements were officers of multiple companies within the group.

MS. WOOTEN: (To Ms. Gamble) If you'll advance to the next slide.

Q: All right. And we're -- now, we're going to switch to the second intercompany transaction. Can you describe what is shown on the screen?

A: Yeah. So, this is showing the, the charge for the management and administrative support. So, parent company, TSC Texas is charging te- -- sorry, TSC the parent is charging TSC Texas and TSC Michigan for management and administrative support. So, TSC parent is recognizing income, and then Texas and Michigan are recognizing corresponding expenses for those charges.

Q: And similar to what we discussed with the first intercompany transaction related to leasing of employees, how is the information you just described relevant with respect to transaction two, management and administrative service to your opinion?

A: So, again, I think it shows that there's a significant amount of interdependency between the various companies. In order for Texas and Michigan to operate and to be able to, you know

-- really to operate, they are heavily dependent upon the back support from the parent.

Q: Okay. And the slide we were just discussing, what tax year was that?

A: I believe that was 2014.

Q: Okay. And did you perform a similar analysis for '15 and '16?

A: Yes.

Q: Okay. And what did you observe for those two years?

A: I noted that it was similar to 2014. There was an intercompany company charge, there was revenue recognized by the parent and a corresponding expense recognized by Texas and Michigan. And then, an elimination for that transaction in the consolidated trial balance.

Q: And again, similar to the leasing of employees intercompany agreement, with respect to the shared administrative services, what did you observe with regard to that particular agreement for -- with respect to who signed the agreement?

A: That there were common officers of the various companies that were signing the agreements on behalf of each member of the, of the group that was part of that transaction.

Q: Okay. All right. Now, we're going to flip to intercompany transaction three.

All right. Can you briefly give us your understanding of the procurement transaction, and then explain to us what's on the screen?

A: Yeah. So, my understanding is that Tractor Supply of Texas is purchasing and providing a procurement function for other members of the consolidated group. So, they -- they're purchasing the inventory, they're providing certain services related to procurement that -- there's a sale of the -- of inventory to Tractor Supply Company of -- the parent, and then Tractor Supply Company of Michigan. So that's the procurement function.

Q: Okay. And now, if you could describe the information that is on the screen for intercompany transaction three of the procurement.

A: Yeah. So, this particular slide is showing several things. It's showing cost of sale. So in -- so, it's showing, it's documenting, from a journal entry standpoint, the transactions between Texas and the transactions between the parent and Michigan, and an example of that would be GL account 51600. And that's showing that there are intercompany cost of sales between Texas, parent and Michigan. And then, in the elimination column for that account, it's showing that because these are intercompany transactions on a consolidated basis, there's an elimination of that transaction. It's showing that -- there's also GL account 50300, which is the actual intercompany sales amount between Texas, the parent and Michigan. So, when I look at account 50300, that's showing the amount that Texas is reporting as revenue on intercompany transactions with Michigan and parent, which includes the 9.7 percent markup. And then, there's a corresponding cost of sales amount to offset that as cost of goods sold.

Q: Okay. So, let's back up and do some clarification of -- or explanation for this slide.

There are lines denoted in green and there are lines denoted in yellow, what do those represent?

A: So, the lines denote -- denoted in yellow represent the intercompany transactions. So these are clearly showing how much each company is booking with respect to transactions between related companies. The lines in green are showing actual revenue generated by, either the retail -- generally, by the retail stores, and in the case of the parent company, some additional revenue related to shipping and handling. And then, it's also reporting cost of sales associated with third party retail sales.

Q: And how is the information that you've just described on this ---

MS. WOOTEN: And I'll -- Exhibit 30 -- it's Joint Exhibit 30, it's in the record. It's the trial balance for 2014.

Q: How is that information relevant to our opinion in this case?

A: So, again, I think it's clearly showing that when you look at the amount of intercompany sales between Texas, the parent and Michigan, there is a significant amount of revenue that is being generated by the parent -- oh, sorry, by Texas on these intercompany transactions.

And you can see that clearly in, in line 50300. And then, it's also showing that from a dependency standpoint, because these are intercompany transactions, that they're eliminated in the elimination column.

Q: All right. And did you observe similar facts with regard to Tax Year 2015 and 2016?

A: Yes.

Q: Okay.

MS. WOOTEN: (To Ms. Gamble) If you'll advance to the next slide.

Q: So, this slide is -- the source exhibit is Joint Exhibit 30, but it's a different Bates label because it's a different Excel spreadsheet. And this Excel spreadsheet corresponds to 2015.

Generally -- we don't have to go through all of this again, but how is this -- the information on slide -- this particular slide with reference to 2015, relate to the information you just discussed on 2014 Trial Balance?

A: It's very similar. There may be a couple of other smaller accounts where there's revenue generated, but for the most part, it's exactly

-- pretty much, exactly the same as the 2014 slide.

Q: All right.

MS. WOOTEN: (To Ms. Gamble) And again, if you'll advance to the next slide.

Q: This is the Trial Balance from 2016. It's denoted under a different Excel spreadsheet.

But, again, how -- what did you find with respect to 2016 in comparison to the 2014 and 2015 Trial Balances?

A: Very similar to both 2014 and 2015.

Q: Okay. As part of your tax practice and your background and experience, do you advise companies that have subsidiaries?

A: Yes.

Q: Okay. And how often have you done that?

A: Throughout my 25-year career.

Q: Okay. And do you have an idea of how many companies that you have advised over your 25-year career?

A: Several hundred.

Q: Okay. Is it common for corporate taxpayers -- or your clients, to have subsidiaries?

A: Yes.

Q: Okay. And have you considered the business

structure of Tractor Supply Company?
A: Yes.
Q: And is that something that accountants normally do in their profession?
A: Yes.
Q: Okay. And why would they do that?
A: It's important to understand what each company in a group is doing. One, from a -- from an accounting and financial statement standpoint, but also from a tax standpoint, it's important to understand it with respect to making determinations on how companies should be filing on a multistate basis.
Q: Okay. From an accounting perspective, what did you observe with regard to Tractor Supply's business structure as a retailer?
A: What I observed was that there was the parent, which houses most, if not all, of the retail operations outside of Texas, Michigan, and I think Utah. I, I observed that there were significant intercompany transactions between the various members of the group, that there was a significant amount of functional integration between the groups, common executives, things of that nature. So there's

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Q: And so, after observing and document- -- or reviewing what you just, what you just described, is Tractor Supply -- from your perspective as an accountant, is it a common structure?

A: It's, it's not necessarily a common structure because, from a procurement -- with respect to, with respect to the administrative and management fees, I see that quite often. With respect to the procurement function, it -- you know, I've seen that a few times in my career, but not every retail company has that type of structure.

Q: Okay.

MS. WOOTEN: (To Ms. Gamble) If you'll advance to the slide -- to the next slide.

Q: Okay. The next slide is a ti- -- or a portion of the taxpayer's federal consolidated return from 2014. If you could describe the information on this particular.

A: Yeah. So, so when you're preparing a federal return, there are consolidated schedules that are attached to the back of the return that show the revenue, the income and the expenses of various companies that are included in the consolidated return. So, what this is showing me is, the revenue that is generated by Tractor Supply Company, as well as the expenses. The same for Michigan and the same for Texas. And then, in the consolidated return, again, given that -- from a federal income tax standpoint, you want to ensure that you're not artificially reflecting income or expenses within the group, you're required to eliminate those transactions.

Q: Okay. And how -- and in viewing Tractor Supply's Return, what did you find or conclude with respect to their consolidated return?

A: So, that each company generated -- that each company reported income and expenses on the federal return, but that, in the consolidation of the federal return, the intercompany transactions were eliminated.

Q: Okay. And specifically, with reference to how they book their cost of sales, what did you find?

A: So, again, I noted that any intercompany cost of sales between Texas, Michigan and the parent company were eliminated in that -- in the elimination calculation.

Q: Okay. Do you have any opinion with respect to the amounts of how they book -- or what they booked as -- what Texas booked as its cost of goods sold?

A: Again, I -- that goes back to, sort of, the transfer pricing calculation, which again, I'm not the transfer pricing expert.

Q: Okay. You've testified that you've consulted and advised numerous multistate taxpayers regarding various tax planning opportunities, correct?

A: Correct.

Q: Okay. Have any of those situations involved a client that was currently paying a third party to provide a certain service or function to that client, such as purchasing of inventory?

A: Yes.

Q: Okay. And in that situation, why did the client come to you?

A: Often times it was because they were considering bringing in some or all of the procurement function into their -- into their business. And the same would be for things like back office support, perhaps, they were paying third -- certain third parties to provide that service and they had -- they, they were interested in understanding what it would mean to bring the services in-house.

Q: And how did you guide them through that process of bringing that third party service in-house to a related entity?

A: So, again, I can provide my context in -- from a tax perspective, but often it was, again, sitting down with the company, trying to understand from a legal and operational standpoint what they were trying to accomplish by bringing the procurement services in-house. And then, once we had a better understanding of business purpose, operational purpose, the legal reasons why they were bringing those services in-house, we would advise them in terms of how to structure that to optimize tax benefit.

Q: Okay. So, in the situation we were just talking about, where you had a client -- a multistate client that was -- had a third party provider of procurement services, they decided to come in-house -- bring that in-house, and you've gathered all your information, you understand the business and what their goals are, you've guided them through that process, how did you advise them -- or what did you advise them in how to move that from the third-party function to the in-house function?

A: So, one was, you know -- it -- so one determination is, where within the group do you want to house the procurement function. So, the first thing we would look at is, do we need to create a new entity to house that procurement function, should we continue to do that within a retail company, for example. So, often times there's some determine in terms of where that company sits within the combined group. And then, once we've determined where the company sits, we would advise them on -- operationally, how things should be structured to ensure, for example, that, you know, that a state wouldn't come in and try to challenge that structure. And that would be things like setting up a proper invoicing of goods, making sure that cash is going from one company to another. So, in effect, structuring it very similar to how it was structured with that third party.

Q: All right. Going back -- just, taking one step back. In these tax consulting planning advising roles that you've just discussed, was this primarily done at PwC -- in your role at PwC?
A: Yes.
Q: Okay. All right. Just for the record. Did you work at PwC during the time period that the Taxpayer's Transfer Pricing Report was issued in this case?
A: Yes.
Q: Okay. Did -- were you involved in the Taxpayer's Transfer Pricing Report?
A: No.
Q: And did you had any involvement with Tractor Supply prior to your engagement in this matter?
A: No.
Q: Okay. And you were a member of PwC's State Tax Structuring and Planning Group ---
A: Correct.
Q: --- right? Okay. And you -- as part of that position, you assisted clients with planning or structuring implementation?
A: Yes.
Q: Okay. As part of that process, what kind of

information did you request from the client?

A: So, we would, we would request a significant amount of financial information. If they were a new client, we would ask for tax returns for prior years, to get an understanding of what they're filing. We would ask for a sig- -- we would ask for a significant amount information -- or a better understanding of business purpose. What was -- what were the business reasons that they wanted to implement such a structure? What were some of the legal reasons? What were some of the operational reasons? Those factors were heavily reviewed by us as part of a new structuring project.

Q: Okay. And as part of that process in getting that kind of information, did you send any kind of questionnaires or other document to a taxpayer to obtain that information?

A: Yes. We would often send an information request, which would be broken down into various sections. One included -- one including legal, one including operational, one including business purpose, and then generally, a section around financial information.

Q: All right. And can -- in your experience in those particular situations, can you describe the formatting of that document or that questionnaire -- I'm not sure how PwC would've described it, and the information that would have gone on it, and who provided that information?

A: Yes. So, it was typically a memorandum that was prepared by PwC team that was on the engagement. It was broken out into the various sections, as I mentioned. And that would typically be provided to whoever our point of contact was at the client -- which, often times with large multinational or multistate public companies, it's going to be somebody on the tax side. So we were often dealing with the VP of Tax or the tax director. In some cases, the CFO. In some cases, the controller. It really depended on -- but it was somebody within the company that we would provide that document to.

Q: Okay. And when you go that document back, the comp- -- who provided the information on the company?

A: The company would.

Q: Okay. And why was the company providing that information and not PwC?

A: Because from a legal business-purpose standpoint and operational standpoint, Pw- -- we would not have that information. It's important that we get that information directly from the client.

Q: And why is it important that you get that information from the client versus PwC inputting that information?

A: Because, again, when you're looking at any sort of structure, particularly, a structure where there's going to be some ta- -- where it's going to be structured in a way to optimize tax benefits, you want to ensure that you're able to document legal business-purpose, operational purpose, such that, if a state was to come in and scrutinize the structure you've been able to -- that there's non-tax reasons for setting up the structure.

Q: All right. So going back to your experience in these tax planning opportunities, are you aware of opportunities that involve Texas and limited partnerships?

A: Yes.

Q: Okay. And if you just briefly explain what that particular opportunity is.

A: Yeah. So, at that point in time, there was an opportunity to, essentially, put your op- -- your Texas operations into a Texas limited partnership structure. The benefit being that, a corporate Limited Partner in a Texas limited partnership was not subject to corporate inc- -- not subject to Texas franchise tax on any income generated as a partner in a Texas limited partnership.

So, the common way to structure that was, you would create a corp- -- an out-of-state corporate partner that owned 99 percent of a Texas limited partnership, you'd have a one percent general partner, and the corporate -- the out-of-state corporate partner that owned 99 percent would not be subject to Texas franchise tax on 99 percent of the income that flowed through to it.

Q: Okay. So, that's Texas. Are you aware, in your experience, of any tax planning opportunities with respect to Michigan and the single business tax?

A: Yes. So, at that time, one of the components of the single business tax calculation was that payroll expense was added back to the tax base.

So, if you had a client that operated in Michigan that had a significant amount of payroll expense, they would have to add that back to the tax base and essentially, pay Michigan single business pax on payroll expenses.

So, at that point in time, there was an opportunity to shift your payroll into a leasing company structure such that, the entity that has a significant presence in Michigan would not have a significant amount of payroll expense and would not therefore have to add that back and pay tax on it.

Q: And currently in your practice, do you see these types of tax planning strategies with taxpayers?

A: You don't see them any longer. For one, Texas has chang- -- Texas, in the mid-2000s, changed it's tax to a margin's Tax, that's done on a combined unitary basis. And they -- as part of that, they subjected LPs to Texas' margins tax. So, that was no longer a valid opportunity. And then, Michigan moved to corporate income tax around the same time, and that's also on a combined unitary basis. So, they're -- because a lot of states have moved to combined unitary reporting, you do not see these types of structures implemented any longer.

Q: And why is relevant if a state is -- or if a taxpayer files a combined unitary return -- well, uses combined unitary reporting for tax planning opportunities, why is that relevant?

A: It's relevant because, again, the idea behind a lot of the tax structure opportunities was to, to have intercompany transactions in such a way that a significant amount of income was shielded from separate state income tax by, essentially, moving income out of entities that filed in separate states and, and thereby reducing the separate state benefit. In combined unitary states, most, if not all, combined unitary states require an elimination of intercompany transactions, so you don't get that same benefit in combined unitary states.

Q: All right. And based on your research and observations and experience, what have you observed from an accounting perspective of how Tractor Supply Company, the taxpayer in this case, generates its income?

A: So, 95 percent of its income is generated from retail transactions. And any income generated by Texas and Michigan outside of the retail operations within those Companies, is generally from intercompany transactions.

Q: Okay. So, let's -- that was specific for the taxpayer, Tractor Supply Company. Now, let's look at Tractor Supply Company the group. So, including Michigan and Texas. From the accounting perspective, how does the group earn income?

A: So, Tractor Supply Company the parent earns income from retail sales in their retail stores. Tractor Supply Company of Texas generates income from Texas retail stores, but also from intercompany between the parent and Michigan. Michigan generates income primarily from Michigan retail stores.

Q: Okay. And looking at it from the group's perspective, how much of the income of the group is generated from the retail operations?

A: I believe it's 95 percent ---

Q: Okay.

A: --- plus.

Q: All right. And, lastly, you testified that combined unitary reporting is a reasonable apportionment method. Can you explain from an accounting perspective, why combined unitary reporting is reasonable?

A: It's reasonable because when you have a significant amount of intercompany transactions within a group -- again, going back to the concept that often times one of the benefits of these types of structuring projects was to reduce separate state benefit, and again, when you look at certain unitary characteristics, especially contribution independency, functional integration, where there's a significant amount of integration between companies, combined unitary reporting allows for a true reflection of the income of the group in a particular state without artificially creating tax benefits through intercompany transactions.

Q: Okay. And so, in looking in this case and your background -- understanding your background in combined unitary reporting, what factors -- or facts are present in this case, as it's relevant to combined unitary reporting?

A: So, I think there's several. When you look at the unity of operations test, there are heavy reliance on back office administrative support, as well as management services between the related companies. When we look at the concept of unity of use, there's common executives, there's common decision making happening between the various Companies. When you look at unity of ownership, clearly there's more than 50 percent voting stock ownership between the various companies. And then, when you look at the contribution and dependency test, there's a heavy dependency upon vari- -- between the companies in the group and ensuring that they're able to operate at a successful level, and that's clearly an example in the procurement services that are provided between Texas, Michigan and the parent.

Q: Okay. So, we've discussed your three -- your three opinions or, maybe, two opinions with a sub-component, is there anything related to those opinions that we have not discussed as relevant here today?

A: No.

Q: Okay. Thank you. Please, answer any questions Tractor Supply's counsel has.

MS. WOOTEN: Oh, before, Your Honor, at this time the Department would move Respondent's Exhibit 32 into evidence.

(Respondent's Exhibit Number 32 was offered into evidence.)

MR. STREISEL: That's fine. No objection.

THE COURT: It's admitted.

(Respondent's Exhibit Number 32 was admitted into evidence.)

MS. WOOTEN: Thank you.

MS. GEER: Your Honor, would the Court be okay with a short break?

THE COURT: It would be.

MS. GEER: Restroom and coffee break.

(Off the record from 11:09 a.m. until 11:19 a.m.)

THE COURT: Proceed.

MR. STREISEL: May I approach?

THE COURT: Yeah.

MR. STREISEL: All right. I got a few things to carry up here. You ready?

THE COURT: Oh, go ahead. Yeah.

MR. STREISEL: All right.

MR. SEHGAL - CROSS EXAMINATION BY MR. STREISEL:

Q: Hey. How are you doing? Good to get to see you again.

A: You too.

Q: Is Akash all right?
A: Yep.
Q: All right. I guess, the beginning of your testimony, I think you said that you have experience with companies that are similar to Tractor Supply that helps form the basis of your opinions. And are you allowed to give me the names of those companies, or no?
A: I don't think I would be able to share them because a lot of them were at times I was at PwC, and I don't know what their protocol is for sharing that, so.
Q: Okay.
A: I'm happy to share details with you, maybe not -- without naming them.
Q: I guess, how -- are there any companies that specifically come to mind, like just -- like a number, like there's five companies in your head right now, what would that number be?
A: I dealt with a lot of retail companies, so I think that number is probably in the 15 to 20 range.
Q: Okay. And would most of them be filing tax returns and -- or would all of those be filing tax returns in the, majority or all of the 50

states?
A: Yeah. They -- most of them were Fortune 500, Fortune 1,000 retail companies.
Q: Okay.
A: That operate, you know, in all 50 states.
Q: Okay. So, many filed tax returns in South Carolina?
A: South Carolina, absolutely.
Q: All right. Is that true before and after 2010?
A: I think you mean 2012, when I left PwC?
Q: Yeah. Let's talk -- how about that, was it -- what'd -- did you do that after PwC?
A: So, I have clients that operate on a multistate basis, they're not, they're not the size of Fortune 500 or Fortune 1,000 companies, but they still operate in, you know, anywhere from one to 20 states, let's say.
Q: Okay. So, the companies you're thinking of that are similar to Tractor Supply, do they file South Carolina tax returns?
A: Yes.
Q: And you advise them on how to comply with South Carolina law?
A: Yes.
Q: Okay. How many of those have you told to file

a combined unitary return?

A: I don't think I've advised any of them to file combined unitary, primarily, because a lot of the companies I deal with now are not combined unitary groups. They're, they're generally single taxpayers.

Q: I'm talking about the companies that said are similar to Tractor Supply Company that you used to form your opinions that they're a unitary business.

A: Oh, so a lot of those companies would have been companies that I dealt with while I was at PwC, and in many of those years, I think they were years before South Carolina had unitar- -- like, had any alternative apportionment rule or combined unitary -- the general med- -- the *Media General* case, for example. So, I don't believe, you know -- I didn't -- I'm not sure whether combined unitary reporting was an option in South Carolina during the years I was advising them.

Q: Okay. So, you've never advised a company to file a combined unitary return in South Carolina ---

A: Correct.

Q: --- is that accurate?
A: Correct.
Q: Okay. Have you ever advised a company to file a combined unitary return in Georgia?
A: Not that I can think of.
Q: Have you ever advised a company to file a unitary -- combined unitary return in North Carolina?
A: Not off the top of my head.
Q: Okay. Earlier, you were talking unitary business. You said you applied a few tests. What were those tests, again?
A: Unity of operations, unity of ownership, unity of use, and then the contribution and dependency test.
Q: Okay. And are you applying that -- all right, let me back up a second.
Is that what South Carolina law says to apply as a test for a unitary business?
A: I think those factors are factors within the cap- -- the unitary group determination. But they're pretty common unitary tests across all states that have combined reporting.
Q: Okay. But you're not trying to specifically give an opinion on South Carolina law with

respect to unitary business, right?
A: Correct.
Q: Okay. And you said, one opinion is that combined reporting is reasonable. Are you talking about reasonable, as that term is used in the Alternative Apportionment Statute in South Carolina that we've been discussing?
A: Yes.
Q: So, are you giving an opinion that that reasonableness test is met?
A: I'm giving an opinion that when I look at the facts and circumstances of this particular situation, it appears that combined reporting is a reasonable method to file in South Carolina. I don't know that I'm giving it in relation to that particular test.
Q: Okay. So, it's from an accounting perspective ---
A: Correct.
Q: You're not trying to give a legal opinion on it.
A: Correct.
Q: Okay. And you said earlier that -- I think you were talking about interdependency of the group, and you talked about Texas providing

valuable procurement services. Do you recall that testimony?

A: Yes.

Q: And I think you also said combined reporting, it eliminates intercompany transactions.

A: Yes.

Q: Okay. And so, if that's a valuable service, why should Texas be paid nothing for providing that service?

A: I think Texas should be paid to provide that service. I think when you look at it from a combined unitary standpoint, one of the principles is to ensure that it's truly reflecting the income of the combined group. And when you have intercompany transactions you run the risk of, essentially, artificially increasing income through intercompany transactions unless you provide for some sort of elimination to truly reflect the income of the combined group. Because when you think about combined unitary reporting, often times the idea behind it is that, it's a single taxpayer made up of many different entities within the group.

Q: Okay. But you agree that it's a valuable service that, service that should be compensated?

A: Yeah. Again, I'm not making any determination on the actual pricing of it or any of that, but typically, when you have a service that's being provided, you need to ensure that it's at arm's length, right? So, yeah.

Q: I'm just asking whether there is value to the service Texas is providing the parent?

A: Yes.

Q: Okay. So, you talked earlier about the -- the Texas LP benefit that used to exist, and then also the tax benefit in Michigan, right?

A: Yes.

Q: Did you ever recommend structures where either of those were taken advantage of?

A: Certainly, for Texas limited partnership structures. I would say that was probably one, if not the most common structure at that point in time. And for the Michigan, I think I had one or two clients where we recommended something similar.

Q: Okay. So, you've recommended both of those general structures?

A: Sure.

Q: Okay. And you mentioned that PwC would typically give a questionnaire to new clients when, you know, you undertake a restructuring, or evaluate whether to restructure them.

A: Yes.

Q: Okay. And would PwC go forward with the restructure without getting that back?

A: No. You would typically get that back and you would have an opportunity to analyze all the information and -- and make a determination whether to purs- -- to continue with a restructuring plan or to not continue.

Q: Okay. And I think you said that that was, in part, to make sure there was a business purpose for the restructuring?

A: Well, it was to make sure that we had a full understanding of the reasonings for a restructuring, and to ensure that optimizing tax benefits was not the sole reason.

Q: Okay. And then, as long as you were convinced that that was not the sole reason, you know, you -- it was okay to assist the client with the restructuring?

A: Generally, yes.

Q: Is there a time when you assisted the client

with a restructuring when you were not comfortable that there was a business purpose?
A: I can't remember a time, because we were very -- we had very strict policies on ensuring that we had a full understanding of it, and to ensure that the client had a business purpose. Otherwise, we would be putting the firm at risk.
Q: Okay. And so, you wanted to -- you know, didn't want to put the firm at risk for recommending structures that could be challenged for no business purpose, correct?
A: Correct.
Q: Okay. And so, where -- I have your resume. Where -- where are you right now?
A: I'm at Green Hasson Janks, GHJ.
Q: Okay. What's your document retention policy there, how long do you keep documents around?
A: Seven years.
Q: Seven years. Why is that?
A: Seven years is, I believe, it is a standard, and it's something that the AICPA has set as, sort of, a general standard for accounting firms. Often times, we want to ensure that we keep documents, particularly, on the tax side

for any open statute years. So, if, if there's an open statute year with a state or the IRS, we want to ensure we keep those documents. And because, in some cases, the statute may be six years, depending on how a return was reported and how income is reported, we feel seven years is a reasonable time frame.

Q: Okay. So, a general rule of thumb is seven years, and it's based on the possible six-year statute of limitations, absent fraud or something, right?

A: Correct.

Q: Okay. And is it generally the same with state tax issues, as well?

A: Yeah. I mean, we keep seven years for federal and state.

Q: Okay. And do you know whether that was generally the rule -- do you know whether that was also the rule at PwC?

A: I can't remember exactly what the rule was at PwC, but I have to assume that seven years is pretty common in the accounting industry.

Q: Okay. And is there a reason that the -- oh, no, let me back that up.

So, seven years, is -- let me make sure I understand this. The general reason is because absent fraud, the statute of limitations for a tax position would be six years or less, correct?

A: Yeah. It's generally three to four years, depending on the jurisdiction, but if you significantly understate your revenue, both the IRS, as well as states, often will increase the statute period to six years, so seven years seems to encompass both those situations. The general stat -- statute of limitation period, and then the -- the statute of limitation that would apply if there was some sort of fraud or other, other under-reporting of income.

Q: Okay. And when you're talking about statue of limitations, I assume you're talking about the client's tax position versus what you did as the accounting firm?

A: When I'm talking about statute of limitations, I mean the, the time period from which a state has the opportunity to come in and impose ta- -- impose additional tax on a client's particular tax return.

Q: Yeah. And I think you answered the question, but I just wanted to make sure of that. So,

when you assist a client, you are keeping documents, general rule of thumb, seven years, because they -- in case they are needed to support the client's tax position?
A: Correct.
Q: Okay. Earlier, you were talking about how the companies generate revenue. I think you said 95-plus percent is from the retail stores, is that right?
A: Yes.
Q: So that, you were just talking about revenue that comes from sources outside the company.
A: Yes.
Q: All right. One second. Okay. And so, you don't have a law degree, right?
A: Correct.
Q: Okay. And you said earlier, you're not a transfer pricing expert?
A: That's right.
Q: So, you're -- let's see. Yeah. So, you're not giving an opinion on whether the 9.7 percent markup is the right or wrong price?
A: That's correct.
Q: Okay. So, you said a lot of your clients, they are, you know, large -- let me just back that

up.

A lot of your clients have been large retailers, right?

A: Yes.

Q: And most of them has subsidiaries, I assume.

A: Yes.

Q: So, do you agree that there are -- can be benefits to operating through multiple entities versus operating in the single entity?

A: Yes.

Q: What are some common benefits that could exist?

A: So, you know, depending on the industry, you can -- it -- you know, sometimes there's legal reason why you want an operation segregated into separate legal entities. So there's often times legal reasons, operationally, depending on where the, where the companies operate, it may make sense to have separate legal entities. It may make sense from a economies of scale standpoint to have enti- -- separate legal entities set up. So, it really depends on the client's facts and circumstances as to whether, whether it makes sense to have multiple subsidiaries within the group, but generally speaking, there can be benefits to doing that.

Q: Okay. Is one common benefit legal liability protection?
A: Sure.
Q: And I think you mentioned operating efficiencies.
A: Sometimes.
Q: And so, you said you worked with a lot of large retailers, right?
A: Yes.
Q: And do many of them have procurement functions of their own?
A: Some have, some have had procurement functions. Most of the retailers that I've worked with, including the large Fortune 500 companies, did not have separate procurement functions in a -- in separate legal entities, it was all part of the retail function. But they would have things like distribution centers in separate legal entities.
Q: Okay. So, I think you said a lot of them have procurement functions, just not in a separate entity.
A: Yeah. They would procurement functions, but not in separate legal entities. They, they were all part of the same retail function.

Q: Okay. Did you have any clients who had procurement in a separate legal entity?
A: There may have been one -- a couple, one or two.
Q: So, yes?
A: Yes.
Q: And so, for the clients that did not have them in separate entities, I mean, what's a ballpark number of what you're thinking of?
A: I would say 95 percent of the clients, the retail clients that I've dealt with, have not had procurement in a separate legal entity. And I want to say that number is, you know, throughout my career, well over a hundred retail clients that I dealt with.
Q: Okay. And most of that -- well, you -- most of your work was on the west coast, right?
A: Correct.
Q: Okay.
A: But they were na- -- they were national retailers. So, they operated it on a national basis, but most of the -- their headquarters were in western states.
Q: Okay. Do you agree that there can be benefits for housing a procurement function in a

separate legal entity?

A: I think there's -- there can be benefits of having a separate procurement function. I don't know -- you know, outside of opining on a legal ba- -- legal reasons for doing it, which I'm not an attorney, so I don't want to make those determinations, I don't know that there's often times a benefit of having it in a separate legal entity. But I do think there's a benefit of having a separate procurement function.

Q: So, are you saying that you do not think there can be a benefit for having a procurement function in a separate legal entity?

A: I mean, I'm sure they can be, but again, that goes to legal and operation- -- operational reasons for doing it, which I don't think that that's something that I can make a determination on.

Q: Okay. But there can be legal reasons that it could be beneficial to having separate entities?

A: I'm sure, I'm sure there can be.

Q: And there can be operational reasons?

A: Sure.

Q: Okay. And Tractor Supply the parent, they perform administrative services for the group ---
A: Yes.
Q: --- right? And I think you said this already, when you said that that's common for a lot of retailers?
A: Yeah.
Q: And I think you would agree, there's nothing wrong with tax planning, right?
A: No. Tax planning is, is -- I don't have -- yeah. There's -- I don't see anything wrong with tax planning.
Q: I mean, you -- you've done tax planning your entire career, right?
A: Yeah. I wouldn't be in my position if I didn't do tax planning, right? So ---
Q: Okay. And, and -- so you help clients structure themselves in a way to reduce taxes?
A: Yes. Although, that was not the main benefit -- that was not the main reason for doing it.
Q: Okay. So, you're just saying that yes, you help clients structure themselves to save taxes, provided there's some other reason that's not going to make it's disqualified?

A: Yes.
Q: Okay. And, yeah, at PwC -- so 2000 to 2004, you were on the state tax restructuring team?
A: Yes.
Q: Okay. And I think you did that work through 2012, right, there just no formal team?
A: Correct.
Q: And do you recall discussions of east-west structures yesterday?
A: Yes.
Q: And that's a common state corporate income tax planning structure, right?
A: Yes.
Q: Okay. And in your career, have you assisted a client in creating this type of structure?
A: I think there may have been a couple of instances where I've helped clients with an east-west structure. But again, given that most of my clients are on the west coast, there oftentimes was not a -- outside of legal and operational reasons, there wasn't a significant tax benefit of creating those structures, depending on where they would operate and the volume of operations that they would have in some of the east coast states.

Q: Okay. And so, most of your clients have been on the west coast, and has that been true your whole career?
A: I would say the majority of my clients are headquartered on the west coast, and that has been the case for most of my career.
Q: Okay. And so, I guess, there are combined reporting states out there and that's why you're saying there's no benefit in trying to set up that structure out there, is that right?
A: Well, it -- it dep- -- a lot of it depends on where the company operates, but also, what are the big market states for the company -- these companies. A lot of west coast clients, they're biggest market state is California. California is a mandatory combined reporting state. So, there's not often a lot of tax benefit of creating these types of structures when your biggest market state is California. In situations where we have set these up, where I've been involved in these structures, it's because clients have had a significant presence on the east coast.
Q: All right.
A: Or in, in states outside of the wes- -- outside

of the western part of the U.S.
Q: Okay. And so, that's why you set up the structure, because it was worth it based on how a company was operating?
A: Yeah. That was one of the factors you would look at.
Q: And so, you said, at your time at PwC, when you were working with clients on setting up alternative structures, you would try to make sure that there was a business purpose for that structure?
A: Correct.
Q: That was the entire time you were at PwC?
A: Yes.
Q: Okay. Do you remember any times when you were at PwC where you told a client there was no alternative structure that could be supported?
A: Yeah. I'm sure there was several situations where we would review structures, we would review things like business purpose and other operational reasons for setting up a structure, and we'd concluded that there was no -- again, from a tax perspective or an accounting perspective, there was no significant benefit of setting up an alternative structure.

Q: Okay. And so, you turned some people -- did you ever turn clients away because you didn't it was a structure that could be supported if challenged by a taxing authority?

A: Absolutely, we would do that. Yes.

Q: Why would you turn them away?

A: When we say turn them away, we would often times advise them that setting up a certain structure would subject them to scrutiny by a state taxing jurisdiction, and often because that specific state has challenged similar structure in the past.

Q: Okay.

A: So, that would be prob- -- the primary reason. We would also, essentially, turn clients away when we didn't feel like there was any support from a business purpose, legal or operational standpoint for setting up a structure.

Q: Okay. And is that because there was a big risk to the firm if you recommended implementing a structure with no business purpose?

A: Absolutely. Yeah. We had very, very strict policies for that.

Q: Okay. Were these formal policies or just informal policies?

A: Generally, informal, but pretty well understood by everyone on the team.
Q: And do you have any reason to believe other offices would be acting any differently at PwC?
A: No.
Q: Because if other offices are recommending bad structures, it would reflect on your office, right?
A: Correct. And it would reflect on the entire firm in the state tax practice.
Q: Okay. And so, tell me, you know, when you were at PwC, let's -- well, restructuring in this case, correct -- 2001, right?
A: Yes.
Q: And you're aware that PwC helped with that restructuring, correct?
A: Yes.
Q: Okay. And just -- you know, so tell me, you know, your office, what would you do if you were advising a cli- -- or let me back up a second.
Just describe to me the process that your office were undertake to make sure there's a business purpose to a restructuring from your client.

A: Well, as I previously mentioned, we would start off with discussions with the client. So, oftentimes that would include the client's general counsel, the tax group, if needed, the CFO or some other -- the COO of the company, and we would walk through what the company is trying to accomplish from a legal, operational or even a business purpose standpoint. And then once we had sufficient information to feel comfortable that there were non-tax reasons for setting up a structure, we would then look at all of the data and advise on modifications to the structure to ensure that we also optimize tax benefit.

Q: And so, you would talk to business executives and operational people within the company?

A: Yes.

Q: And legal counsel of the company?

A: Yes.

Q: Okay. Do you know Kelly Smith?

A: Yes.

Q: I think -- you know him pretty well, would you say?

A: Pretty well.

Q: And so, he was a partner at the Atlanta office,

right ---
A: Correct.
Q: --- when you were working at PwC?
A: Yes.
Q: And did you do any work with him when you were at PwC?
A: I did work with him. I don't -- I can't remember any structuring projects I did with him, but I did tap into his knowledge about southern states and income tax positions, and filing positions for clients that I had on the west coast.
Q: And so, you and Kelly Smith, you had fairly similar job responsibilities, right?
A: We had similar job responsibilities, although, he was partner and I was a director, so just different titles, but similar experience and job functions.
Q: And -- I mean, you're aware that he assisted Tractor Supply with their restructuring, right?
A: Yes.
Q: So, just, based on what you know about him, would you have expected him to be talking to Tractor Supply's, you know, executives and operational teams to make sure they had a

business purpose, as well?

A: I mean, you know, I can't say in this particular situation what he did, but generally speaking, I would have expected him to have those conversations, yes.

Q: Okay. So, you would surprised if he did not exercise due diligence when he was helping Tractor Supply?

A: I would be surprised.

Q: And with respect to his role in assisting Tractor Supply with their new structure, you're not aware of any reason that his expertise or advise should be questioned, correct?

A: Correct.

Q: So when you were at PwC and assisting clients with restructuring, just like we've been talking about, what kind of documents would you typically generate for the client as part of the process?

A: It was primarily two-fold. One, we would document tax -- the tax implications of a structure in some sort of memorandum. Could be multiple memorandums, depending on the issue and the length and things like that, but there was usually some form of documentation in terms of the tax implications of a structure. And that's typ- -- that was typically in memorandum format. We would also potentially prepare calculations that would show, this is what it means from a tax perspective, this is the tax savings you get from the structure. So, it was a combination of memorandums, as well as calculations.

Q: Okay. And they focused on tax issues, you were saying?

A: It was primarily tax issue driven. We would -- obviously, we're not a law firm so we can't prepare legal documents and things of that nature, and so it's primarily tax driven.

Q: Okay. And so, was it general practice to provide these documents -- or, no. Let me just back up with that.

Was it, was it your general practice to include documents talking about potential challenges in state taxing agencies?

A: Yes.

Q: And so, my understanding is, PwC generally would not be preparing memos explaining the business purposes for the restructuring, is that correct?

A: That is correct.

Q: You generally relied on the client or legal counsel to deal with that?

A: Yes. Because it was not our intention -- it's not our responsibility to make a determination on a client's business purpose, it's really the client's determination to do that.

Q: Okay. And I think you covered this already, but you wouldn't just blindly trust the client if they said, yes, we have a business purpose when you were at PwC, would you?

A: We would do some level of due diligence to ensure that that was the case.

Q: Okay. And is that the due diligence we talked about earlier where you were just saying they talked with executives and operational people?

A: Yes.

Q: Okay. So, is it fair to say that you would not be surprised if there are no memos from PwC that provided detailed explanation of Tractor Supply's business reasons for its restructuring?

A: I would be surprised if those documents were not -- well, I would be surprised if -- sorry. Could -- can you repeat the question, just to

make sure I understand.
Q: Okay. Would you be surprised if there were not PwC documents -- let me back up.
Would you be surprised if there were no memos created by PwC giving detailed descriptions about the business purposes of Tractor Supply's restructuring?
A: I would not be surprised.
Q: Tractor Supply of Michigan does not conduct any business in South Carolina, right?
A: Not that I'm aware of, no.
Q: And Tractor Supply of Texas, they don't conduct any business in South Carolina, right?
A: Correct.
Q: And the parent only -- the parent being Tractor Supply Company, their only business in South Carolina is the retail stores, correct?
A: Correct.
Q: So, South Carolina's Alternative Apportionment Statute 12-6-2320 -- you know what I'm referring to?
A: Yes.
Q: So, you hadn't -- you had not reviewed South Carolina statute before your work on this case, right?

A: Correct.
Q: And you agree that a reporting method and an apportionment method are two different things, right?
A: They're two different calculations -- or two different determinations, but they're oftentimes consistent in terms of, you know, one method or the other. So, if you're filing -- if you make a determination on reporting method, oftentimes the apportionment calculations is done in a similar manner.
Q: But they are two distinct things. The reporting method ---
A: Yes.
Q: --- and the apportionment method?
A: Yes.
Q: Okay. And so, in South Carolina, for example, the standard way for Tractor Supply, in this case, to file its tax returns is separate reporting and then the sales factors, correct?
A: Yes.
Q: So, separate reporting is different than the sales factor, right?
A: Correct.
Q: The sales factor is the apportionment method?

A: Yes.
Q: And then, combined unitary reporting by the Department. So, that is a combined tax return, and then also the sales factor, right?
A: Yes. Done on a combined basis.
Q: Yeah. So, you're just saying that the sales factor and the Department's method includes all of the entities in the numerator and denominator as opposed to just the parent?
A: Correct.
Q: Okay. So, would you agree that the Department's complaint in this case is not about the apportionment method, but is instead about the reporting method?
A: I think -- yeah. I think, the reporting method is the, is the primary focus of the Department.
Q: So ---
A: But, again, they're intertwined. When -- you know, the calculation of the apportionment factor is a function of how you report, in terms of your reporting method.
Q: Right. But the Department is using the sales factor in this case, right, and that's an apportionment method?
A: Yes.

Q: And Tractor Supply is also using the sales factor, right?
A: (No audible response.) (Nods head.)
Q: So, do you agree that ---
COURT REPORTER: I'm going to -- I need a yes or no answer.
Q: --- the Department's ---
THE COURT: Hold on a second.
COURT REPORTER: I just need an answer, a verbal answer. Yes or no.
A: Okay.
THE COURT: Rather than shake your head.
A: Oh, I see. Okay.
Q: So I was just asking, do you agree that the Department's complaint in this case is not about the apportionment method, but is instead about the reporting method?
A: Yes.
Q: Do you believe Tractor Supply would be okay using the Department's apportionment method in a separate return?
A: Yes.
Q: And why is that?
A: So, when you say, using the Department's method, are you referring to the calculation of

the sales factor under a combined unitary method? I'm, I'm not sure I understand the question.

Q: So, we've been talking about how reporting methods are different than apportionment methods, right?

A: Right.

Q: And I'm saying, do you think Tractor Supply would be fine filing a separate tax return and using the Department's apportionment method?

A: The Department's apportionment method meaning, combined unitary calculation of the apportionment factor, or the sales factor?

Q: What's the difference?

A: Well, the sale -- the -- the factor that's being used is sales factor. I don't think anyone is disagreeing in terms of the sales factor is the right factor to use in the, in the calculation. The question is, do you compute the sales factor on a separate reporting basis or a combined reporting basis. I think that's the question here.

Q: I mean -- so I don't, I don't understand that. Let me back up a second. All right.

MR. STREISEL: I'll just take a quick break before wrapping up.

THE COURT: Okay.

(Whispering.)

Q: So, when you were at PwC, what would be an example of a business purpose that you thought was sufficient to go forward with a restructure?

A: So, that would generally include things like economies of scale. So, if a client came to us and said we want to, we want to put a certain function in either a separate legal entity for legal reason, or alternatively, keep it in the same entity but have it as a separate function within that group, and there's non-tax -- there's business reasons for doing it, one, cost savings, the other, efficiencies in operations, maybe a third being, economies of scale, meaning the opportunity to segregate operations or to move operations into an entity to create more efficiency in the structure. Those would typically be good business reason for doing something.

Q: Okay. And do you all of those or just one?

A: I think we need it -- I don't know that we have -- that I would say we needed one or five or six, but I would say that we needed assurance, and we needed to be comfortable that there were non-tax reasons for doing something ---

Q: And we, meaning PwC?

A: Correct.

Q: Okay. And tracking profitability among different corporate functions, was that a business purpose for creating new entities?

A: Sure.

Q: Okay. And I think you said operational benefits, that's another sufficient business purpose?

A: Yes.

Q: And you -- and legal liability protection, is that a common purpose?

A: Yes.

Q: And that's sufficient?

A: Yep.

Q: What if you -- what about, you know, if you're growing or expecting future expansions, is that a reason to create a new structure?

A: Yes.

Q: And that's sufficient?

A: That would often be a sufficient business reason for setting up a new structure.

Q: Okay. And any other reasons you can think of that we haven't already covered?
A: I'm sure there's some others, but, you know, those typically would be the main business purpose reasons.
Q: And we talked a little bit about documentations that PwC would prepare, right?
A: (Nods head.) Yes.
Q: And you said PwC, they would prepare numerous documents as part of this process.
A: Yes.
Q: And, I guess, at times would PwC, you know, include business purpose for the restructuring of the client?
A: We would include documents on business purpose. Typically, the documentation that we would put together would include, not only items prepared by PwC, but memorandums prepared by the company, by the legal team. And the idea was that we would consolidate all of those documents into a binder, which we would then present to the company to make sure we had everything in one repository.
Q: Okay. So, you're saying that sometimes the documents PwC would prepare would include

business reasons that the company had expressed to PwC?

A: We wouldn't necessarily prepare those documents, but we would gather those documents from various others than had prepared that. There may have been some situations where we would document business purpose, but we would then have the company sign off on it by, you know, signing a document that was prepared or something like that. So, there was probably some situations where business purpose was documented by PwC, but for the most part, we would advise the client to provide us with that information in written format.

Q: Okay. But -- so -- but PwC, they would sometimes put their understanding of the client's business reasons for a restructuring in a PwC prepared document?

A: Yes. I can think of a few situations that happened.

Q: Okay. And is there any reason to believe that PwC would do that if they had not already done the due diligence to support their business reasons?

A: No.

Q: Okay. Do you need a business reason to form an LLC?

A: You don't typically need a business purpose to form an LLC. I mean, companies set up LLCs for a variety of different reasons, including tax reasons.

MR. STREISEL: All right. No further questions.

THE COURT: Re-direct?

MS. WOOTEN: Just a few questions, Your Honor.

<u>MR. SEHGAL - RE-DIRECT EXAMINATION BY MS. WOOTEN:</u>

Q: TWC -- or TSC's Counsel asked you some questions about document retention. And he asked you those from the perspective of what would GHG do, and what are PwC's document retention. And as part of your practice of consulting with clients, what advice if any, do you give to your -- to the clients in keeping records of restructuring projects and documentation?

A: Really, our advice would be to keep this documents for -- in, in perpetuity. I mean, we would -- we wouldn't -- I don't know that I can remember a time where we would come in and say, you only need to keep them for a specific period of time, whether it was four years, six years or seven years. Often times, we would tell them, in case of a potential audit or a challenge to the structure down the road, we advise you to keep it for, you know, our period of seven years, you may want to do it for the same. So, I don't know that I have like a specific year amount, but it was, keep it for as long as you can.

Q: Would you advise the client to keep it as long as that structure is in place?

A: Yes.

Q: All right. Counsel also asked you a couple of questions about the activity of Michigan and whether or not there's any acti- -- Michigan activity in South Carolina. What difference, if any, is there between the -- the operation -- the retail operations in Michigan versus the retail operations in South Carolina?

A: I'm not aware of any differences between the retail operations.

Q: Okay.

MS. WOOTEN: One moment, Your Honor. Yeah. Nothing further from the Department.

THE COURT: You may step down.

MR. STREISEL: Could I -- could I ---

THE COURT: Oh, I'm sorry. Did ---

MR. STREISEL: I just ---

THE COURT: --- you have a few? On a new matter raised.

MR. STREISEL: Excuse me?

THE COURT: A new matter.

MS. GEER: (To Mr. Streisel) Not a new matter, but it's on something just raised.

MR. STREISEL: It's on her questions that she just asked.

THE COURT: Yeah.

MR. STREISEL: Not a new matter. Yeah.

THE COURT: Well, her questions had to be opening up a new matter.

MR. STREISEL: Huh?

THE COURT: I'll just hear your questions.

(Laughter.)

MR. STREISEL: Okay.

MR. SEHGAL - RE-CROSS EXAMINATION BY MR. STREISEL:

Q: So, did you say that you advised clients to keep documents an indefinite period of time?

A: Well, I think we would typically advise clients to keep it for the entire time the structure is in place. That could be two years, 20 years, it depends on the client.

Q: When have you ever told a client to keep documents as long as the structure's in place?

A: I can think of probably several situations when I was back at PwC.

Q: Do clients ever ask you how long they should retain documents to support a tax position?

A: I'm sure clients have asked that, but, you know, that was 15, 20 years ago in some cases. I don't remember exactly. But I'm sure clients asked that question, and our advise would be to keep them, you know, as long as the structure was in place.

Q: All right.

MS. GEER: (To Mr. Streisel) Need a copy?

MR. STREISEL: Yeah.

Q: So, are you saying that you do recall clients asking you how long to keep documents to support tax positions?

A: I'm sure clients asked ---

OBJECTION:

MS. WOOTEN: Asked and answered, Your Honor.

MR. STREISEL: What was the answer?

THE COURT: You asked it and he said, yes, to that question.

Q: Okay. Let's see. You were deposed on

September 7th, of 2022, right?
A: Yes.
Q: And that was under oath?
A: Yes.
Q: And did you get a chance to review the transcript?
A: Yes.
Q: Okay.

MR. STREISEL: Your Honor, may I approach the witness with a copy of the transcript?

THE COURT: You may.

MR. STREISEL: This is condensed. Are you okay with that?

MS. WOOTEN: Okay.

MR. STREISEL: All right. Let's see.

Q: Let's look at page 72. So, I'm at line one on page 72, is that where you are?
A: Yeah.
Q: Okay. So, you were asked in line one, I quote, "So throughout your career, 20-something years now, a broad question to start with. In your line of work, do clients ever ask you how long they should retain documents that may be needed to support a tax position that they are taking?" And then, your answer, "I don't know

that I've ever had a client ask me that question. We obviously have document retention policies with the firm, but I'm not aware of a client ever asking me how long they should retain documents."

Did I read that accurately?

A: Yes.

Q: Okay. And that was your sworn testimony, your deposition?

A: Yes.

Q: Okay.

MR. STREISEL: All right. I'm done.

THE COURT: (To Ms. Wooten) On specifically the transcript?

MS. WOOTEN: Sure.

MR. SEGHAL - FURTHER RE-DIRECT EXAMINATION BY MS. WOOTEN:

Q: Mr. Streisel asked you about a question in your deposition and if you'll look at line two, it says, a broad question about how long they should atta- -- retain documents. And your response was, you didn't -- you don't know if you've ever had a client ask me that question. What would your response be had a client asked you that question?

A: My response would be to keep that ---

OBJECTION:

MR. STREISEL: That calls for speculation. Object. Calls for speculation.

THE COURT: I'll overrule that. 'Cause y'all could've asked him about that throughout his questioning.

A: I would advise a client to keep documents for as long as they have the structure in place.

Q: Thank you.

THE COURT: You may step down. And we're going to take a lunch break. 12:09 by my computer. Is that accurate?

MS. GEER: Yes, Your Honor.

THE COURT: Okay.

MS. GEER: Or 10.

MS. WOOTEN: 12:10.

THE COURT: Well then, we'll be back at 1:30, or ---

MS. GEER: That's great.

MS. WOOTEN: That's ---

THE COURT: Okay.

MS. WOOTEN: Thank you.

THE COURT: All right.

(Off the record from 12:10 p.m. to 1:30 p.m.)

THE COURT: Who's next?