

**Multistate Tax Commission  
Financial Institutions Working Group**

***DRAFT AMENDMENTS***  
**Property Factor -- Financial Institutions**

**July 11, 2011**

*For Discussion Purposes Only*

*New/Revised language highlighted*

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**Section 4. Property Factor.**

(a) **General.** The property factor is a fraction, the numerator of which is the average value of real property and tangible personal property rented to the taxpayer that is located or used within this state during the taxable year, the average value of the taxpayer's real and tangible personal property owned that is located or used within this state during the taxable year, and the average value of the taxpayer's loans and credit card receivables that are located within this state during the taxable year, and the denominator of which is the average value of all such property located or used within and without this state during the taxable year.

(b) **Property included.** The property factor shall include only property the income or expenses of which are included (or would have been included if not fully depreciated or expensed, or depreciated or expensed to a nominal amount) in the computation of the apportionable income base for the taxable year.

**(c) Value of property owned by the taxpayer.**

- (1) The value of real property and tangible personal property owned by the taxpayer is the original cost or other basis of such property for Federal income tax purposes without regard to depletion, depreciation or amortization.
- (2) Loans are valued at their outstanding principal balance, without regard to any reserve for bad debts. If a loan is charged-off in whole or in part for Federal income tax purposes, the portion of the loan charged off is not outstanding. A specifically allocated reserve established pursuant to regulatory or financial accounting guidelines which is treated as charged-off for Federal income tax purposes shall be treated as charged-off for purposes of this section.
- (3) Credit card receivables are valued at their outstanding principal balance, without regard to any reserve for bad debts. If a credit card receivable is charged-off in whole or in part for Federal income tax purposes, the portion of the receivable charged-off is not outstanding.

(d) **Average value of property owned by the taxpayer.** The average value of property owned by the taxpayer is computed on an annual basis by adding the value of the property on the first day of the taxable year and the value on the last day of the taxable year and dividing the sum by

two. If averaging on this basis does not properly reflect average value, the [State Tax Administrator] may require averaging on a more frequent basis. The taxpayer may elect to average on a more frequent basis. When averaging on a more frequent basis is required by the [State Tax Administrator] or is elected by the taxpayer, the same method of valuation must be used consistently by the taxpayer with respect to property within and without this state and on all subsequent returns unless the taxpayer receives prior permission from the [State Tax Administrator] or the [State Tax Administrator] requires a different method of determining average value.

**(e) Average value of real property and tangible personal property rented to the taxpayer.**

- (1) The average value of real property and tangible personal property that the taxpayer has rented from another and which is not treated as property owned by the taxpayer for Federal income tax purposes, shall be determined annually by multiplying the gross rents payable during the taxable year by eight.
- (2) Where the use of the general method described in this subsection results in inaccurate valuations of rented property, any other method which properly reflects the value may be adopted by the [State Tax Administrator] or by the taxpayer when approved in writing by the [State Tax Administrator]. Once approved, such other method of valuation must be used on all subsequent returns unless the taxpayer receives prior approval from the [State Tax Administrator] or the [State Tax Administrator] requires a different method of valuation.

**(f) Location of real property and tangible personal property owned by or rented to the taxpayer.**

- (1) Except as described in paragraph (2) of this subsection, real property and tangible personal property owned by or rented to the taxpayer is considered to be located within this state if it is physically located, situated or used within this state.
- (2) Transportation property is included in the numerator of the property factor to the extent that the property is used in this state. The extent an aircraft will be deemed to be used in this state and the amount of value that is to be included in the numerator of this state's property factor is determined by multiplying the average value of the aircraft by a fraction, the numerator of which is the number of landings of the aircraft in this state and the denominator of which is the total number of landings of the aircraft everywhere. If the extent of the use of any transportation property within this state cannot be determined, then the property will be deemed to be used wholly in the state in which the property has its principal base of operations. A motor vehicle will be deemed to be used wholly in the state in which it is registered.

**(g) Location of loans.**

(1)(A) A loan is considered to be located within this state if it is properly assigned to a regular place of business of the taxpayer within this state.

(B) A loan is properly assigned to the regular place of business with which it has a preponderance of substantive contacts. A loan assigned by the taxpayer to a regular place of business without the state shall be presumed to have been properly assigned if-

~~(i) the taxpayer has assigned, in the regular course of its business, such loan on its records to a regular place of business consistent with Federal or state regulatory requirements;~~

~~(ii) such assignment on its records is based upon substantive contacts of the loan to such regular place of business; and~~

~~(iii) the taxpayer uses the same method said records reflecting assignment for assignment of loans for the filing of all state and local tax returns for which an assignment of loans to a regular place of business is required.~~

(C) The presumption of proper assignment of a loan provided in subparagraph (B) of paragraph (1) of this subsection may be rebutted upon a showing by the [State Tax Administrator], supported by a preponderance of the evidence, that the preponderance of substantive contacts regarding such loan did not occur at the regular place of business to which it was assigned ~~on~~ the by the taxpayer's records. When such presumption has been rebutted, the loan shall then be located within this state if (i) the taxpayer had a regular place of business within this state at the time the loan was made; and (ii) the taxpayer fails to show, by a preponderance of the evidence, that the preponderance of substantive contacts regarding such loan did not occur within this state.

(2) In the case of a loan which is assigned by the taxpayer to a place without this state which is not a regular place of business, it shall be presumed, subject to rebuttal by the taxpayer on a showing supported by the preponderance of evidence, that the preponderance of substantive contacts regarding the loan occurred within this state if, at the time the loan was made the taxpayer's commercial domicile, as defined by subsection (c) of Section 2, was within this state.

(3) To determine the preponderance of substantive contacts relating to loans, loans may be grouped by classes of similar instruments, by customer base, and/or another method (including a method combining instruments and customer bases) that reflects the taxpayer's books and records. For example, loans could be grouped as consumer loans, real property loans and commercial loans. Consumer loans could be further grouped such as into installment loans, credit card receivables, student loans, etc. The method of grouping should be consistent with the method of tracking loans within the taxpayer's own books and records used in the normal

course of business that reasonably reflects the products/services sold as identified by the taxpayer. The taxpayer's loan groupings will be presumed to have been properly determined if the taxpayer applies the groupings consistently from year to year unless there has been a material change of fact with respect to that loan group. If a taxpayer cannot group loans, the preponderance of substantive contacts shall be determined on a loan by loan basis.

**NOTE – INDUSTRY DECIDED TO TACKLE THE ASSIGNMENT OF CENTRALIZED CONSUMER LOANS FIRST AND THEN SUBSEQUENTLY EVALUATE OTHER CATEGORIES THROUGH THIS PRISM. THUS IN REVIEWING THE SOURCING BELOW, WE HAVE ONLY FOCUSED ON THE SOURCING OF CENTRALIZED CONSUMER LOANS FOR NOW.**

(4) To determine the state in which the preponderance of substantive contacts relating to a loan group have occurred, the facts and circumstances regarding the loan group at issue shall be reviewed ~~on a case-by-case basis~~ and consideration shall be equally given ~~to the location of to such activities as the solicitation,~~ ~~i~~Investigation, ~~n~~Negotiation, ~~a~~Approval and ~~a~~Administration (“INAA”) of the loan group.

(A) The state assignment for the equally weighted INAA elements for each loan group should be attributable to the state in which the greater number of INAA elements are assigned.

(B) After (A) above is applied, if there is not a single state with a greater number of assigned INAA elements, then Administration shall be accorded greater weight than the other activities, and the loans shall be included in the property factor numerator of the state in which Administration of the loans occurs.

(C) In determining the assigned state for each of the INAA elements, if more than a de minimus amount of activity occurs in multiple states, then the INAA element at issue will be assigned to the state with the greatest Full-Time Equivalent Employees conducting activities related to that element and those loans.

“Full-Time Equivalent Employees” means the quotient obtained by dividing the total number of hours for which employees were compensated for employment in the element activities by two thousand eighty.

(D) The terms ~~"solicitation"~~, "investigation", "negotiation", "approval" and "administration" are defined as follows:

(A) ~~Solicitation.~~ Solicitation is either active or passive. Active solicitation occurs when an employee of the taxpayer initiates the contact with the customer. Such activity is located at the regular place of business which the taxpayer's employee is regularly connected with or working out of, regardless of where the services of such employee were actually performed. Passive solicitation occurs when the customer initiates the contact with the

~~taxpayer. If the customer's initial contact was not at a regular place of business of the taxpayer, the regular place of business, if any, where the passive solicitation occurred is determined by the facts in each case.~~

~~(iB) Investigation.~~ Investigation is the procedure whereby employees of the taxpayer determine the credit-worthiness of the customer as well as the degree of risk involved in making a particular agreement. Such activity is located at (i.e., assigned to) the regular place of business which the taxpayer's employees are regularly connected with or working out of, regardless of where the services of such employees were actually performed. If computerized investigation is primarily applied to the loan group, then investigation is located at (assigned to) the state where the management overseeing the investigation function for the loan type is located.

~~(iiC) Negotiation.~~ Negotiation is the procedure whereby employees of the taxpayer and its customer determine the terms of the agreement (e.g., the amount, duration, interest rate, frequency of repayment, currency denomination and security required). Such activity is located at the regular place of business which the taxpayer's employees are regularly connected with or working out of, regardless of where the services of such employees were actually performed. For loan groups that have set durations, interest rates and repayment frequency (e.g., standard credit cards), negotiation is located at (assigned to) the state where the taxpayer's office in which management that sets the terms for the type of loan is located.

~~(iiiD) Approval.~~ Approval is the procedure whereby employees or the board of directors of the taxpayer make the final determination whether to enter into the agreement. Such activity is located at the regular place of business which the taxpayer's employees are regularly connected with or working out of, regardless of where the services of such employees were actually performed. If the board of directors makes the final determination, such activity is located at the commercial domicile of the taxpayer. If computerized approval is primarily applied to the loan group, then approval is located at (assigned to) the state where the management that sets the approval criteria/standards for the type of loan is located.

~~(ivE) Administration.~~ Administration is the process of managing the account. This process includes bookkeeping, collecting the payments, corresponding with the customer, reporting to management regarding the status of the agreement and proceeding against the borrower or the security interest if the borrower is in default. Such activity is located at the regular place of business which oversees this activity.

(E) Example: Taxpayer makes credit card loans to consumers in all 50 states. The process by which these cards are solicited is through the mail and the Internet. The management overseeing the credit card investigation function

is located in State B. The management that sets the credit cards terms is located is located in State A, and the management that sets the approval criteria/standards for the credit cards are located in State A. In addition, the administration for the credit cards is located in State A. ~~The process of investigating the credit worthiness of the customer, approving the application for the cards and collecting the payments (i.e., administering) the accounts all takes place utilizing a centralized computer system in State A.~~ The credit card loans will all be assigned to State A.

(F) Example: Customers in State A pick up applications for the loans at their local branches and submit them back to local branches in State A. The management groups that set the approval criteria/standards and that set the loan terms are located in State B. ~~All substantive decisions regarding approval, investigation and~~ The administration of the loans is also performed in State B. The loans are assigned to State B as the preponderance of substantive contacts occurs in State B.

(G) Example: Customers in State A meeting with bank employees at State A branch locations, request credit cards and provide relevant information to the bank employees who enter it into a computer terminal. The computer hardware and software related to credit cards are located in State B. The management groups overseeing the credit card investigation function, the terms and rates for credit cards, and the credit card approval criteria/standards are all located in State C. The credit card administration is all done in State D. The loans in this category will be assigned to State C because investigation, negotiation and approval (INA) are assigned to State C.

(H) Example: Taxpayer issues Big Box Retailer private label credit cards to consumers in all 50 states. These credit cards can only be used to make purchases at Big Box Retailer stores and through its internet subsidiary. The process by which these cards are solicited is through the mail, the Internet and in Big Box Retailer stores. The management overseeing Taxpayer's credit card investigation function is located in State B. Taxpayer's management that sets the credit cards terms is located is located in State A, and its management that sets the approval criteria/standards for the credit cards are located in State A. Taxpayer's administration for the credit cards is located in State B. Since two of the INAA elements are assigned to State A and two are assigned to State B, the Administration element is accorded higher weight than the other INA elements and therefore, the greater INAA elements are in State B and Taxpayer's credit card loans will all be assigned to State B.

(I) Example: Taxpayer acquires a portfolio of mortgage loans from an unrelated party. The portfolio includes loans secured by real property in all 50 states. The investigation and negotiation of the purchase occurred at Taxpayer's mortgage division located in State A. The approval of the purchase occurred at the Board of Director's meeting in State B and the portfolio will be serviced and administered at a processing center located in State C. Because

both Investigation and Negotiation occur in State A, the loans in the purchased portfolio will be assigned to State A.

(h) **Location of credit card receivables.** For purposes of determining the location of credit card receivables, credit card receivables shall be treated as loans and shall be subject to the provisions of subsection (g) of this section.

(i) **Period for which properly assigned loan remains assigned.** A loan that has been properly assigned to a state shall, absent any change of material fact, remain assigned to said state for the length of the original term of the loan. Thereafter, said loan may be properly assigned to another state if said loan has a preponderance of substantive contact to a regular place of business there.

(1) The transfer of a loan or a pool of loans, to/from an entity that is within the same controlled group of corporations as the seller shall not by itself be considered as a material change of fact.

(2) The acquisition of the stock of an entity that owns loans shall not by itself be considered as a material change of fact.

(3) The acquisition of a loan or pool of loans from an entity that is not within the same controlled group of corporations shall be considered a material change of fact with respect to that loan group.

(4) For purposes of this subsection, “controlled group of corporations” means “controlled group of corporations” as defined in Section 1563(a) of the Internal Revenue Code, except that:

(A) “More than 50 percent” shall be substituted for “at least 80 percent” each place it appears in Section 1563(a)(1) of the Internal Revenue Code.

(B) The determination shall be made without regard to subsections (a)(4) and (e)(3)(C) of Section 1563 of the Internal Revenue Code.