

**REPORT OF THE HEARING OFFICER
RE PROPOSED TRUCKING REGULATION**

Bylaw No. 7 of the Multistate Tax Commission requires the hearing officer to submit to the Commission a report which shall contain a synopsis of the hearing proceedings and a detailed recommendation for Commission action. In the case of a hearing held pursuant to Article VII(2) of the Multistate Tax Compact, the recommendation shall include a proposed draft of the regulation which was the subject matter of the hearing.

Pursuant to the above-described requirements, this Report is necessarily divided into three parts. The first part is a synopsis of the public hearing proceedings pertaining to the proposed regulation. The second part is a brief discussion of certain substantive issues addressed by the proposed Regulation. The third part is a detailed recommendation for Commission action by the hearing officer, including a proposed draft of the regulation. A copy of the Commission's resolution and of the proposed Regulation IV.18(f) as originally proposed is attached as Exhibit 1.

I

SYNOPSIS OF PUBLIC HEARING PROCEEDINGS

A. Notices

A Notice of Hearing was mailed to the member states on August 28, 1984 and later published in the Multistate Tax Commission Review, Volume 1984, No. 2 distributed in October, 1984. Another notice was published in the Wall Street Journal on September 14, 1984, and another later distributed to the State Tax Administrators and other potential interested parties. The Notice called for a public hearing on the proposed Trucking Regulation to be held on November 13, 1984 in the 7th Floor Hearing Room of the Colorado Department of Revenue, 1375 Sherman Street, Denver, Colorado beginning at 10:00 A.M. The proposed Trucking Regulation was set forth with the Notice of Hearing. A copy of the Notice is attached as Exhibit 2.

B. Material Submitted for Record

The hearing, in accordance with the Notice, was called to order at 10:02 A.M. on November 13, 1984 by Alan H. Friedman, Assistant General Counsel of the Multistate Tax Commission, who presided as Hearing Officer for the Commission.

There were four persons who registered as being in

attendance, three persons representing certified public accounting firms and one person representing the Colorado Department of Revenue. None of these persons presented any testimony at the hearing.

The written record of these proceedings consists of the proposed MTC Trucking Regulation (Reg. IV.18.(f) Special Rules: Trucking), three written statements submitted concerning the proposed regulation and the problem needed to be addressed by such a regulation, and a transcript of the tape recording of the proceedings. Copies of these written submittals are attached to this report as Exhibits 3, 4, and 5.

The Hearing Officer left the record open for the receipt of additional written and oral presentations, if any person was interested in doing so, until April 1, 1985. No such additional presentation was received before that date.

II

SUBSTANTIVE ISSUES TO BE DECIDED BY THE COMMISSION

A. Nexus Standard

A suggestion was received from the Private Truck Council of America, Inc. that the states should adopt a de minimus nexus standard exempting from taxation of net income those carriers which (1) do not own or rent any real or tangible property, except vehicles, in the state; and (2) do not make any pick-ups or deliveries within the state; and (3) neither travel in excess of 50,000 miles within the state, nor conduct more than twelve round trips into the state during any taxable year, unless such 50,000 miles or the miles incurred in the round-trips represents more than five percent of the total miles traveled in all states.

The Hearing Officer is convinced by the present judicial decisions that no such suggested limitation on the states' power to tax is required by the due process clause of the United States Constitution. See, Complete Auto Transit Co. v. Brady, 430 U.S. 274 (1977); Western Maryland Ry. Co. v. Goodwin, 282 S.E. 2d 240 (W.Va. 1981). While such a standard is not required by law, the suggestion has sufficient merit, when coupled with a "throw-out" rule, to be considered by the states. See IID.2.c. for Hearing Officer's recommendation.

B. Components of Apportionment Formula

The primary issue of concern expressed by state representatives throughout the development of this rule proposal was the treatment of "purchased transportation" in the

property factor. Little input was received from the private sector regarding this issue to support inclusion or exclusion of purchased transportation in the property factor. A reasonable inference to be drawn is that many members of the trucking industry utilize purchased transportation on a regular basis. If such use of property in the state is not included in the taxpayer's property factor, then a taxing disparity arises, leaving those companies using purchased transportation with a tax advantage not shared by those companies that own their own mobile property. It is the Hearing Officer's finding and conclusion that, on balance, the inclusion of purchased transportation will lead to a more equitable and uniform tax treatment of those trucking companies operating in each state adopting the proposed rule. To this end, the Hearing Officer has made certain changes in the rule as originally proposed at Reg. IV.18.f.(ii).A. and IV.18.f.(ii).B.2, 6, and 7 to define certain terms and clarify the effect of including purchased transportation in the property factor.

C. Definition of Mobile Property Mile

In order to clarify the intent of the proposed rule that the numerators of the property and revenue factors be apportioned on a mobile mile basis, irrespective of whether the trailer was loaded or unloaded, proposed Reg. IV.-18.f.(ii).B.3. has been modified to reflect that intent.

D. Recommendations of Private Truck Council of America, Inc.

1. By letter, the Private Truck Council of America, Inc. made the following additional suggestions concerning the proposed rule:

- a. "Utilize the "Revenue Miles" method of apportionment which fairly apportions income and keeps the trucking industry on equal terms with other members of the transportation industry with whom we compete."
- b. "Recognize some of the unique aspects of private carriers that may now be engaged in for-hire transportation operations and address these issues as set forth in this submission."
- c. "Adopt the de minimus nexus standard as set forth in this submission. This standard establishes an objective test which would aid both the taxpayer and governmental body in making the sometimes evasive determination of nexus."

- d. "Abandon the MTC administrative policy of classifying all income as "business" income and conform those definitions with the recent U.S. Supreme Court mandates as set forth in this submission. This would eliminate needless litigation for both the taxpayer and the governmental agency."

2. The Hearing Officer has considered the recommendations of the Private Truck Council of America, Inc., and has concluded as follows:

- a. While there is merit in the revenue miles approach, the mobile property approach is preferable for the purpose of apportioning income of a trucking business.
- b. The recommendation concerning the unique aspects of private carriers is well taken; and the Hearing Officer has sought to take them into account by recommending modifications in the proposed regulation.
- c. The Hearing Officer recognizes the difficulty of complying with the rather inexact nature of the due process nexus standard without the aid of a de minimus standard such as the one recommended by the Private Truck Council. However, the Hearing Officer believes that the level of de minimus activities suggested by the Private Truck Council is too high, and finds the level recommended in the proposed rule reasonable. In addition, in order to prevent the use of a de minimus standard resulting in the insulation from taxation in all states of income which, absent the standard, would be attributable to a particular state, the Hearing Officer recommends that the property, payroll and sales which are attributable to a state in which the de minimus activity takes place be excluded from the denominator of the respective factors of the apportionment formula for all other states adopting the regulation. See specific recommendation contained in part III, infra.
- d. The Hearing Officer recognizes the significance of the decisions in ASARCO and Woolworth; he also recognizes the modifications in those decisions which were effected by Container. Just as the due process standard for nexus is inexact, so is that applied to the business/nonbusiness dis-

inction; and, just as the suggested de minimus rule seeks to establish a workable objective test, so should a similarly workable objective test be sought for the purpose of determining which income should be subjected to apportionment and which to allocation. It appears to the Hearing Officer that the best way to eliminate the problem would be to eliminate the distinction and that, since the vast majority of all trucking income is apportionable, treating all trucking income as apportionable would best accomplish the purposes of simplification, clarity and certainty. Otherwise, those states which adopt the regulation will have to be relied upon by the industry to seek to construe the regulation in a manner which is consistent with the holdings of ASARCO, Woolworth and Container; and it is likely that there will not be unanimity of opinion as to the import of those decisions with respect to any particular fact situation to which the regulation may be applied. However, since in the development of the present rule proposal, this issue was not addressed by the states, the Hearing Officer recommends that no action be taken in this regard in the context of this specific rule. It is also recommended that the Commission review the possible need for amendment to the definition of business and nonbusiness income contained in Reg. IV.1.(a) that may be warranted in light of the ASARCO, Woolworth and Container decisions.

III

RECOMMENDATION OF HEARING OFFICER

A National Governors Association Working Group has begun efforts to develop definitional and substantive provisions concerning various taxes, e.g. motor fuel and ton-mile taxes, concerning the trucking industry. Its charge is to be completed in June of 1986. One alternative would be for the Commission to defer action on the proposed rule until its 1986 Annual Meeting in order to ensure compatibility, at least in definitions, with the recommendations to be produced by the Working Group. Unless the Commission members share a sense of urgency regarding adoption of the proposed rule, the Hearing Officer recommends that action on the proposal be deferred to its 1986 Annual Meeting, with MTC staff being requested to monitor and assist, if invited, the efforts of the Working Group.

If, however, the Commission desires to adopt the proposed rule at its 1985 Annual Meeting, in order to expedite the states' administrative consideration of the proposal, the Hearing Officer recommends that the Commission adopt the proposed Reg. IV.18.(f) in the following form:

Reg. IV.18.(f)(1): In General

With the exception of renumbering where indicated, no change is recommended from the regulation as originally proposed.

Reg. IV.18.(f)(2): Business and Nonbusiness Income

Given the thrust of the Hearing Officer's statement reflected in section II.D. of this Report, no change is recommended.

Reg. IV.18.(f)(3): Apportionment of Business Income

For the reason stated in section II.B. of this report, the following changes are suggested with respect to Reg. IV.18.(f)(3):

Reg. IV.18.(f)(3)(i): No recommended change.

Reg. IV.18.(f)(3)(ii): It is recommended that Reg. IV.18.(f)(3)(ii)A. provide as follows:

(ii) The Property Factor

A. Property Valuation. Owned property shall be valued at its original cost and property rented from others, including purchased transportation, shall be valued at eight (8) times the net annual rental rate in accordance with Article IV.11 and Regulation IV.11. To the extent that the taxpayer's records reflect a separate charge incurred for the use of purchased transportation attributable to the property so used, such separate charge shall be used in calculating the value of rented property. If such a charge is not separated from that attributable to the compensation paid for the operator of the purchased transportation, the total combined charged shall be reduced by 20% to determine that portion of the charge attributable solely to the value of the rented property. Mobile property which is owned by other trucking companies and temporarily used by the taxpayer in its business and for which a per diem or mileage charge is made shall not be included in the property factor as rented property. Mobile property which is owned by the taxpayer and temporarily used by other trucking companies in their business and for which a per diem or mileage charge is made by the taxpayer shall be included in

the property factor of the taxpayer.

Reg. IV.18.(f)(3)(ii)B.1., 4., 5.: No recommended changes.

Reg. IV.18.(f)(3)(ii)B.2.: It is recommended that Reg. IV.18.(f)(3)(ii)B.2. provide as follows:

2. "Mobile property" means all motor vehicles, including trailers, engaged directly in the movement of tangible personal property, other than support vehicles used predominantly in a local capacity. Mobile property shall include purchased transportation.

Reg. IV.18.(f)(3)(ii)B.3.: It is recommended that Reg. IV.18.(f)(3)(ii)B.3. provide as follows:

3. A "mobile property mile" is the movement of a unit of mobile property a distance of one mile whether loaded or unloaded.

Reg. IV.18.(f)(3)(ii)B.6. and 7.: It is recommended that these be renumbered as 8. and 9., with two new definitional paragraphs, numbered 6. and 7., being added to provide as follows:

Reg. IV.18.(f)(3)(ii)B.6. "Purchased transportation" means the taxpayer's use of a motor vehicle owned and operated by another for the purpose of transporting tangible personal property for which a charge, whether based upon a per diem, mileage, or other basis is incurred by the taxpayer.

Reg. IV.18.(f)(3)(ii)B.7. "Temporarily used" means the use of any mobile property owned by another for a period not to exceed a total of 30 days during any income year.

Reg. IV.18.(f)(5): It is recommended that Reg. 18.(f)(5) be added to provide as follows:

(5) De Minimis Nexus Standard.

(i) General.

Notwithstanding any provision contained herein, this Regulation IV.18.(f) shall not apply to require the apportionment of income to this state if the trucking company during the course of the income tax year neither:

a. owns nor rents any real or

personal property in this state, except mobile property; nor

b. makes any pick-ups or deliveries within this state; nor

c. travels more than twenty-five thousand mobile property miles within this state; provided that the total mobile property miles travelled within this state during the income tax year does not exceed three percent of the total mobile property miles travelled in all states by the trucking company during that period; nor

d. makes more than twelve trips into this state.

(ii) Exclusions: "Throwout Rule"

If a trucking company is not subject to a net income tax, a franchise tax measured by net income, a franchise tax for the privilege of doing business or a corporate stock tax in one or more other states because its business activities in the other states are not sufficient to create a taxable nexus therein for whatever reason, the denominators of the property, payroll and sales (receipts) factors referred to in Reg. IV.18.(f)(3) for this state shall not include the value of any of those activities which are attributable to said other states.

A copy of the proposed rule containing all of the modifications suggested by the Hearing Officer is attached as Exhibit 6.

Respectfully submitted this 25th day of May, 1985.

Alan H. Friedman
Hearing Officer

EXHIBIT 1

MULTISTATE TAX COMMISSION
RESOLUTION REGARDING HOLDING
OF PUBLIC HEARING ON PROPOSED
TRUCKING REGULATION

WHEREAS, the Multistate Tax Commission (hereafter "Commission") possesses the authority pursuant to Article VII, paragraph 1 of the Multistate Tax Compact (hereafter "Compact") to adopt recommendations for uniform regulations for any phase of the administration of, among other things, the income tax laws of the party States to the Commission; and

WHEREAS, the Uniformity Committee of the Commission has met on several occasions to develop and propose a recommendation for regulation under Article IV of the Compact relating to the allocation and apportionment of income earned by members of the trucking industry; and

WHEREAS, at a meeting of the Uniformity Committee held on April 24 and 25, 1984, that Committee recommended to the Executive Committee that a public hearing be conducted upon said trucking regulation proposal in accordance with paragraph 2, Article VII of the Compact; and

WHEREAS, on June 5, 1984, the Executive Committee, being in agreement with the recommendation of the Uniformity Committee, has recommended that the Commission hold a public hearing upon the proposed trucking regulation pursuant to Article VII of the Compact and the Bylaws of the Commission.

NOW, THEREFORE, BE IT RESOLVED that a public hearing upon said proposed trucking regulation, a copy of which is attached hereto, be held on the 9th day of October, 1984, or at such later date and at such specific time and location as determined by the Hearing Officer; and

BE IT FURTHER RESOLVED that Alan H. Friedman, Deputy Executive Director of the Commission, is hereby designated and appointed to act as Hearing Officer for said public hearing; and that he is directed to submit his report and recommendation to the Commission within a reasonable period of time after the completion of said public hearing.

Upon motion duly made and seconded, this Resolution was adopted by the Commission on the 13th day of July, 1984.

MULTISTATE TAX COMMISSION
PROPOSED TRUCKING REGULATION

Regulation IV.18. (). Special Rules: Trucking Companies.

The following special rules are established with respect to trucking companies:

(1) In General. As used in this regulation, the term "trucking company" means a motor common carrier, a motor contract carrier, or an express carrier which primarily transports tangible personal property of others by motor vehicle for compensation. Where a trucking company has income from sources both within and without this state, the amount of business income from sources within this state shall be determined pursuant to this regulation. In such cases, the first step is to determine what portion of the trucking company's income constitutes "business" income and what portion constitutes "nonbusiness" income under Article IV.1 and Regulation IV.1 thereunder. Nonbusiness income is directly allocable to specific states pursuant to the provisions of Article IV.5 to .8, inclusive. Business income is apportioned among the states in which the business is conducted and pursuant to the property, payroll, and sales apportionment factors set forth in this regulation. The sum of (1) the items of nonbusiness income directly allocated to this state plus (2) the amount of business income attributable to this state constitutes the amount of the taxpayer's entire net income which is subject to tax in this state.

(2) Business and Nonbusiness Income. For definitions, rules, and examples for determining business and nonbusiness income, see Regulation IV.1.

(3) Apportionment of Business Income.

(i) In General. The property factor shall be determined in accordance with Regulation IV.10 to .12, inclusive, the payroll factor in accordance with Regulation IV.13 and .14, and the sales factor in accordance with Regulation IV.15 to .17, inclusive, except as modified by this regulation.

(ii) The Property Factor.

A. Property Valuation. Owned property shall be valued at its original cost and property rented from others, including purchased transportation, shall be valued at eight (8) times the net annual rental rate in accordance with Article IV.11 and Regulation IV.11. Mobile property owned and operated by other trucking companies and temporarily used by the taxpayer in its business and for which a per diem mileage charge is made shall not be included in the property factor as rented property. Mobile property owned and operated by the taxpayer and temporarily used by other trucking companies in their business and for which a per diem or mileage charge is made by the taxpayer shall be included in the property factor of the taxpayer.

B. General Definitions. The following definitions are applicable to the numerator and denominator of the property factor, as well as other apportionment factor descriptions:

1. "Average value" of property means the amount determined by averaging the values at the beginning and end of the income tax year, but the (insert here the title of the appropriate administrative agency) may require the averaging of monthly values during the income year or such averaging as is necessary to reflect properly the average value of the trucking company's property. (See Article IV.12 and Regulation IV.12).

2. "Mobile property" means all motor vehicles, including trailers, engaged directly in the movement of tangible personal property, other than support vehicles which are used predominantly in a local capacity.

3. A "mobile property mile" is the movement of a unit of mobile property a distance of one mile.

4. "Original cost" is deemed to be the basis of the property for federal income tax purposes (prior to any federal income tax adjustments, except for subsequent capital additions, improvements thereto, or partial dispositions); or, if the property has no such basis, the valuation of such property for Interstate Commerce Commission purposes. If the original cost of property is unascertainable under the foregoing valuation standards, the property is included in the property factor at its fair market value as of the date of acquisition by the taxpayer. (Regulation IV.11.(a)).

5. "Property used during the course of the income year" includes property which is available for use in the taxpayer's trade or business during the income year.

6. The "value" of owned real and tangible personal property means its original cost. (See Article IV.11 and Regulation IV.11.(a)).

7. The "value" of rented real and tangible personal property means the product of eight (8) times the net annual rental rate. (See Article IV.11 and Regulation IV.11.(b)).

C. The Denominator and Numerator of the Property Factor.

The denominator of the property factor shall be the average value of all the taxpayer's real and tangible personal property owned or rented and used during the income year. The numerator of the property factor shall be the average value of the taxpayer's real and tangible personal property owned or rented and used in this state during the income year. In the determination of the numerator of the property factor, all property, except mobile property as defined in this regulation, shall be included in the numerator of the property factor in accordance with Article IV.10 to .12 inclusive, and Regulation IV.10 to .12, inclusive.

Mobile property, as defined in this regulation, which is located within and without this state during the income year shall be included in the numerator of the property factor in the ratio which mobile property miles in the state bear to the total mobile property miles.

(iii) The Payroll Factor. The denominator of the payroll factor is the compensation paid everywhere by the taxpayer during the income year for the production of business income. (See Article IV.13 and .14 and Regulation IV.13 and .14) The numerator of the payroll factor is the total compensation paid in this state during the income year by the taxpayer. With respect to all personnel, except those performing services within and without this state, compensation paid to such employees shall be included in the numerator as provided in Article IV.13 and .14 and Regulation IV.13 and .14.

With respect to personnel performing services within and without this state, compensation paid to such employees shall be included in the numerator of the payroll factor in the ratio which their services performed in this state bear to their services performed everywhere based on mobile property miles.

(iv) The Sales (Revenue) Factor

A. In General. All revenue derived from transactions and activities in the regular course of the taxpayer's trade or business which produce business income shall be included in the denominator of the revenue factor. (See Article IV.1 and Regulation IV.1.)

The numerator of the revenue factor is the total revenue of the taxpayer in this state during the income year. The total state revenue of the taxpayer, other than revenue from hauling freight, mail, and express, shall be attributable to this state in accordance with Article IV.15 thru .17 and Regulation IV.15 thru .17.

B. Numerator of the Sales (Revenue) Factor From Freight,

Mail, and Express. The total revenue of the taxpayer attributable to this state during the income year from hauling freight, mail, and express shall be:

1. Intrastate: All receipts from any shipment which both originates and terminates within this state; and,

2. Interstate: That portion of the receipts from movements or shipments passing through, into, or out of this state as determined by the ratio which the mobile property miles traveled by such movements or shipments in this state bear to the total mobile property miles traveled by movements or shipments from points of origin to destination.

(4) Records. The taxpayer shall maintain the records necessary to identify mobile property and to enumerate by state the mobile property miles traveled by such mobile property as those terms are used in this regulation. Such records are subject to review by (insert here the title of the appropriate administrative agency) or its agents.

NOTICE OF PUBLIC HEARING

THE MULTISTATE TAX COMMISSION WILL HOLD A PUBLIC HEARING AT THE COLORADO DEPARTMENT OF REVENUE, 1375 SHERMAN STREET, 7TH FLOOR HEARING ROOM, DENVER, COLORADO, BEGINNING AT 10:00 AM ON NOVEMBER 13, 1984, ON THE FOLLOWING SUBJECT:

Proposed Regulation under Article IV.18. of the Multistate Tax Compact regarding the allocation and apportionment of income earned by trucking companies.

All interested parties are invited to participate in the public hearing. Those requesting to make oral presentations before the hearing officer are required to notify:

Mr. Alan H. Friedman
Assistant General Counsel
Multistate Tax Commission
1790 30th Street, Suite 314
Boulder, Colorado 80301

in writing on or before October 26, 1984. Those desiring to submit written presentations are required to file them on or before November 5, 1984 with Mr. Friedman at the above address. A copy of the Proposed Regulation is available upon request.

MULTISTATE TAX COMMISSION

By: 

Eugene F. Corrigan
Executive Director

Sent Notice of Hearing for Trucking Regulations and a copy of the Proposed Regulations:

1. American Trucking Association
1616 P Street, N.W.
Washington, D.C. 20036
2. Interstate Commerce Commission
12th and Constitution Ave., N.W.
Washington, D.C. 20423
3. U.S. Department of Transportation
400 7th Street, S.W.
Washington, D.C. 20590
4. Household Goods Carriers Bureau
2425 Wilson Blvd.
Arlington, VA 22201
5. Rocky Mountain Motor Tariff
P.O. Box 5746
Denver, CO 80217
(303) 433-6731
6. Middlewest Motor Freight Bureau
215 Volker Blvd.
Kansas City, MO 64112
(816) 931-4333
7. Sammons Trucking
Attn: James O. Bendickson, Controller
P.O. Box 4347
Missoula, Montana 59806
8. National Accounting and Financial Council
1616 P Street, N.W.
Washington, D.C. 20036
(202) 797-5462
9. To TAs of all states
10. Commerce Clearing House, Inc.
4025 W. Peterson Avenue
Chicago, Illinois 60646
11. Prentice-Hall
Englewood Cliffs, NJ 07632

October 13, 1982

Mr. Gene Corrigan
Multi-state Tax Commission
1790 - 30th Street
Suite 314
Boulder, CO 80301

RE: Uniformity Issue involving States X, Y, and Z

Dear Mr. Corrigan:

You may be aware of the dilemma we are facing in trying to get States X, Y and Z to adopt and follow the same rules for this multi-state taxpayer. The two areas in which we are having difficulty are:

1. Non-business income — State X feels they are entitled to 100% of non-business income because we are domiciled in State X. States Y and Z (and several others) feel interest income is business income and should therefore be allocated in the same manner as all other business income. Apparently, the Supreme Court is addressing this issue and perhaps its decision will give some clarification.
2. Property Factor Computation — State X has concluded that purchased transportation (the dollars we pay to our owner/operators for providing equipment and driving services) does not constitute rents and is therefore not includible, on the basis of mileage, in the computation of the property factor. States Y and Z, on the other hand, have both concluded purchased transportation is rent and have recomputed the property factors and adjusted our returns accordingly for the years in question.

I have communicated with [persons representing the Revenue Departments of States X, Y and Z] and have encouraged them to come to the Uniformity Committee meeting this month prepared to discuss these issues. Of course I recognize I really have no control over the agenda of that meeting. But these are uniformity issues and we are finding

Mr. [Name]
Multi-state Tax Commission
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ourselves in a double-taxation situation until the issues are discussed and resolved. Anything you can do to further the "cause" of uniformity would be greatly appreciated.

I have enclosed, for your review, copies of some of the correspondence and documentation which has been exchanged over the last year and a half. If there is anything I can do to assist you or the committee in its deliberations, please feel free to contact me.

Very truly yours,

October 9, 1984

Mr. Alan H. Friedman
Assistant General Counsel
Multistate Tax Commission
1790 30th Street, Suite 314
Boulder, Colorado 80301

Dear Mr. Friedman:

I have a copy of your notice of Public Hearing on a proposed rule on allocation and apportionment of income earned by trucking companies.

"Business Income is apportioned among the states in which the business is conducted and pursuant to the property, payroll and sales apportionment factors set forth in this regulation." Presumably, the ultimate apportionment factor is the average of these three factors. I can not see that the proposed rule makes this explicit. This is mere nit-picking and I only raise the observation in passing. Of more significance:

The numerator of the sales factor from freight, mail and express has two features which cause some concern in my mind:

- it distinguishes intrastate and interstate shipments, and
- it apportions interstate freight revenues on the basis of "mobile property miles" only.

Distinguishing interstate and intrastate freight revenues may give rise to some interesting auditing problems where the taxpayer's books are not designed to make such a segregation. Some serious thought should be given to whether the increased cost of compliance to the State and to the taxpayer will, in fact, produce a more meaningful or more fair and reasonable apportionment. It may well be that no purpose is served by making the distinction.

But most fundamentally, I am concerned with your proposal to apportion freight revenues solely on the basis of mobile property miles. There is a great deal more to earning freight revenues than over the road operations. The formula ignores pick up and delivery operations and terminal operations and apportions such revenue to the state of transit.

- I would anticipate some unintended and inequitable results in the application of this rule, particularly in some of the smaller, but densely populated, Eastern states.
- It equates all carriers of cargo for hire similarly. There are marked differences among them.
- It seems to apportion sales to the State of transit.

Mr. Alan H. Friedman

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I would suggest a formula which segregates freight revenues into two segments. Consider that the freight companies typically account for the costs of local pickups and deliveries, terminal operations and over the road costs separately.

Segment #1, over the road costs divided by the total of all three costs times freight revenues probably should be apportioned on the basis of mobile property miles.

Segment #2, the balance of freight revenues might be apportioned on the basis of the state of consignment of the goods or on some other reasonable basis.

Very truly yours,

James J. Manning, CPA
210 Bentley Avenue
Trenton, N. J. 08619



PRIVATE TRUCK COUNCIL of AMERICA, Inc.

2022 P STREET, N.W., WASHINGTON, D.C. 20036
202/785-4900

Richard D. Henderson, Executive Vice President
Richard P. Schweitzer, Legislative Counsel

ALTER L. WEYMOUTH, President
ITE Transport, Inc. Danvers, MA

UCE R. BIGLAND, Western V.P.
Union '78 Los Angeles, CA

CK MEYERS, Central V.P.
Central Soya Co., Inc. Fort Wayne, IN

WARD SZYMANSKI, Eastern V.P.
Airco Industrial Gases Murray Hill, NJ

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November 2, 1984

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J. PETTIGREW
Dean Foods Co. Huntley, IL

F. RODA
Koppers Co. Pittsburgh, PA

J. SAREFIELD
Borden, Inc. Columbus, OH

SCOTT
Wal-Mart Stores, Inc. Bentonville, AK

J. STEPHENS
Oscar Mayer Foods Corp. Madison, WI

F. SZYMANSKI
Airco Industrial Gases Murray Hill, NJ

A. WILSON
CITGO Petroleum Dallas, TX

Mr. Alan H. Friedman
Assistant General Counsel
Multistate Tax Commission
1790 30th Street, Suite 314
Boulder, Colorado 80301

Dear Mr. Friedman:

Please accept the enclosed statement as the comments of the Private Truck Council of America, Inc., on proposed regulation IV.18 concerning special state taxation rules for trucking companies.

Sincerely,

Richard P. Schweitzer
Legislative Counsel

RPS/dr
Enclosure

SUBMISSION REGARDING THE PROPOSED TRUCKING
REGULATION OF THE MULTISTATE TAX COMMISSION

I. History

From a state taxation standpoint, the trucking industry has been recognized as being a unique type of business wherein normal rules of apportionment of income were recognized as inadequate and inappropriate. Accordingly, most states have adopted statutory or regulatory language which recognizes this fact and adequately addresses fair apportionment. These methods typically utilize one of the following concepts:

1. Revenue miles within and without the state.
2. Ton miles within and without the state.
3. Miles within and without the state.

The trucking industry recognizes and accepts any of the above methods as reflecting a fair apportionment standard.

II. Three Factor Formula For The Trucking Industry

The proposed three factor formula adds needless complexity to the calculation of the apportionment factors. It adds allocation and apportionment machinations to the payroll and property factors which increases the compliance burden of the taxpayer and the audit burden of the auditing governmental agency.

Additionally, there is a real potential that the trucking industry could be placed at a competitive disadvantage with the railroad and air transportation industries with which we compete because they would be subject to the rules previously referenced in this submission.

III. Revenue Miles - The Preferred Method

The trucking industry prefers this method because it fairly apportions income both in terms of fact and perception.

An opponent to this methodology would argue that the revenue miles method does not account for the "dead head" miles which would occur in the state and the state would still be required to maintain the highways, provide police protection, etc.

The response to this argument is that the apportionment formula is used to apportion income and that the income is only earned through the transportation of property for a price. No income or revenue is earned on "dead head" trips. Additionally, the payment of substantial motor fuel and in some cases highway use taxes more than compensates for highway usage, police protection, etc.

The revenue mile method offers ease of administration and fairly apportions the income from both the industry and state perspective.

IV. Private Carriers Conducting For-Hire Transportation Operations

In March, 1978, the Interstate Commerce Commission issued its landmark Toto decision (Toto Purchasing & Supply Co., Inc., 128 M.C.C. 873) which held for the first time that a single entity may engage in both private carriage operations on its own behalf and for-hire operations for unrelated shippers.

As a result of Toto and deregulation of the trucking industry by the I.C.C. generally, three primary options have evolved for corporations that heretofore were not engaged in the business of for-hire operations:

A. Corporate Option

The fleet secures for-hire authority, either common or contract, to serve other shippers while at the same time maintaining unregulated private carrier operations.

B. Subsidiary Dual Option

The fleet establishes a wholly-owned subsidiary and serves the parent company virtually as a private carrier under ICC exemptions, but under common or contract authority, it serves other shippers as a separate business. The ICC requires the maintenance of separate books and records for both segments of the business.

C. Subsidiary Option

The fleet establishes a transportation-only subsidiary. Unlike the second option, however, the subsidiary serves the parent through its common or contract certificate. The difference is that the transportation-only subsidiary is a profit center deriving revenues from the parent, and the separate ICC reporting requirements do not exist.

This proposed regulation does not contemplate some of these situations, accordingly the following is recommended:

- I. If a corporation's normal trade or business is not for-hire transportation, and does secure for-hire authority, either common or contract, such corporation shall not be subject to this regulation. Income derived from these operations shall be classified as "business income".

This would eliminate the need for cumbersome separate accounting requirements.

2. If a corporation has or forms a "Dual Option" subsidiary, for purposes of the revenue mile apportionment formula, there

shall be deemed revenue equal to 75% of the average hauling rate that it has experienced with unrelated third party shippers. This deeming provision is rebuttable by the taxpayer, if the taxpayer can demonstrate that an arms-length charge has occurred

This provision should eliminate the concern that the M.T.C. has expressed with respect to intercompany pricing. The 75% rate is used because the parent typically would provide this subsidiary with the vast majority of the subsidiaries' volume and therefore would be given a more favorable rate even if an arms length contract could be negotiated.

3. If a transportation-only subsidiary serves its parent through its common or contract certificate, such subsidiary shall be subject to this regulation without modification.

V. De Minimus Nexus Standard

In order to conform to the Due Process requirements of the Fourteenth Amendment to the Federal Constitution and to further the goals of the M.T.C. in having de minimus nexus standards in other state income tax areas, the following language is suggested:

The provisions of _____ (insert appropriate income/franchise tax title) shall not be applicable to a carrier which neither owns nor rents real or tangible personal property within this State, except vehicles, which has made no pick-ups or deliveries within this State, and which has traveled less than fifty thousand vehicle miles in this State in the taxable year or to a carrier which neither owns nor rents any real or tangible personal property within this State, except vehicles, and which makes no more than twelve round trips into this State during a taxable year; provided that the mileage traveled under fifty thousand miles or the mileage traveled in such round trips does not represent more than five percent of the total miles annually traveled in all states by such carrier.

This language mirrors the language found in Title 58, Chapter 4, Section 58-151.050. Code of Virginia, as amended.

VI. "Business" v. "Nonbusiness" Income

The Multistate Tax Commission Regulation IV.1 fails to conform to recent U.S. Supreme Court decisions. Therefore, it is imperative that the Proposed Trucking Regulation be modified to conform with the U.S. Supreme Court's concept of business and nonbusiness income as well as the Supreme Court of Missouri (an M.T.C. member state).

Dividends, interest, and capital gains on the sale of securities which are earned from non-unitary business operations should not be apportioned. The United States Supreme Court recently held in ASARCO and in F.W. Woolworth Company v. Taxation and Revenue Department, 458 U.S. 345 (1982), 73 L.Ed.2d 819, 102 S. Ct. 3128 (1982), that interest income, along with dividends and capital gains are only apportionable if a unitary business relationship exists between the out-of-state, income-producing activities and the activities within the state which is attempting to tax such income.

The United States Supreme Court in ASARCO considered Idaho's contention that "intangible income should be considered a part of the unitary business if the intangible property ... is 'acquired, managed or disposed of for purposes relating or contributing to the taxpayer's business.'" 102 S. Ct. at 3114. The state contended that "it is this integration - i.e., between the business use of the intangible asset ... and ASARCO's mining, smelting and refining business - which makes the income part of the unitary business." Id. The Court squarely rejected this argument stating:

This definition of a unitary business would destroy the concept. The business of a corporation requires that it earn money to continue operations and to provide a return on its invested capital. Consequently, all of its operations, including any investment made, in some sense can be said to be "for purposes related to or contributing to the (corporation's) business." When pressed to its logical limit, this conception of the "unitary business" limitation becomes no limitation at all. Id. (emphasis in original).

In Woolworth the Court refused to "trivialize (the) due process limitation (of the unitary business principle) by holding it satisfied if the income in question 'adds to the riches of the corporation ...'" 102 S.Ct. at 3135. The Court stated:

Income, from whatever source, always is a "business advantage" to a corporation. Our cases demand more. In particular, they specify that the proper inquiry looks to "the underlying unity or diversity of business enterprise" not to whether the nondomiciliary parent derives some economic benefit - as it virtually always will - from its ownership of stock in another corporation. Id. (citations omitted).

The unitary business principle was again addressed by the United States Supreme Court in Container Corp. of America v. Franchise Tax Board. 103 S.Ct. 2933 (1983). The Court stated:

(The out-of-state activities of the purported "unitary business" (must) be related in some concrete way to the in-State activities. The functional meaning of this requirement is that there be some sharing or exchange of value not capable of precise identification or measurement - beyond the mere flow of funds arising out

of a passive investment or a distinct business operation - which renders formula apportionment a reasonable method of taxation. 103 S.Ct. at 2940.

The Court in Woolworth emphasized that it is immaterial whether or not income from subsidiaries is commingled with the general funds of the parent corporation and used for general corporate operations. The Court indicated that if significance were placed on the commingling of funds, it would "likewise (subvert) the unitary business limitation," for all income from other corporations "would become part of a unitary business if the test were whether the corporation commingled (income) from other corporations, whether subsidiary or not." 102 S.Ct. at 3135 n.11.

The principle that the determination of apportionable business income is directly linked to the unitary business concept was recently reemphasized in Missouri (an MTC member state) in the case of James v. International Telephone and Telegraph Corp. 654 S.W.2d 865 (Mo. 1983). By regulation, Missouri defines business income subject to apportionment as:

Income of any type or class and from any source is business income if it arises from transactions and activity occurring in the regular course of a trade or business. Accordingly, the critical element in determining whether income is "business income" or "non-business income" is the identification of the transactions and activity which are the elements of a particular trade or business. In general, all transactions and activities of the taxpayer which are dependent upon or contribute to the operations of the taxpayer's economic enterprise as a whole constitute the taxpayer's trade or business and will be transactions and activity arising in the regular course of, and will constitute integral parts of, a trade or business." 645 S.W.2d at 865 (citing 12 C.S.R. 10-2.075(4) (1974)).

Relying on the ASARCO, Woolworth, and Container cases, the Supreme Court of Missouri concluded that income generated from the holding or sale of intangible assets did not constitute a unitary business and, therefore, could not be apportioned. 645 S.W.2d 865.

VII. Summary of Recommendations

- A. Utilize the "Revenue Miles" method of apportionment which fairly apportions income and keeps the trucking industry on equal terms with other members of the transportation industry with whom we compete.
- B. Recognize some of the unique aspects of private carriers that may now be engaged in for-hire transportation operations and address these issues as set forth in this submission.

- C. Adopt the de minimus nexus standard as set forth in this submission. This standard establishes an objective test which would aid both the taxpayer and governmental body in making the sometimes evasive determination of nexus.
- D. Abandon the MTC administrative policy of classifying all income as "business" income and conform those definitions with the recent U.S. Supreme Court mandates as set forth in this submission. This would eliminate needless litigation for both the taxpayer and the governmental agency.

This submission was prepared by Lawrence J. Gilsdorf, Jr., Manager - Multistate Taxation, Amway Corporation (a member company) for the Private Truck Council of America, Inc. and accurately reflects our position with respect to this Proposed Trucking Regulation.

LJG/pla

Revised 5/25/85

MULTISTATE TAX COMMISSION
PROPOSED TRUCKING REGULATION

Regulation IV.18. (f). Special Rules: Trucking Companies.

The following special rules are established with respect to trucking companies:

(1) In General. As used in this regulation, the term "trucking company" means a motor common carrier, a motor contract carrier, or an express carrier which primarily transports tangible personal property of others by motor vehicle for compensation. Where a trucking company has income from sources both within and without this state, the amount of business income from sources within this state shall be determined pursuant to this regulation. In such cases, the first step is to determine what portion of the trucking company's income constitutes "business" income and what portion constitutes "nonbusiness" income under Article IV.1 and Regulation IV.1 thereunder. Nonbusiness income is directly allocable to specific states pursuant to the provisions of Article IV.5 to .8, inclusive. Business income is apportioned among the states in which the business is conducted and pursuant to the property, payroll, and sales apportionment factors set forth in this regulation. The sum of (i) the items of nonbusiness income directly allocated to this state plus (ii) the amount of business income attributable to this state constitutes the amount of the taxpayer's entire net income which is subject to tax in this state.

(2) Business and Nonbusiness Income. For definitions, rules, and examples for determining business and nonbusiness income, see Regulation IV.1.

(3) Apportionment of Business Income.

(i) In General. The property factor shall be determined in accordance with Regulation IV.10 to .12, inclusive, the payroll factor in accordance with Regulation IV.13 and .14, and the sales factor in accordance with Regulation IV.15 to .17, inclusive, except as modified by this regulation.

(ii) The Property Factor.

A. Property Valuation. Owned property shall be valued at its original cost and property rented from others, including purchased transportation, shall be valued at eight (8) times the net annual rental rate in accordance with Article IV.11 and Regulation IV.11. To the extent that the taxpayer's records reflect a separate charge incurred for the use of purchased transportation attributable to the property so used, such separate charge shall be used in calculating the value of rented property. If such a charge is not separated from that attributable to the compensation paid for the operator of the purchased transportation, the total combined charged shall be reduced by 20% to determine that portion of the charge attributable solely to the value of the rented property. Mobile property, other than purchased transportation, which is owned by other trucking companies and temporarily used by the taxpayer in its business and for which a per diem or mileage charge is made shall not be included in the property factor as rented property. Mobile property which is owned by the taxpayer and temporarily used by other trucking companies in their business and for which a per diem or mileage charge is made by the taxpayer shall be included in the property factor of the taxpayer.

B. General Definitions. The following definitions are applicable to the numerator and denominator of the property factor, as well as other apportionment factor descriptions:

1. "Average value" of property means the amount determined by averaging the values at the beginning and end of the income tax year, but the (insert here the title of the appropriate administrative agency) may require the averaging of monthly values during the income year or such averaging as is necessary to reflect properly the average value of the trucking company's property. (See Article IV.12 and Regulation IV.12).

2. "Mobile property" means all motor vehicles, including trailers, engaged directly in the movement of tangible personal property, other than support vehicles used predominantly in a local capacity. Mobile property shall include purchased transportation.

3. A "mobile property mile" is the movement of a unit of mobile property a distance of one mile whether loaded or unloaded.

4. "Original cost" is deemed to be the basis of the property for federal income tax purposes (prior to any federal income tax adjustments, except for subsequent capital additions, improvements thereto, or partial dispositions); or, if the property has no such basis, the valuation of such property for Interstate Commerce Commission purposes. If the original cost of property is unascertainable under the foregoing valuation standards, the property is included in the property factor at its fair market value as of the date of acquisition by the taxpayer. (Regulation IV.11.(a)).

5. "Property used during the course of the income year" includes property which is available for use in the taxpayer's trade or business during the income year.

6. "Purchased transportation" means the taxpayer's use of a motor vehicle owned and operated by another for the purpose of transporting tangible personal property for which a charge, whether based upon a per diem, mileage, or other basis is incurred.

7. "Temporarily used" means the use of any mobile property owned by another for a period not to exceed a total of 30 days during any income year.

8. The "value" of owned real and tangible personal property means its original cost. (See Article IV.11 and Regulation IV.11.(a)).

9. The "value" of rented real and tangible personal property means the product of eight (8) times the net annual rental rate. (See Article IV.11 and Regulation IV.11.(b)).

C. The Denominator and Numerator of the Property Factor.

The denominator of the property factor shall be the average value of all the taxpayer's real and tangible personal property owned or rented and used during the income year. The numerator of the property factor shall be the average value of the taxpayer's real and tangible personal property owned or rented and used in this state during the income year. In the determination of the numerator of the property factor, all property, except mobile property as defined in this regulation, shall be included in the numerator of the property factor in accordance with Article IV.10 to .12 inclusive, and Regulation IV.10 to .12, inclusive.

Mobile property, as defined in this regulation, which is located within and without this state during the income year shall be included in the numerator of the property factor in the ratio which mobile property miles in the state bear to the total mobile property miles.

(iii) The Payroll Factor. The denominator of the payroll factor is the compensation paid everywhere by the taxpayer during the income year for the production of business income. (See Article IV.13 and .14 and Regulation IV.13 and .14) The numerator of the payroll factor is the total compensation paid in this state during the income year by the taxpayer. With respect to all personnel, except those performing services within and without this state, compensation paid to such employees shall be included in the numerator as provided in Article IV.13 and .14 and Regulation IV.13 and .14.

With respect to personnel performing services within and without this state, compensation paid to such employees shall be included in the numerator of the payroll factor in the ratio which their services performed in this state bear to their services performed everywhere based on mobile property miles.

(iv) The Sales (Revenue) Factor

A. In General. All revenue derived from transactions and activities in the regular course of the taxpayer's trade or business which produce business income shall be included in the denominator of the revenue factor. (See Article IV.1 and Regulation IV.1.)

The numerator of the revenue factor is the total revenue of the taxpayer in this state during the income year. The total state revenue of the taxpayer, other than revenue from hauling freight, mail, and express, shall be attributable to this state in accordance with Article IV.15 thru .17 and Regulation IV.15 thru .17.

B. Numerator of the Sales (Revenue) Factor From Freight, Mail, and Express. The total revenue of the taxpayer attributable to this state during the income year from hauling freight, mail, and express shall be:

1. Intrastate: All receipts from any shipment which both originates and terminates within this state; and,

2. Interstate: That portion of the receipts from movements or shipments passing through, into, or out of this state as determined by the ratio which the mobile property miles traveled by such movements or shipments in this state bear to the total mobile property miles traveled by movements or shipments from points of origin to destination.

(4) Records. The taxpayer shall maintain the records necessary to identify mobile property and to enumerate by state the mobile property miles traveled by such mobile property as those terms are used in this regulation. Such records are subject to review by (insert here the title of the appropriate administrative agency) or its agents.

(5) De Minimus Nexus Standard.

(i) General.

Notwithstanding any provision contained herein, this Regulation IV.18.(f) shall not apply to require the apportionment of income to this state if the trucking company during the course of the income tax year neither:

a. owns nor rents any real or personal property in this state, except mobile property; nor

b. makes any pick-ups or deliveries within this state; nor

c. travels more than twenty-five thousand mobile property miles within this state; provided that the total mobile property miles travelled within this state during the income tax year does not exceed three percent of the total mobile property miles travelled in all states by the trucking company during that period; nor

d. makes more than twelve trips into this state.

(ii) Exclusions: "Throwout Rule"

If a trucking company is not subject to a net income tax, a franchise tax measured by net income, a franchise tax for the privilege of doing business or a corporate stock tax in one or more states because its business activities in the other states are not sufficient to create taxable nexus therein for whatever reason, the denominators of the property, payroll and sales (receipts) factors referred to in Reg. IV.18.(f)(3) for this state shall not include the value of any of those activities which are attributable to said other states.

**RESOLUTION REGARDING ADOPTION OF
PROPOSED TRUCKING REGULATION**

WHEREAS, on July 13, 1984, the Multistate Tax Commission (hereafter "Commission") by resolution directed a public hearing be held upon the adoption of proposed rules regarding the apportionment of income derived by trucking companies doing interstate business; and

WHEREAS, on November 13, 1984 said public hearing was held in Denver, Colorado, with Alan H. Friedman, Hearing Officer, presiding; and

WHEREAS, pursuant to Article VII of the Multistate Tax Compact said Hearing Officer has filed his Report dated May 25, 1985, recommending, among other alternatives, that the Commission defer acting upon the adoption of such proposed rules until its 1986 Annual Meeting in order to coordinate more closely with the research and proposals being developed by the National Governors Association Working Group on Truck Taxation; and

WHEREAS, good cause appears for so deferring action on the proposed rules until after such time passes as is necessary to permit coordination with said Task Force; and

WHEREAS, said Task Force is to conclude its work no later than June 30, 1986;

NOW, THEREFORE, BE IT RESOLVED that the Commission defer acting upon the Report of the Hearing Officer until its 1986 Annual Meeting; and

BE IT FURTHER RESOLVED that said Report may be further modified between this date and the date of the 1986 Annual Meeting as may be required by the Hearing Officer.

Adopted this 21st day of June, 1985.

Multistate Tax Commission

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Adopted this _____ day of June, 1985.

Multistate Tax Commission

By: _____

Executive Director