MULTISTATE TAX COMMISSION

MEMORANDUM

To: Multistate Tax Commission Uniformity Committee

From: Helen Hecht, General Counsel

Regarding: DRAFT of Minutes – Meeting of July 14, 2016 (By Phone)

Date: July 14, 2016

A meeting of the Uniformity Committee was held by phone on July 14, 2016 for the purpose of considering comments on draft amendments to the General Allocation and Apportionment Regulations – Sections 1 and 17 which were referred by the Executive Committee.

Attendees (those who identified themselves):

Wood Miller, MO DOR (Chair)
Chris Coffman, WA DOR (Vice Chair)
Michael Fatale, MA DOR
Ellen Golden, WV DOR
James Savage, VA DOR
Lenny Collins, NC DOR
Jennifer Hays, KY LRC
Karl Frieden, COST
Alysse McLoughlin, McDermott Will & Emery
Lynn Dender, Bank of America
Scott Fryer, Arkansas
Holly Coon, Alabama
Karen Boucher, FIST Coalition
Rebecca Paulson, U.S. Bank
Phil Horwitz, CO DOR
Matt Seltzer, Reed Smith
Helen Hecht, MTC
Bruce Fort, MTC
Sheldon Laskin, MTC
Nate Nielson, ID DOR
Steve Wynn, ID DOR
Gene Walborn, MT DOR
Lee Baerlocher – MT DOR
Jeff Henderson, OR DOR
Don Jones, OR DOR
Dave Hesford, WA DOR

Holly Coon, AL DOR

Wood Miller, Chair, asked for initial public comment.

Initial Public Comment

Karen Boucher, FIST Coalition – Wanted to clarify that before the UDITPA rewrite, she believes that Section 17 clearly sourced interest and dividend income. Now, the revised language refers to the taxpayer's "market" and refers to particular categories of receipts. So, if it is being asserted that only the identified categories of receipts are to be included, she believes refunds can be claimed in states that have adopted the Sec. 17 language. Also, she noted that under the existing Sec 18 regulations (prior to amendment) – only receipts that could not be sourced were considered excluded.

Wood asked for any changes to draft minutes of July 7, 2016 (as revised and posted on the web page). There were no changes and the minutes were approved without objection.

Wood noted that the committee was down to the treatment of receipts from interest and dividends and to the question of whether the committee would recommend a delay in the adoption of Sec. 1 and 17 regulations, pending the drafting of Sec. 18 regulations.

Wood also asked if staff had any other clarification and Helen Hecht, MTC, noted that there were two emails both containing information (also posted on the agenda for the meeting) addressing these issues (one which included comments from Phil Skinner who could not be on the call).

Committee Discussion

- Nate Nielson, Idaho, expressed concern that there might not be time to vote on the question of whether the committee would recommend delay.
- Chris Coffman, Vice Chair, noted that if the committee agreed to a delay until all Sec. 18 issues might be addressed, it could be years before the regulations could be issued.
- Phil Horwitz, Colorado – agreed with Chris.
- Nate – agreed that the committee should not recommend delay.
- Holly Coon, Alabama – stated that there was a need in a number of states for the market sourcing rules and a delay would be a problem for that reason.
- **Phil H. moved that the committee report to the Executive Committee that there should be no delay in the adoption of regulations for Sec. 17 and Sec. 1 pending the adoption of Sec. 18 regulations. The motion passed. (Y**

means no delay - MF –Y, NC-Y, AR-Y, AL-Y, MO-Y, ID- Y, MT-Y, CO-Y, WA-Y, OR-Y)

Discussion of Interest and Dividends

- Karen made additional comments. In her view, it was the intent of the UDITPA changes that interest from treasury function would be excluded but other interest would not. So, for example, interest on packages of loans that that a taxpayer acquired, rather than made, would need to be included in the receipts factor and sourced.
- Chris stated that he believed the issues of interest and dividends are different and would address each one separately.
- Wood agree that dividends should not be in the apportionment factor.
- Bruce Fort, MTC, noted that if the committee agrees that dividends are not in the receipts factor then it might consider amending the definition of "gross receipts" to clarify this issue.
- Wood commented that this suggestion would go along with Phil Skinner's thoughts (summarized in an email to the committee) and the need to clarify the issue. He expressed the view that the regulations do not now explicitly provide the answer. He suggested that the committee might make it part of the report back to the executive committee that more explicit language addressing the issue be included in these regulations.
- Michael Fatale, Massachusetts, asked whether the committee could volunteer that language.
- Wood responded that this was possible and that the language could be drafted by staff and reviewed, or drafted and reviewed by the committee at its upcoming in-person meeting.
- Nate – also agreed that interest and dividends are different. He suggested cleaning up language in the regulations where interest and dividends are mentioned.
- Steve Wynn, Idaho, commented that this is complicated enough that the committee might want to take a closer look at the issue.
- Karen made the comment that the Sec. 18 work group was looking at including interest and dividend receipts in some cases.
- Bruce noted that it might be possible to clarify the treatment of dividends and interest under Sec. 1 as a lead-in to treatment and sourcing under Sec. 18.
- Steve noted that there is also a separate question under Sec. 17, which is whether there is a "market," and it appears this provides an additional reason to exclude the receipts.
- Chris noted that this doesn't mean that dividends are not apportionable, it just means that they are not included in the receipts factor.
- Michael expressed his view that this Sec. 17 issue (which Steve raised) also applies to interest.

- Wood agreed.
- Nate commented that there might be some categories of interest that would be included in the receipts factor.
- Steve gave an example of interest on accounts receivable.
- **Chris made the motion that the committee should state clearly to the Executive Committee that dividend receipts should not be part of the receipts factor. Steve asked that this also be clarified in the regulations. (Chris agreed.) After some discussion, Wood restated the motion: to recommend to the Executive Committee that dividends be treated as excluded from the receipts factor and language be included in these draft regulations to clarify this conclusion (under Sec. 1 or Sec. 17 as appropriate). The motion passed. – (MF-Y, NC-Y, KY-Y, AR-Y, MO-Y, ID-Y, MT-Y, CO-Y, WA-Y, OR-Y, AL-Y)**

- Phil H. stated that it was not clear to him what the UDITPA drafting group's intent was in terms of treating interest. His understanding was that there is not a market for interest in most cases. The only exception is where the interest is finance charges for installment sales. There, the interest is incidental and sourced to the same place as the sale. This seems like the right answer. He believed that Karen raised legitimate points about taxpayers that have only interest income, but that this was an issue to be addressed under Sec. 18. So his conclusion was that interest receipts should be treated the same as dividends.
- Karen asked whether he had the same opinion of a situation where a company buys portfolios of loans.
- Phil H. responded that, yes, those entities should be treated under the financial institution rules. If a state excludes those entities (or doesn't have such rules) then it would be stuck – but it would also have a bigger problem.
- Steve asked whether the conclusion that interest is excluded is based on Sec. 1 or Sec. 17.
- Phil H. responded that he believes it is clearer that interest is excluded under Sec. 1 – a loan of cash. (The treatment of dividends is tougher.) But, in his view, interest is clearly receipts of a taxpayer from a loan. While the language is not 100%, it seems fairly clear.
- Karen stated that the staff memo (from Shirley Sicilian in 2012 to the Executive Committee) only speaks to treasury function receipts.
- Helen reminded the committee that this memo referred to Sec. 1 amendments as originally proposed and prior to the hearing. These amendments included an exception for securities dealers and so, at that time, they were viewed as only affecting treasury function receipts. But later, after the public hearing and in response to the hearing officer's report, the committee had removed the exception for securities dealers so that the exclusion for receipts now applies generally (without any exception).

- Michael noted that another issue where the exclusion might apply is where accounts receivable are transferred – sometimes outside the affiliated group – so that neither Sec. 16 or 17 would clearly provide a way to source those receipts. This, again, is why they fall under Sec. 18.
- Nate and Steve commented that in their view, Sec. 1's language is somewhat ambiguous.
- Michael responded that he was focusing on Sec. 17.
- Steve Wynn agreed that interest might be thrown out under Sec. 17 but wondered whether that should be clarified.
- Wood summarized the discussion to that point, that interest receipts are generally excluded but that it would be useful to add language to the regulations to make this clear.
- Michael noted that a single statement in the regulations, in Sec. 1 or Sec 17 as appropriate, would suffice.
- Alysse McLoughlin, McDermott Will & Emery, noted that even though there is some types of interest receipts that arguably cannot be sourced under Sec. 17, there is a market for other types of interest receipts (for example, where at taxpayer makes and holds onto the loans). Interest receipts will not always be "passive."
- Michael questioned whether, even then, the taxpayer might not have other receipts that are clearly attributable to a market and can provide an basis for apportionment.
- Karen noted that this might mean excluding a substantial amount of receipts from the apportionment factor. She also wondered whether it might not be useful to reach out to those who were involved in the drafting of the UDIPA amendments, including the hearing officer, Professor Pomp, for clarification of the intent of the drafters.
- Michael commented that he was involved in the drafting of UDITPA Sec. 17 and it was clear that the intent of the drafters was to focus on receipts that had a market – and not necessarily to include all of a taxpayer's receipts in the receipts factor. When this creates problems for particular circumstances, it is a Sec. 18 issue.
- **Phil H. made a motion to take the same approach to interest as to dividends—that we recommend to the Executive Committee that interest is excluded under Sec.s 1 and 17 and also that language be included in these regulations (including Sec. 2 and Sec. 15), as appropriate, to clarify this. The motion passed. (MA-Y, NC-y, KY-Y, AL-Y, AR-Y, MO-Y, MT-Y, ID-Y, CO-Y, WA-Y, OR-Y.)**

Wood commented that this would appear to address all the issues referred to the Uniformity Committee. He also noted that staff would draft a written report to the Executive Committee summarizing the work and recommendations of the Uniformity Committee and that that this report will be available prior to the in-person meeting of

the Uniformity Committee (Tuesday, July 26). There it can be discussed and finalized prior to being given to the Executive Committee. He also encouraged members who could to plan on attending or calling into the meeting of the Executive Committee meeting (Thursday, July 28).