

EXHIBIT A

RECOMMENDED APPORTIONMENT FORMULA

EXHIBIT A: 1

**Final Recommended Apportionment Formula
issued pursuant to May 6, 1994 Resolution of the
Multistate Tax Commission Executive Committee**

**[RESERVED FOR EXHIBIT A: 1: FINAL RECOMMENDATION
SUBJECT TO M.T.C. BYLAW VII SURVEY
OF MEMBER STATES]**

EXHIBIT A: 2

**Initial Recommended Apportionment Formula as Attached to Final Report of
Hearing Officer dated April 28, 1994 (superseded by Final Recommended
Apportionment Formula (Exhibit A: 1))**

EXHIBIT A

STATUTORY PROPOSAL FOR APPORTIONMENT AND ALLOCATION OF NET INCOME OF FINANCIAL INSTITUTIONS

Section 1. Apportionment and Allocation.

(a) A financial institution whose business activity is taxable both within and without this state shall allocate and apportion its net income as provided in this Act. All items of nonbusiness income (income which is not includable in the apportionable income tax base) shall be allocated pursuant to the provisions of []. All business income (income which is includable in the apportionable income tax base) shall be apportioned to this state by multiplying such income by the apportionment percentage.

(b) The apportionment percentage is determined by adding the taxpayer's receipts factor (as described in section 3 of this article), property factor (as described in section 4 of this article), and payroll factor (as described in section 5 of this article) together and dividing the sum by three. If one of the factors is missing, the two remaining factors are added and the sum is divided by two. If two of the factors are missing, the remaining factor is the apportionment percentage. A factor is missing if both its numerator and denominator are zero, but it is not missing merely because its numerator is zero.

(c) Each factor shall be computed according to the method of accounting (cash or accrual basis) used by the taxpayer for the taxable year.

(d) If the allocation and apportionment provisions of this Act do not fairly represent the extent of the taxpayer's business activity in this state, the taxpayer may petition for or the [State Tax Administrator] may require, in respect to all or any part of the taxpayer's business activity, if reasonable:

- (1) separate accounting;
- (2) the exclusion of any one or more of the factors,
- (3) the inclusion of one or more additional factors which will fairly represent the taxpayer's business activity in this State; or
- (4) the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

Section 2. Definitions.

As used in this [Act], unless the context otherwise requires:

(a) "**Billing address**" means the location indicated in the books and records of the taxpayer on the first day of the taxable year (or on such later date in the taxable year when the customer relationship began) as the address where any notice, statement and/or bill relating to a customer's account is mailed.

(b) "**Borrower or credit card holder located in this state**" shall mean (1) a borrower, other than a credit card holder, that is engaged in a trade or business which maintains its commercial domicile in this state; and (2) a borrower that is not engaged in a trade or business or a credit card holder whose billing address is in this state.

(c) "**Commercial domicile**" means the headquarters of the trade or business, that is, the place from which the trade or business is principally managed and directed. If a taxpayer is organized under the laws of a foreign country, or of the Commonwealth of Puerto Rico, or any territory or possession of the United States, such taxpayer's commercial domicile shall be deemed to be the state which the taxpayer has declared to be its home state pursuant to the provisions of the International Banking Act of 1978; or, if the taxpayer described in this subdivision has not made such a declaration or is not required to make such a declaration, its commercial domicile for the purposes of this

[ACT] shall be deemed to be the state of the United States or the District of Columbia to which the greatest number of employees are regularly connected or out of which they are working, irrespective of where the services of such employee are performed, as of the last day of the taxable year.

(d) "**Compensation**" means wages, salaries, commissions and any other form of remuneration paid to employees for personal services that are included in such employee's gross income under the Federal Internal Revenue Code. In the case of employees not subject to the Federal Internal Revenue Code, e.g., those employed in foreign countries, the determination of whether such payments would constitute gross income to such employees under the Federal Internal Revenue Code shall be made as though such employees were subject to the Federal Internal Revenue Code.

(e) "**Credit card**" means credit, travel or entertainment card.

(f) "**Credit card issuer's reimbursement fee**" means the fee a taxpayer receives from a merchant's bank because one of the persons to whom the taxpayer has issued a credit card has charged merchandise or services to the credit card.

(g) "**Employee**" means, with respect to a particular taxpayer, any individual who, under the usual common-law rules applicable in determining the employer-employee relationship, has the status of an employee of that taxpayer.

(h) "**Financial institution**" means: [insert state's definition here][for a beginning point for the development of a definition, see Appendix, paragraph A]

(i) "**Gross rents**" means the actual sum of money or other consideration payable for the use or possession of property. "Gross rents" shall include, but not be limited to:

(1) any amount payable for the use or possession of real property or tangible property whether designated as a fixed sum of money or as a percentage of receipts, profits or otherwise,

(2) any amount payable as additional rent or in lieu of rent, such as interest, taxes, insurance, repairs or any other amount required to be paid by the terms of a lease or other arrangement, and

(3) a proportionate part of the cost of any improvement to real property made by or on behalf of the taxpayer which reverts to the owner or lessor upon termination of a lease or other arrangement. The amount to be included in gross rents is the amount of amortization or depreciation allowed in computing the taxable income base for the taxable year. However, where a building is erected on leased land by or on behalf of the taxpayer, the value of the land is determined by multiplying the gross rent by eight and the value of the building is determined in the same manner as if owned by the taxpayer.

(4) The following are not included in the term "gross rents":

(i) reasonable amounts payable as separate charges for water and electric service furnished by the lessor;

(ii) reasonable amounts payable as service charges janitorial services furnished by the lessor;

(iii) reasonable amounts payable for storage, provided such amounts are payable for space not designated and not under the control of the taxpayer; and

(iv) that portion of any rental payment which is applicable to the space subleased from the taxpayer and not used by it.

(j) "**Loan**" means any extension of credit resulting from direct negotiations between the taxpayer and its customer, and/or the purchase, in whole or in part, of such extension of credit from another. Loans include participations, syndications, and leases treated as loans for federal income tax purposes.

Loans shall not include: properties treated as loans under section 595 of the Federal Internal Revenue Code; futures or forward contracts; options; notional principal contracts such as swaps; credit card receivables, including purchased credit card relationships; non-interest bearing balances due from depository institutions; cash items in the process of collection; federal funds sold; securities purchased under agreements to resell; assets held in a trading account; securities; interests in a REMIC, or other mortgage-backed or asset-backed security; and other similar items.

(k) "**Merchant discount**" means the fee (or negotiated discount) charged to a merchant by the taxpayer for the privilege of participating in a program whereby a credit card is accepted in payment for merchandise or services sold to the card holder.

(l) "**Participation**" is an extension of credit in which an undivided ownership interest is held on a *pro rata* basis in a single loan or pool of loans and related collateral. In a loan participation, the credit originator initially makes the loan and then subsequently resells all or a portion of it to other lenders. The participation may or may not be known to the borrower.

(m) "**Person**" shall mean an individual, estate, trust, partnership, corporation and any other business entity.

(n) "**Principal base of operations**" with respect to transportation property means the place of more or less permanent nature from which said property is regularly directed or controlled. With respect to an employee, the "base of operations" means the place of more or less permanent nature from which the employee regularly (1) starts his or her work and to which he or she customarily returns in order to receive instructions from the taxpayer, or (2) communicates with his or her customers or other persons, or (3) performs any

other functions necessary to the exercise of his or her trade or profession at some other point or points.

(o) "**Real property owned**" and "**tangible personal property owned**" means real and tangible personal property, respectively, (1) on which the taxpayer may claim depreciation for federal income tax purposes, or (2) property to which the taxpayer holds legal title and on which no other person may claim depreciation for federal income tax purposes (or could claim depreciation if subject to federal income tax). Real and tangible personal property do not include coin, currency, or property acquired in lieu of or pursuant to a foreclosure.

(p) "**Regular place of business**" means an office at which the taxpayer carries on its business in a regular and systematic manner and which is continuously maintained, occupied and used by employees of the taxpayer.

(q) "**State**" means a state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, any territory or possession of the United States or any foreign country.

(r) "**Syndication**" is an extension of credit in which two or more persons fund and each person is at risk only up to a specified percentage of the total extension of credit or up to a specified dollar amount.

(s) "**Taxable**" means that a taxpayer is subject in another state to a net income tax, a franchise tax measured by net income, a franchise tax for the privilege of doing business, a corporate stock tax (including a bank shares tax), a single business tax, an earned surplus tax, or any other tax which is imposed upon or measured by net income.

(t) "**Transportation property**" means vehicles and vessels capable of moving under their own power, such as aircraft, trains, water vessels and motor vehicles, as well as any equipment or containers attached to such property, such as rolling stock, barges, trailers or the like.

Section 3. Receipts Factor.

(a) **General.** The receipts factor is a fraction, the numerator of which is the receipts of the taxpayer in this state during the taxable year and the denominator of which is the receipts of the taxpayer within and without this state during the taxable year. The method of calculating receipts for purposes of the denominator is the same as the method used in determining receipts for purposes of the numerator.

The receipts factor shall include only those receipts described herein which constitute business income and are included in the computation of the apportionable income base for the taxable year.

(b) **Receipts from the lease of real property.** The numerator of the receipts factor includes receipts from the lease or rental of real property owned by the taxpayer if the property is located within this state or receipts from the sublease of real property if the property is located within this state.

(c) **Receipts from the lease of tangible personal property.**

(1) Except as described in paragraph (2) of this subdivision, the numerator of the receipts factor includes receipts from the lease or rental of tangible personal property owned by the taxpayer if the property is located within this state when it is first placed in service by the lessee.

(2) Receipts from the lease or rental of transportation property owned by the taxpayer are included in the numerator of the receipts 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 receipts that is to be included in the numerator of this state's receipts factor is determined by multiplying all the receipts from the lease or rental 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. 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.

(d) **Interest from loans secured by real property.**

(1) The numerator of the receipts factor includes interest and fees or penalties in the nature of interest from loans secured by real property if the property is located within this state. If the property is located within this state and one or more other states, the receipts described in this subdivision are included in the numerator of the receipts factor if more than fifty percent of the fair market value of the real property is located within this state. If more than fifty percent of the fair market value of the real property is not located within any one state, then the receipts described in this subdivision shall be included in the numerator of the receipts factor if the borrower is located in this state.

(2) A loan is secured by real property if, at the time the original loan agreement was made, fifty percent or more of the aggregate value of the collateral was real property.

(3) The determination of whether the real property securing a loan is located within this state shall be made as of the time the original agreement was made and any and all subsequent substitutions of collateral shall be disregarded.

(e) **Interest from loans not secured by real property.** The numerator of the receipts factor includes interest and fees or penalties in the nature of interest from loans not secured by real property if the borrower is located in this state.

(f) **Net gains from the sale of loans.** The numerator of the receipts factor includes net gains from the sale of loans. Net gains from the sale of loans includes income recorded under the coupon stripping rules of section 1286 of the Internal Revenue Code.

(1) The amount of net gains (but not less than zero) from the sale of loans secured by real property included in the numerator is determined by multiplying such net gains by a fraction the numerator of which is the amount included in the numerator of the receipts factor pursuant to subdivision (d) of this section and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans secured by real property.

(2) The amount of net gains (but not less than zero) from the sale of loans not secured by real property included in the numerator is determined by multiplying such net gains by a fraction the numerator of which is the amount included in the numerator of the receipts factor pursuant to subdivision (e) of this section and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans not secured by real property.

(g) **Receipts from credit card receivables.** The numerator of the receipts factor includes interest and fees or penalties in the nature of interest from credit card receivables and receipts from fees charged to card holders, such as annual fees, if the billing address of the card holder is in this state.

(h) **Net gains from the sale of credit card receivables.** The numerator of the receipts factor includes net gains (but not less than zero) from the sale of credit card receivables multiplied by a fraction, the numerator of which is the amount included in the numerator of the receipts factor pursuant to subdivision (g) of this section and the denominator of which is the taxpayer's total amount of interest and fees or penalties in the nature of interest from credit card receivables and fees charged to card holders.

(i) **Credit card issuer's reimbursement fees.** The numerator of the receipts factor includes all credit card issuer's reimbursement fees multiplied by a fraction, the numerator of which is the amount included in the numerator of the receipts factor pursuant to subdivision (g) of this section and the denominator of which is the taxpayer's total amount of interest and fees or penalties in the nature of interest from credit card receivables and fees charged to card holders.

(j) **Receipts from merchant discount.** The numerator of the receipts factor includes receipts from merchant discount if the commercial domicile of the merchant is in this state. Such receipts shall be computed net of any cardholder charge backs, but shall not be reduced by any interchange transaction fees or by any issuer's reimbursement fees paid to another for charges made by its card holders.

(k) **Loan servicing fees.**

(1) The numerator of the receipts factor includes loan servicing fees derived from loans secured by real property multiplied by a fraction the numerator of which is the amount included in the numerator of the receipts factor pursuant to subdivision (d) of this section and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans secured by real property.

(2) The numerator of the receipts factor includes loan servicing fees derived from loans not secured by real property multiplied by a fraction the numerator of which is the amount included in the numerator of the receipts factor pursuant to subdivision (e) of this section and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans not secured by real property.

In circumstances in which the taxpayer receives loan servicing fees for servicing either the secured or the unsecured loans of another, the numerator of the receipts factor shall include such fees if the borrower is located in this state.

(l) **Receipts from services.** The numerator of the receipts factor includes receipts from services not otherwise apportioned under this section if the service is performed in this state. If the service is performed both within and without this state, the numerator of the receipts factor includes receipts from services not otherwise apportioned under this section, if a greater proportion of the income-producing activity is performed in this state based on cost of performance.

(m) Receipts from investment assets and activities and trading assets and activities.

(1) Interest, dividends, net gains and other income from investment assets and activities and from trading assets and activities shall be included in the receipts factor. Investment assets and activities and trading assets and activities include but are not limited to: investment securities; trading account assets; federal funds; securities purchased and sold under agreements to resell or repurchase; options; future contracts; forward contracts; notional principal contracts such as swaps; equities; and foreign currency transactions. With respect to the investment and trading assets and activities described in subparagraphs (A) and (B) of this paragraph, the receipts factor shall include the amounts described in such subparagraphs.

(A) The receipts factor shall include the amount by which interest from federal funds sold and securities purchased under resale agreements exceeds interest expense on federal funds purchased and securities sold under repurchase agreements.

(B) The receipts factor shall include the amount by which interest, dividends, net gains and other income from trading assets and activities, including but not limited to assets and activities in the matched book, in the arbitrage book, and foreign currency transactions, exceed interest expense from securities sold not yet purchased and net losses from such assets and activities.

(2) The numerator of the receipts factor includes interest, dividends, net gains and other income from investment assets and activities and from trading assets and activities described in paragraph (1) that are attributable to this state.

(A) The amount of interest, dividends, net gains and other income from investment assets and activities in the investment account to be attributed to this state and included in the numerator is determined by multiplying all such income from such assets and activities by a fraction, the numerator of which is the average value of such assets which are properly

assigned to a regular place of business of the taxpayer within this state and the denominator of which is the average value of all such assets.

(B) The amount of interest from federal funds sold and purchased and from securities purchased under resale agreements and securities sold under repurchase agreements attributable to this state and included in the numerator is determined by multiplying the amount described in subparagraph (A) of paragraph (1) from such funds and such securities by a fraction, the numerator of which is the average value of federal funds sold and securities purchased under agreements to resell which are properly assigned to a regular place of business of the taxpayer within this state and the denominator of which is the average value of all such funds and such securities.

(C) The amount of interest, dividends, net gains and other income from trading assets and activities, including but not limited to assets and activities in the matched book, in the arbitrage book and foreign currency transactions, (but excluding amounts described in subparagraphs (A) or (B) of this paragraph), attributable to this state and included in the numerator is determined by multiplying the amount described in subparagraph (B) of paragraph (1) by a fraction, the numerator of which is the average value of such trading assets which are properly assigned to a regular place of business of the taxpayer within this state and the denominator of which is the average value of all such assets.

(D) For purposes of this paragraph, average value shall be determined using the rules for determining the average value of tangible personal property set forth in subdivisions (c) and (d) of section four.

(3) In lieu of using the method set forth in paragraph (2) of this subdivision, the taxpayer may elect, or the [State Tax Administrator] may require in order to fairly represent the business activity of the taxpayer in this state, the use of the method set forth in this paragraph.

(A) The amount of interest, dividends, net gains and other income from investment assets and activities in the investment account to be attributed to this state and included in the numerator is determined by

multiplying all such income from such assets and activities by a fraction, the numerator of which is the gross income from such assets and activities which are properly assigned to a regular place of business of the taxpayer within this state and the denominator of which is the gross income from all such assets and activities.

(B) The amount of interest from federal funds sold and purchased and from securities purchased under resale agreements and securities sold under repurchase agreements attributable to this state and included in the numerator is determined by multiplying the amount described in subparagraph (A) of paragraph (1) from such funds and such securities by a fraction, the numerator of which is the gross income from such funds and such securities which are properly assigned to a regular place of business of the taxpayer within this state and the denominator of which is the gross income from all such funds and such securities.

(C) The amount of interest, dividends, net gains and other income from trading assets and activities, including but not limited to assets and activities in the matched book, in the arbitrage book and foreign currency transactions (but excluding amounts described in subparagraphs (A) or (B) of this paragraph), attributable to this state and included in the numerator is determined by multiplying the amount described in subparagraph (B) of paragraph (1) by a fraction, the numerator of which is the gross income from such trading assets and activities which are properly assigned to a regular place of business of the taxpayer within this state and the denominator of which is the gross income from all such assets and activities.

(4) If the taxpayer elects or is required by [the State Tax Administrator] to use the method set forth in paragraph (3) of this subdivision, it shall use this method on all subsequent returns unless the taxpayer receives prior permission from the State Tax Administrator to use, or the State Tax Administrator requires a different method.

(5) The taxpayer shall have the burden of proving that an investment asset or activity or trading asset or activity was properly assigned to a regular place of business outside of this state by demonstrating that the day-

to-day decisions regarding the asset or activity occurred at a regular place of business outside the state. Where the day-to-day decisions regarding an investment asset or activity or trading asset or activity occur at more than one regular place of business and one such regular place of business is in this state and one such regular place of business is outside this state, such asset or activity shall be considered to be located at the regular place of business of the taxpayer where the investment or trading policies or guidelines with respect to the asset or activity are established. Unless the taxpayer demonstrates to the contrary, such policies and guidelines shall be presumed to be established at the commercial domicile of the taxpayer.

(n) **All other receipts.** The numerator of the receipts factor includes all other receipts pursuant to the rules set forth in ... [INSERT YOUR STATE'S REGULAR SITUSING RULES FOR THE RECEIPTS NOT COVERED BY THIS SECTION.]

(o) **Attribution of certain receipts to commercial domicile.** All receipts which would be assigned under this section to a state in which the taxpayer is not taxable shall be included in the numerator of the receipts factor, if the taxpayer's commercial domicile is in this state.

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 the 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 leased 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 subdivision 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 subdivision, 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 -

(i) it is properly assigned to a regular place of business of the taxpayer within this state; or

(ii) in the case of a taxpayer organized under the laws of the United States or of any state of the United States, the District of Columbia, the Commonwealth of Puerto Rico or any territory or possession of the United States, the loan is assigned to a place which is not a regular place of business of the taxpayer and such taxpayer's commercial domicile is within this state; or

(iii) in the case of a taxpayer organized under the laws of a foreign country, the loan is assigned to a place which is not a regular place of business of the taxpayer and such taxpayer has declared this state to be its home state pursuant to the provisions of the International Banking Act of 1978. If a taxpayer described in this clause has not made such a declaration or is not required to make such a declaration, the loan shall be presumed to be located at the place in the United States to which the greatest number of employees are regularly connected or out of which they are working, irrespective of where the services of such employee are performed, as of the last day of the calendar year.

(B) The state in which a loan has a preponderance of substantive contact with a regular place of business of the taxpayer shall be the state in which a loan is properly assigned.

(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 subdivision (g) of this section.

(i) **Elements to Consider in Determining Proper Assignment of Certain Intangible Assets.**

In order to determine the state to which loans or credit card receivables are properly assigned under the "preponderance of substantive contact" test for the purpose of locating said property under Section 4(g)(1)(B) and 4(h), consideration is to be given to such things as: solicitation, investigation, negotiation, approval and administration. The terms "solicitation", "investigation", "negotiation", "approval" and "administration" are defined as follows:

(1) *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.

(2) *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 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.

(3) *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.

(4) *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.

(5) *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.

Notwithstanding any provision contained herein to the contrary, the taxpayer shall have the burden to prove, by clear and convincing evidence, that an item of receipt, property or payroll has been properly assigned on its books and records.

(j) **Period for which Properly Assigned Loan Remains Assigned.**

A loan that has been properly assigned to a state shall 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 there.

Section 5. Payroll factor.

(a) **General.** The payroll factor is a fraction, the numerator of which is the total amount paid in this state during the taxable year by the taxpayer for compensation and the denominator of which is the total compensation paid both within and without this state during the taxable year. The payroll factor shall include only that compensation is included in the computation of the apportionable income tax base for the taxable year.

(b) **Compensation relating to Nonbusiness Income and Independent Contractors.**

The compensation of any employee for services or activities which are connected with the production of nonbusiness income (income which is not includable in the apportionable income base) and payments made to any independent contractor or any other person not properly classifiable as an employee shall be excluded from both the numerator and denominator of the factor.

(c) **When Compensation Paid in this state.** Compensation is paid in this state if any one of the following tests, applied consecutively, is met:

- (1) The employee's services are performed entirely within this state.

(2) The employee's services are performed both within and without the state, but the service performed without the state is incidental to the employee's service within the state. The term "incidental" means any service which is temporary or transitory in nature, or which is rendered in connection with an isolated transaction.

(3) If the employee's services are performed both within and without this state, the employee's compensation will be attributed to this state:

(A) if the employee's principal base of operations is within this state; or

(B) if there is no principal base of operations in any state in which some part of the services are performed, but the place from which the services are directed or controlled is in this state; or

(C) if the principal base of operations and the place from which some part of the services are directed or controlled are not in any state in which some of service is performed but the employee's residence is in this state.

EXHIBIT B

PRE-MAY 10, 1990 PROCEEDINGS

EXHIBIT B: 1

Initial Draft Proposal of Regulation (July 1987)

July 1987 Draft Proposal of

**PROPOSED REGULATION FOR THE ATTRIBUTION OF THE INCOME OF
FINANCIAL INSTITUTIONS**

- (A) **Definitions.** Except as specifically defined herein, all terms used in this regulation shall have the same meaning as such terms have under [here include your State cite to the Multistate Tax Compact or other applicable state law] and the rules and regulations promulgated thereunder.
- (1) "Receipts" for the purpose of the receipts factor, means gross income, including net taxable gain on disposition of assets (including securities, loans, personal and real property and money market transactions) when derived from transactions and activities in the regular course of the taxpayer's trade or business.
 - (2) "Participation Loan" means a loan in which more than one lender is a creditor to a common borrower.
 - (3) "Securities" means United States Treasury securities, obligations of United States Government agencies and corporations, obligations of State and political subdivisions, corporate stock and other corporate securities, participations in securities backed by mortgages held by United States or State government agencies, loan-backed securities and similar investments to the extent that such investments are reflected as assets under generally accepted accounting principles.
 - (4) "Money Market Instruments" mean Federal funds sold and securities purchased under agreements to resell, commercial paper, banker's acceptances, and purchased certificates of deposit and similar instruments to the extent that such instruments are reflected as assets under generally accepted accounting principles.
 - (5) "Property Located in this State"
 - (a) **Tangible Property: General Rule.** -- Except as otherwise provided in this section, tangible and real property which is security for a loan or property subject to a lease, shall be considered to be located in the state in which such property is physically situated.
 - (b) **Moveable tangible property.** -- Tangible personal property which is characteristically moving property, such as motor vehicles, rolling stock,

aircraft, vessels, mobile equipment, and the like shall be considered to be located in a state if:

- (i) the operation of the property is entirely within the state; or
- (ii) the operation of the property is in two or more states, but the principal base of operations from which the property is sent out is in the state. It shall be presumed, subject to rebuttal, that the location of operation of the property and the principal base of operations from which the property is sent out shall be that duly certified in writing by the lessee or borrower.

(6) "Exercising a Corporate Franchise or Transacting Business in a State." A financial institution is exercising a corporate franchise or transacting business in this state if:

- (a) it has a place of business in this state;
- (b) it has employees, representatives or independent contractors conducting business activities in its behalf in this state; or,
- (c) it engages in regular solicitation in this state (whether at a place of business, by travelling loan officers or other representatives, by mail, by telephone or other electronic means), and the solicitation results in the creation of a depository or direct debtor/creditor relationship with a resident of this state. For purposes of this regulation, mere processing or transfer through financial intermediaries of checks, credit card receivables, commercial paper and the like does not create a debtor/creditor relationship.

A financial institution is engaged in regular solicitation within this state if it has entered into any of the relationships listed in subsection (c) above with 20 or more residents of this state during any tax period or if it has \$5,000,000 or more of assets attributable to sources within this state at any time during the tax period.

(7) "Taxpayer" means a financial institution which is subject to taxation in a state because it is exercising its corporate franchise or is transacting business in a corporate or organized capacity in the state and has gross income attributable under this regulation to sources within this state.

- (8) "Subsidiary" means a corporation whose voting stock is more than 50% owned, directly or indirectly, by a financial institution.
- (9) "Holding Company" means any corporation subject to [insert citation of the state law governing the creation of bank holding companies] or registered under the Federal Bank Holding Company Act of 1956, as amended, or registered as a savings and loan holding company under the Federal National Housing Act, as amended.
- (10) "Regulated Financial Corporation" means an institution the deposits or accounts of which are insured under the Federal Deposit Insurance Act or by the Federal Savings and Loan Insurance Corporation, any institution which is a member of a Federal Home Loan Bank, any other bank or thrift institution incorporated or organized under the laws of the United States, any State or any foreign country which is engaged in the business of receiving deposits or which holds a bank charter, any corporation organized under the provision of 12 U.S.C. sections 611 to 631 (Edge Act Corporations), and any agency of a foreign depository as defined in 12 U.S.C. section 3101.
- (11) "Business of a Financial Institution" includes the following:
- (a) the business that a regulated financial corporation may be authorized to do under state or federal law or the business that its subsidiary is authorized to do by the proper regulatory authorities.
 - (b) the business that any corporation organized under the authority of the United States or organized under the laws of this state or any other state or country does/or has authority to do which is substantially similar to the business which a corporation may be created to do under [insert citations of state's laws governing the creation of banks and trust companies, industrial banks, savings and loan associations, etc.] or any business which a corporation or its subsidiary is authorized to do by said laws.
 - (c) the business that any corporation organized under the authority of the United States or organized under the laws of this state or any other state or country does or has authority to do if such corporation derives more than fifty percent of its gross income from lending activities (including discounting obligations) in substantial competition with the businesses described in subsections (a) and (b) above. For purposes of this subsection, the computation of the gross income of a corporation

shall not include income from nonrecurring, extraordinary items.

- (12) "Financial Institution" includes the following:
- (a) A holding company.
 - (b) Any regulated financial corporation.
 - (c) Any other corporation organized under the laws of the United States or organized under the laws of this state or any other state or country which is carrying on the business of a financial institution.
- (13) "Place of consumption or use of services" means the state in which the benefits of the services are received. If such benefits are received in more than one state, the receipts from those benefits shall be apportioned to this state pro rata according to the portion of the benefits received in this state.
- (14) "Borrower" means the individual or entity who is primarily liable on a debt instrument. If more than one individual or entity is primarily liable on a debt instrument, each such individual or entity shall be considered the borrower to the extent of its interest in the debt instrument. For purposes of this regulation, a partnership shall be treated as a group of individuals.
- (15) "Deposit" means:
- (a) the unpaid balance of money or its equivalent received or held by a financial institution in the usual course of business and for which it has given or is obligated to give credit, either conditionally or unconditionally, to a commercial, checking, savings, time, or thrift account whether or not advance notice is required to withdraw the credited funds, or which is evidenced by its certificate of deposit, thrift certificate, investment certificate, or certificate of indebtedness, or other similar name, or a check or draft drawn against a deposit account and certified by the financial institution, or a letter of credit or a traveler's check on which the financial institution is primarily liable; provided, that, without limiting the generality of the term "money or its equivalent," any such account or instrument must be regarded as evidencing the receipt of the equivalent of money when credited or issued in exchange for checks or drafts or for a promissory note upon which the person obtaining any such credit or instrument is primarily or secondarily liable or for a charge against a deposit

account or in settlement of checks, drafts, or other instruments forwarded to such bank for collection;

- (b) trust funds received or held by such financial institution, whether held in the trust department or held or deposited in any other department of such financial institution;
 - (c) money received or held by a financial institution, or the credit given for money or its equivalent received or held by a financial institution in the usual course of business for a special or specific purpose, regardless of the legal relationship thereby established, including, without being limited to, escrow funds, funds held as security for an obligation due the financial institution or others (including funds held as dealers reserves) or for securities loaned by the bank, funds deposited by a debtor to meet maturing obligations, funds deposited as advance payment on subscriptions to United States Government securities, funds held for distribution or purchase of securities, funds held to meet its acceptances or letters of credit, and withheld taxes; provided that there shall not be included funds which are received by the financial institution for immediate application to the reduction of an indebtedness to the receiving financial institution, or under condition that the receipt thereof immediately reduces or extinguishes such an indebtedness;
 - (d) outstanding drafts (including advice or authorization to charge a financial institution's balance in another such institution), cashier's checks, money orders, or other officer's checks issued in the usual course of business for any purpose, but not including those issued in payment for services, dividends, or purchases or other costs or expenses of the financial institution itself;
 - (e) money or its equivalent held as a credit balance by a financial institution on behalf of its customer if such entity is engaged in soliciting and holding such balances in the regular course of its business.
- (16) "State" means a state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, or any territory or possession of the United States or any foreign country.
- (17) "Taxable in a State." For the purpose of the receipts factor, a taxpayer is taxable in another state if: (a) in that state, he is subject to a franchise tax measured by net income, a net income tax, a franchise tax for the

privilege of doing business, or a corporate stock tax, or (b) that State has jurisdiction to subject the taxpayer to such a tax regardless of whether, in fact, the State does or does not.

(18) "Resides/Residence/Resident." A person shall be considered to reside or make his or her residence in or be a resident of a state if, in the case of an individual, he/she resides there for more than 100 days of the relevant tax period. For purposes of this regulation, a partnership shall be treated as a group of individuals, each of whom is subject to the above residence rule. A corporation shall be considered a resident of the state in which it has an office or other place of business during the relevant tax period. For purposes of this regulation, a corporation may be a resident of more than one state. An individual or a corporation shall be presumed, subject to rebuttal, to reside at (i.e., be a resident of, make his residence at) the address to which the statement of account is regularly mailed.

(B) **Business Income.** All income (taxable under the laws of this State) which arises from the business of a financial institution shall be deemed derived from transaction in the regular course of the taxpayer's business and subject to apportionment under this regulation. All such income which arises from activities of a financial institution which are not the business of a financial institution as defined in this rule shall be apportioned or allocated in accordance with the rules set forth in [here include your State cite to UDITPA or the Multistate Tax Compact].

(C) **Apportionment of Business Income.**

(1) **General Method.**

(a) If a financial institution is carrying on the business of a financial institution both within and without this state and if, by reason of such business activity, it is taxable in another state, the portion of the net income (or net loss) arising from such business which is derived from sources within this state shall be determined by apportionment in accordance with this regulation.

(b) The tax applicable to financial institutions whose net income (or net loss) is apportionable according to the rules in this section shall be determined by multiplying the tax base by a fraction the numerator of which is the sum of the receipts factor, the

property factor, and the payroll factor as defined in this regulation and the denominator of which is three. If any factor(s) is missing, the remaining factors are added together and the sum is divided by the number of remaining factors. A factor is missing if both its numerator and denominator are zero, but it is not missing merely because its numerator is zero.

- (2) Receipts Factor. In general. -- The receipts factor is a fraction the numerator of which is the receipts of the taxpayer within this state during the tax period and the denominator of which is the total receipts of the taxpayer from all states in which the taxpayer is taxable during such tax period. The numerator of the receipts factor shall include, in addition to items otherwise assignable under [here include your State cite to the Multistate Tax Compact or other applicable state law]:
- (a) Receipts from the lease or rental of real or tangible personal property (including both finance leases and true leases) shall be attributed to this state if the property is located in this state;
 - (b) Interest income and other receipts from assets in the nature of loans which are secured primarily by real estate or tangible personal property shall be attributed to this state if such security property is located in this state;
 - (c) Interest income and other receipts from consumer loans not secured by real or tangible personal property that are made to residents of this state (whether at a place of business, by travelling loan officer, by mail, by telephone or other electronic means) shall be attributed to this state;
 - (d) Interest income and other receipts from commercial loans and installment obligations not secured by real or tangible personal property shall be attributed to this state if and to the extent that the borrower is a resident of this state;
 - (e) Interest income and other receipts from a participating financial institution's portion of participation loans shall be attributed under the rules set forth in subsections (a) through (d);
 - (f) Interest income and other receipts, including service charges from financial institution credit card and travel and entertainment credit card receivables and credit card holders' fees shall be attributed to the state to which such card charges and fees are regularly billed;

- (g) Merchant discount income derived from financial institution credit card holder transactions with a merchant shall be attributed to the state in which the merchant is located. In the case of merchants located within and without this state, only receipts from merchant discounts attributable to sales made from locations within the state shall be attributed to this State. It shall be presumed, subject to rebuttal, that the location of a merchant is the address shown on the invoice submitted by the merchant to the taxpayer.
 - (h) Receipts from the performance of fiduciary and other services are attributed to this state if the services are consumed or used in this state;
 - (i) Receipts from the issuance of travelers checks and money orders shall be attributed to the state in which such checks and money orders are purchased;
 - (j) Receipts from investments of a financial institution in securities of this state, its political subdivisions, agencies and instrumentalities shall be attributed to this state;
 - (k) Receipts from investments of a financial institution in other securities and from money market instruments shall be apportioned to this state based upon the ratio that total deposits from this state, its residents, its political subdivisions, agencies and instrumentalities bear to the total deposits from all states, their residents, their political subdivisions, agencies and instrumentalities. In the case of an unregulated financial institution subject to this regulation, such receipts shall be apportioned to this state based upon the ratio that its gross business income earned from sources within this state bears to gross business income earned from sources within all states. For purposes of this subsection, deposits made by this state, its residents, its political subdivisions, agencies and instrumentalities shall be attributed to this state, whether or not such deposits are accepted or maintained by the taxpayer at locations within this state.
 - (l) All receipts located by this rule in a state without jurisdiction to tax shall be excluded from both the numerator and the denominator of the receipts factor.
- (3) Property Factor. In general. -- The property factor is a fraction the numerator of which is the average value

of the taxpayer's real and tangible personal property owned or rented and used in and intangible property attributed to this state during the tax period and the denominator of which is the average value of all of the taxpayer's real and tangible personal property owned or rented and used in and intangible property attributed to all states during the tax period. For purposes of this regulation, the value of property owned by the taxpayer shall be its federal income tax basis, without diminution for bad debt reserves; the value of property rented by the taxpayer shall be eight times its net annual rental rate. The net annual rental rate for any item of rented property is the annual rate paid by the taxpayer for such property less the aggregate annual subrental rates paid by subtenants of the taxpayer. Intangible personal property shall be included at its tax basis for federal income tax purposes. Goodwill shall not be included in the property factor. The numerator of the property factor shall include, in addition to items otherwise assignable under [here include your State cite to the Multistate Tax Compact or other applicable state law], the following:

- (a) Coin and currency located in this state shall be attributed to this state;
- (b) Lease financing receivables shall be attributed to this state if and to the extent that the property is located within this state;
- (c) Assets in the nature of loans which are secured by real or tangible personal property shall be attributed to this state if and to the extent that the security property is located within this state;
- (d) Assets in the nature of consumer loans and installment obligations which are unsecured or secured by intangible property shall be attributed to this state if the loan was made to a resident of this state;
- (e) Assets in the nature of commercial loan and installment obligations which are unsecured or secured by intangible property shall be attributed to this state if and to the extent that the borrower is a resident of this state;
- (f) Assets in the nature of funds deposited by one financial institution in another financial institution shall be attributed to this state if the depositor is a resident of this state;

- (g) A participating financial institution's portion of a participation loan shall be attributed under the rules set forth in subsections (b) through (e);
- (h) Financial institution credit card and travel and entertainment credit card receivables shall be attributed to this state if such credit card charges and fees are regularly billed to a resident of this state;
- (i) Assets in the nature of securities of this State, its political subdivisions, agencies and instrumentalities shall be attributed to this state;
- (j) Assets in the nature of securities and money market instruments shall be apportioned to this state based upon the ratio that total deposits from this State, its residents, its political subdivisions, agencies and instrumentalities bear to the total deposits from all States, their residents, their political subdivisions, agencies and instrumentalities. In the case of an unregulated financial institution subject to this regulation, such receipts shall be apportioned to this state based upon the ratio that its gross business income earned from sources within all states. For purposes of this subsection, deposits made by this State, its residents, its political subdivisions, agencies and instrumentalities shall be attributed to this state whether or not such deposits are accepted or maintained by the taxpayer at locations within this state.

All property located by this rule in a state without jurisdiction to tax shall be excluded from both the numerator and the denominator.

- (4) Payroll Factor. In general. -- The payroll factor is a fraction the numerator of which is the total amount paid by the taxpayer for compensation during the year and the denominator of which is the total amount of compensation paid in every state.
 - (a) Neither the numerator nor the denominator of the payroll factor shall include wages paid to an employee in a state without jurisdiction to tax.

- (D) **Special Rules.** If the allocation and apportionment provisions of this regulation do not fairly represent the extent of the taxpayer's activity in this state, the taxpayer may petition for or the tax administrator may require, in respect to all

or any part of the taxpayer's business activity, if reasonable:

- (1) Separate accounting;
- (2) The exclusion of any one or more of the factors;
- (3) The inclusion of one or more additional factors which will fairly represent the taxpayer's business activity in this state; or
- (4) The employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

EXHIBIT B: 2

**Proposed Revisions to MTC's Draft Regulations from Eugene Mason
(First Bank System, Minneapolis, MN)
(April 1988)**

Multistate Tax Commission Meeting
Midwest Financial Institutions
Chicago - April 19, 1988

Eugene Mason
First Bank System
Minneapolis, MN

Proposed Revisions to MTC's Draft Regulations

1. (A) (2) "Participation Loans" means ~~a loan in which more than one lender is a creditor to a common borrower~~ an arrangement in which a lender makes a loan to a borrower and then sells, assigns, or otherwise transfers, all or a part of the loan to a purchasing financial institution. A syndication loan is a multi bank loan transaction in which all the lenders are named as parties to the loan documentation, are known to the borrower, and have privity of contract with the borrower.

2. (A) (5) (b) Movable tangible property. - Tangible personal which is characteristically moving property, such as motor vehicles, rolling stock, aircraft, vessels, mobile equipment, and the like shall be considered to be located in a State if:
 - (i) the operation of the property is entirely within the state; or
 - (ii) the operation of the property is in two or more states, but the principal base of operations from which the property is sent out is in the state. ~~It shall be presumed, subject to rebuttal, that the location of operation of the property and the principal base of operations from which the property is sent out shall be in the same state as the billing address of the borrower or lessee.~~

It shall be presumed, subject to rebuttal, that the location of operation of the property and the principal base of operations from which the property

is sent out shall be in the same state as the
billing address of the borrower or lessee.

3. (A)(6)(c) it engages in regular solicitation in this state (whether at a place of business, by traveling loan officers or other representatives, by mail, by telephone or other electronic means), and the solicitation results in the creation of a depository of or direct debtor/creditor relationship with a resident of this state. For purposes of this regulation, mere processing or transferor through financial intermediaries of checks, credit card receivables, commercial paper and the like does not create a debtor/creditor relationship. A financial institution is presumed, subject to rebuttal, to be engaged in regular solicitation within this state if it has entered into any of the relationships listed in subsection (c) above with 100 or more residents of this state during any tax period or it has ~~\$5,000,000~~ 50,000,000 or more of assets attributable to sources within this state at any time during the tax period.

4. (A)(6)(d) Exceptions - A financial institution will not be considered to have exercised a corporate franchise nor transacting business in this state due to the ownership of an interest in the following types of property (including those contacts with this state reasonably required to evaluate and complete the acquisition or disposition of the property, the servicing of the property or the income from it, the collection of income from the property, or the acquisition or liquidation of collateral relating to the property):
- (i) an interest in real estate mortgage investment

conduit, a real estate investment trust, or a regulated investment company, as those terms are defined in the Internal Revenue Code of 1986, as amended through December 31, 1988;

- (ii) an interest in securities as defined in section (A)(3), or money market instruments as defined in (A)(4) above.
- (iii) an interest in a loan-backed, mortgage-backed, or receivable-backed security representing either (1) ownership in a pool of promissory notes, mortgages, or receivables or certificates of interest or participation in such notes, mortgages, or receivables, or (2) debt obligations or equity interest which provide for payments in relation to payments or reasonable projections of payments on the notes, mortgages, or receivables;
- (iv) an interest acquired from a person in any asset described in section (C)(3)(b) to (j), subject to the provisions contained in section (A)(6)(e);
- (v) an interest acquired from a person in the right to service, or collect income from any assets described in section (C)(3)(b) to (j), subject to the provisions contained in section (A)(6)(e);
- (vi) an interest acquired from a person in a funded or unfunded agreement to extend or guarantee credit whether conditional, mandatory, temporary, standby, secured or otherwise subject to the provisions contained in section (A)(6)(e);
- (vii) an interest of a person other than an individual, estate, or trust, in any intangible, tangible, real, or personal property acquired in satisfaction, whether in

whole or in part of any asset embodying a payment obligation which is in default, whether secured or unsecured, the ownership of an interest in which would be exempt under the preceding provisions of this section, provided the property is disposed of within a reasonable period of time; or

(viii) amounts held in escrow or trust accounts, pursuant to and in accordance with the terms of property described in this section.

5. (A)(6)(e) For purposes of clauses (iv) to (vi) of (A)(6)(d):

(i) an interest in the types of assets or credit agreements described shall be deemed to exist at the time the owner becomes legally obligated (conditionally or unconditionally) to fund, acquire, renew, extend, amend or otherwise enter into the credit arrangement.

(ii) An owner has acquired an interest from a person in clauses (iv) to (vi) of (A)(6)(d) assets if (1) the owner at the time of the acquisition of the asset does not own, directly or indirectly, 15 percent or more of the capital or profit interests of the person from whom it has acquired the asset, (2) such person from whom the owner has acquired the asset regularly sells, assigns or transfers interests in any clauses (iv) to (vi) of (A)(6)(d) assets during the full twelve calendar months immediately preceding the month of acquisition to three or more persons and (3) such person from whom the owner has acquired the asset does not sell, assign or transfer 90 percent or more of its clauses (iv) to (vi) of (A)(6)(d) assets during the full twelve calendar months immediately preceding the month of acquisition to the

owner. For purposes of determining indirect ownership under (1) of this paragraph, the owner is deemed to own all stock, capital or profit interests owned by another person if the owner directly owns 15 percent or more of the stock, capital or profit interests in that other person. The owner is also deemed to own through any intermediary parties all stock, capital and profit interests directly owned by any person to the extent there exists a 15 percent or more chain of ownership of stock, capital or profit interests between the owner, intermediary parties and that person.

(iii) If the owner of the asset is a member of a unitary group, clauses (iv) to (viii) do not apply to an interest acquired from another member of the unitary group. If the interest in the asset was originally acquired from a non-unitary member and at that time qualified as (A)(6)(d) asset, the foregoing limitation does not apply.

6. (A)(7) "Taxpayer" means a financial institution which is subject to taxation in a state because it is exercising its corporate franchise, or is transacting business in a corporate or organized capacity in the state, and or has gross income attributable under this regulation to sources within this state.

7. (A)(10) "Regulated Financial Corporation: means an institution, the deposits or accounts of which are insured under the Federal Deposit Insurance Act or by the Federal Savings and Loan Insurance Corporation, any institution which is a member of a Federal Home Loan Bank, any other bank or thrift institution incorporated or organized under the laws of the United

States, any State or any foreign corporation organized under the provision of 12 U.S.C. sections 611 to 631 (Edge Act Corporations), and any agency of a foreign depository as defined in 12 U.S.C. section 3101. It is presumed that either a holding company [as defined in (A)(9) above] or a subsidiary [as defined in (A)(8) above] of a regulated financial institution is a regulated financial institution for purposes of this regulation.

8. (C)(2)(h) Receipts from the performance of services are attributed to this state if:
- (i) the service receipts are loan related fees and the borrower resides in this state:
 - (ii) the service receipts are deposit related fees and the depositor resides in this state:
 - (iii) the service receipts are third party financial institution check processing fees and the third party financial institution resides in this state:
 - (iv) the service receipts is a brokerage fee and ~~the brokerage account is maintained at an office of the financial institution located~~ billing address of the account holder is located in this state:
 - (v) the service receipts are fees related to estate or trust services and ~~the executor or trustee resides in this state or, if there are two or more executors or trustees, the executor or trustee primarily responsible for administering the estate or trust is located~~ decendent for whom the estate relates resided in this state immediately before death or the grantor who either funded or established the trust resides in this state: or
 - (vi) the service receipt is associated with the

performance of any other service not
identified above and the service is primarily
performed in this state.

Reasons for Proposed Changes
MTC's 1/89 Draft Regulations

1. To the extent that MTC adopts a secondary market (see new (A)(6)(d)) asset exception to the exercising a corporate franchise or transacting business in the state provision, this definition must be changed to provide a distinction between participation loans which may qualify for exemption and syndicated loans which should not qualify for exemption.
2. The presumptive rule would not have applied to (5)(b)(i) and property would be assigned to state where located. This result was not consistent with adding the presumption to (5)(a) and (5)(b)(ii).
3. - Correction of apparent drafting error.
 - The deminimis exception based on the \$5,000,000 dollars of assets located in a state is too low to provide a meaningful exemption for most financial institutions. The floor amount must be increased to a higher amount, similar to the increase in the number of transactions which were increased from 20 to 100 in the 1/89 redraft.
4. The current regulation will allow a state to impose its taxes on a foreign financial institution if that institution acquires intangible assets, such as loans and leases, which would be situated in that state, regardless of how the assets are acquired. For example the regulation would provide identical taxation of two consumer loans to a state resident, the only difference between the two being that one loan was made directly to the resident via the bank's direct marketing activities, the other loan being purchased as part of a large pool of loans, originated and packaged by a bank domiciled in the state. The above amendment would recognize an inherent difference between financial assets directly solicited and entered into by a taxpayer and the repurchase of loans and leases which are originated by another.

5. Provides timing and limitation rules for identifying assets which if acquired by a out of state financial institution would not lead to the exercising of a corporate franchise or doing business in the state. Clause (i) would provide the timing rule for determining when a asset is created. This is important where adjustments, refundings, and other changes are called for in the original contract to extend credit or provide other services. Clause (ii) provides a three prong test analysing the relationship between a buyer and seller of financial assets to determine whether the transfer should be excludable. Clause (iii) provides that assets which are transferred between members of an unitary group are not excludable.

6. The definition is very unclear which of the three factors must be satisfied in order for a financial institution to be considered a taxpayer. The redraft above requires satisfying only 1 of the 3 conditions.

7. The regulation provides for different apportionment rules for the regulated and unregulated financial institutions. The regulations do not provide guidance on the application of these rules when an affiliated group of companies include both regulated and unregulated companies. Since the decision to conduct a regulated financial business either in a single entity form, or thru multiple entities encompassing a holding company, the regulated financial institution, and one or more nonbank subsidiaries is one of merely business philosophy and does not reflect a fundamental difference in the type of business being conducted there is not a valid basis for providing different tax rules.

Without adopting an amendment to the regulation treating all affiliated members of a regulated financial institution group, the MTC must adopt regulations providing guidance on the use of the existing rules.

8. These amendments would identify the state location of either the brokerage account holder, the state of residency of the

decedent immediately prior to death, or the state of residency of a trust grantor for purposes of situsing these service fees. Identifying the location of the user of the services is consistent with the aim of loan and deposit related receipts in (i) and (ii) of this section.

EXHIBIT B: 3

**Letter from Haskell Edelstein
(Citicorp) (September 19, 1988)**

Citicorp
399 Park Avenue
New York, NY
10043

Haskell Edelstein
Senior Vice President and
General Tax Counsel

September 19, 1988

Eugene F. Corrigan
Executive Counsel
Multistate Tax Commission
1790 30th Street - Suite 314
Boulder, Colorado 80301 - 1024

Dear Gene:

As I promised, I have carefully reviewed the material you sent me regarding the MTC draft regulations on the state taxation of financial institutions, and offer the comments in this letter and its attachments. While my delay in responding was due to unforeseen circumstances, it turns out to be rather fortuitous because events which have developed recently help to reinforce my concerns.

At the outset, I believe there is general agreement that the best tax system is one which is fair and equitable to both taxpayer and tax collector, produces predictable results, is capable of being administered, complied with by taxpayers and audited, all with reasonable accuracy and certainty, and without undue expense to either taxpayers or tax collectors.

The responses to your specific questions, and technical comments on the draft regulations, are attached.

As a general proposition, most problems, both substantive and compliance-related, arise because of the fundamental premise underlying the draft regulations: that income from financial services should be sourced and taxed where the customer is located. That premise not only generates many practical problems, but is difficult to support conceptually.

The conceptual problem is that states are entitled to tax corporations on income earned in a state provided the corporation is "doing business" in the state. The location of the customer or user of services is not necessarily an appropriate indicator of where the business of rendering those services was done, or indeed whether the corporation rendering those services was "doing business" at the location of the use of the services. In that respect, many of the problems which would arise in the income tax area would be very similar to the problems of imposing sales taxes on services rendered for a state resident by an out-of-state corporation. The Florida experience in that area is most instructive.

Since financial institutions are in the financial services business, even lending money constitutes a service, not the sale or transfer of an intangible asset. If the financial services business is viewed for taxing purposes as the business of furnishing services, then most business should properly be treated as being conducted where the services are in fact rendered, not the location of the customer.

I recognize that the reason for the approach adopted by the draft regulations is to provide a rationale for the so-called market states to extract tax revenues from the big money-center or regional banks, regardless of whether they have a presence in the state where the customers are located.

There are two substantial problems with such an approach:

1. Unless every major banking state (e.g., New York, California, Illinois and indeed even South Dakota and Nevada) adapts the same rules as the market states, there will inevitably be double taxation of the same income by both the customer's state and the financial institution's state of residence. Multiple state taxation of the same income is intolerable. From my perspective, I have no difficulty in a financial institution paying a reasonable level of taxes to all states in the aggregate. Indeed, assuming an appropriate overall state tax burden can be determined, how the states divide up that "pie" is almost irrelevant. The problem is that, absent universal adoption of the same rules, financial institutions will be badly whipsawed by states applying contradictory rules.

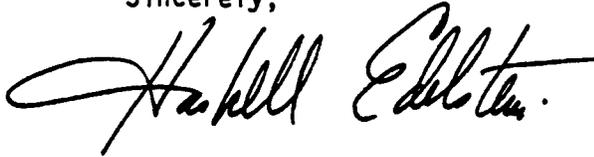
Ideally, that problem could be solved by Federal legislation mandating a uniform set of rules for determining nexus and sourcing of receipts. Better still, each corporation could pay a surtax on its Federal taxable income, which would be put in a pool to be divided up among the states as they saw fit. However, the prospect for Federal Legislation is not favorable. That would seem to leave the problem to the courts if the states proceed in essentially opposite directions.

2. The other major problem is one of compliance and audit. The proposed nexus and sourcing of receipts rules would require detailed and extensive gathering of facts and analysis. Much of the requisite information which the financial institutions would be required to obtain is not readily available, and indeed would not even have any use aside from the possible tax requirements. The data problem is also magnified to the extent that the facts are only obtainable from the customers, or are dependant upon the actions of customers. Determining the tax liability of any business taxpayer, either by requiring it to solicit information, not otherwise needed in its business, from its customers, or making tax liability dependant on the action of customers, is highly questionable tax policy. The data aspects would be particularly burdensome, both in obtaining and in auditing, for the larger institutions. Those burdens could be viewed as so "offensive" as to possibly cause serious problems in voluntary compliance, which is a key element in the successful functioning of any self-assessment taxing system.

Therefore, I see serious fundamental difficulties with the principles underlying the draft regulations. The only practical solution would be to view financial services as a service business, and to tax services where they are rendered, including the service of lending money. While the market states would not gain the revenue they anticipate from taxing non-resident financial institutions, the state tax systems of our nation would be much better served and would clearly function more rationally, effectively, and with better compliance and administration. Perhaps it would also encourage the states to permit interstate branching by depository institutions, since their physical presence in the state would then permit the host state to tax them on their in-state income.

I recognize that the problems of developing appropriate rules for state taxation of financial institutions are complex and difficult to resolve. I hope that my comments will prove instructive. If you have any questions, please let me know. I look forward to my continuing participation, with you and other concerned organizations, in seeking an acceptable resolution of these issues.

Sincerely,

A handwritten signature in cursive script, reading "Haskell Edelman". The signature is written in black ink and is positioned below the word "Sincerely,".

attachments
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MTC DRAFT PROPOSED REGULATIONS - TECHNICAL COMMENTS
(References are to sections of Draft Regulations)

A. Definitions

(1) Receipts - use of the term "net taxable gain" is unclear. Does it mean on each sale, or the net gains and losses from securities and other property sales in the aggregate? It should mean an aggregation.

(2) Participation loans - is there any distinction based upon when a creditor became an owner of part of the loan (at the time the loan is first made or by subsequent purchase from the originator)? Would the treatment differ depending on the type of participation? There should be no distinction.

(5)(b) Movable tangible property - while the proposed rule is logical, it is impractical. Where property is security for a loan, the lender cannot practically relate such information to the accounting requirements needed solely for tax purposes. The principal base rule should be adequate, and should not be subject to change once the loan is made.

(6) Doing business in a state - subsection (c) would seem to raise serious Constitutional issues where solicitation is merely by mail or telephone. The 20 customer/\$5 million assets tests is arbitrary and an unwarranted burden on interstate commerce.

(13) Place of consumption or use of services - this definition is more useful in the case of a sales tax than on income or franchise tax. It is also vague in that "the benefits received" in various states are usually not quantifiable.

(14) Borrower - treating a partnership borrower as a passthrough type entity will create major compliance and audit problems (e.g., where the partners consist of a combination of individuals, corporations and other partnerships).

(15) Deposit - treating a travelers check as a deposit is not correct, as in many cases that is not the legal situation. Other items also are incorrectly included in the term when the legal relationships are substantially different from deposits.

(18) Resident - this definition is perhaps accurate, but not practically applicable, especially so in the case of partnerships. It illustrates the problem of determining the taxation of a financial institution on the basis of the activities and whims of its customers, which can change frequently, and often cannot be known to the financial institution. They are also practically inauditable.

B. Business Income - it is difficult to envision that a financial institution will or can have income not derived from its business.

C. Apportionment

(2)(b) Since security for loans does not alter the activity of the lender, nor the location of the borrower, there should be no distinction between loans with and without security, except perhaps for non-recourse loans.

(2)(c) This has important Constitutional implications which have yet to be considered by the courts.

(2)(e) Participation loans - the application of the general rules creates a compliance nightmare. For example, what happens when a portfolio of consumer loans is "securitized"?

(2)(g) Merchant discount - in the case of a multistate merchant who submits its transactions to the bank from a central location, how is the bank to determine the location of the merchant's sales. This is another reason why the taxation of a bank should not be dependent upon the activities of its customers.

(2)(h) Fiduciary and other services - this sounds like a sales tax approach, not an income tax.

(2)(k) Receipts from investments - funds from deposits bear no necessary relationship to any particular use of funds by the financial institution. Likewise, the gross income test has no logical relationship to the investment income.

(2)(1) This throw-out rule vastly complicates compliance and auditing. In order to reduce double taxation, the rule should be a throw-back to the state of residence of the taxpayer.

(3) Property factor - the same or similar comments apply as in the case of receipts.

(4) Payroll factor - see comment at (2)(1) above re throw-out rule.

Haskell Edelstein
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MULTISTATE TAX COMMISSION - DRAFT REGULATIONS ON TAXATION OF BANKS
Response to Specific Questions

1. Receipts Factor - Assignment of Service Fees

In general, fees for services are earned where the service is performed - i.e., where the preponderance of the "seller's" activity is performed. The need for certainty requires that approach, despite the expressed orientation toward the so-called market states. A bank can with reasonable certainty determine where it renders its services; it is frequently impossible to determine with reasonable accuracy and without major gathering of information where the benefits of services are "received".

The serious problems generated by attempting to source fees from services on the basis of customer location is clearly illustrated by the discussion of the laundry list of fees considered by the Uniformity Committee. The problems can be summarized as follows:

(a) It forces the need for separate rules applicable to every type of service. That would compel constant changes and additions as the financial services of banks change and new financial products are developed. Any rules changes would of necessity come only after the fact of business changes, increasing uncertainty. Instead, there should be a single, simple broadly applicable rule for sourcing fees which would obviate the need to look to particular types of services or apply different rules for different services.

(b) The rules would be extremely difficult to comply with and to audit, because the bank would have to attempt to compile information from its customers which it would have no other use for, and customer cooperation would not be assurable. That problem was a major element in Florida's failed attempt to impose a sales tax on out-of-state services rendered to Florida residents. It ought to be a fundamental rule that the incidence of an income based tax should not be based or dependent upon the actions, or the whims, of persons over which they have no practical control and no ability to anticipate or project.

(c) Sourcing rules as proposed depend on the type of customer -- receipt from individual customers would be sourced in one manner, while the same receipt from the same service would be sourced differently if the customer were a partnership or corporation. There is no logical principle to support such an approach. Furthermore, making the distinctions based on the type of customer would compel examination of individual customer files, since even the name would not necessarily indicate the type of customer (e.g., the "Frank Smith Company" could be an individual, partnership or corporation).

(d) The sourcing rules with respect to the specific types of services seem to be inconsistent, since in many cases they apply the test of where the service is rendered, particularly in the case of corporate customers (e.g., deposit fees, trustee fees in case of non-grantor trusts, brokerage fees).

Some of the difficulties and complexities of applying a customer location test in the case of individuals can be clearly shown by the following:

Income sourced where an individual resides - residence is presumed to be the location to which accounts are mailed, although residence is defined as where an individual resides for more than 180 days.

(a) An individual can be a resident of more than one state - if he spends half his time in each of two states, does the taxpayer have to determine which state he was residing in when the income was earned? What if the individual moves several times in the course of a year?

(b) Individuals frequently designate their office or an agent's office to receive mail. In some cases the bank is instructed to "hold all mail" until physically picked up. What is the taxpayer expected to do in such cases?

(c) If a customer opens an account during the year, does the bank have to inquire as to prior residence during the year? If an individual moves from state A to state B and opens an account with a bank's office in state B, are fees allocated to state A because the individual resided in state A for more than 180 days during the year?

(d) How would fees from escrow accounts be assigned when the individual escrowees reside in different states. The escrow agent would not always know the owner of the account.

(e) If addresses are corrected after a return is filed, would it have to be amended?

(f) Making accurate or required estimated tax payments would be impossible if the allocation factors could not or would not be ascertainable until after the close of the year.

In addition to the foregoing general comments, examination of the discussion with respect to specific types of fees indicates the following:

(a) Deposit fees - it is clearly overreacting to suggest that a state should have the right to tax income generated by out-of-state deposits where the laws of that state preclude a bank from operating a branch and earning income in that state (in which case the deposits of such a branch would under any rule be located in that state).

(b) Points are appropriately treated as interest. It should be noted that the timing for taking such income into account for purposes of the receipts factor should be the same as inclusion of the points in taxable income.

(c) Loan servicing fees - There is no logical basis for distinguishing between originated and purchased loans, since the nature of the income is the same.

(d) Check processing fees - if the proposal is intended to suggest that sourcing is to be based on location of the checking accounts on which the checks are drawn, that information would be difficult at best, and more likely impossible to obtain. Most banks would pay a single fee to the other bank, and then divide up the processed checks internally. The processor would have to depend upon the customer-bank for the necessary data, which is unlikely to be available. It would not be auditable.

(e) check charges - see comment at (a).

(f) Trustee fees - The distinction between grantor and other types of trusts is unwarranted, because the nature of the services is identical.

(g) Brokerage fees - No additional comment.

(h) Guarantee fees - these fees are not the equivalent of interest, since no funds are lent. Therefore, the sourcing rule should not follow the interest rules.

(i) Other fees - The problems and concerns would in general be eliminated by not using a location of customer rule as the initial approach.

In general, the various approaches for sourcing of fees indicate a certain schizophrenia -- if there is a problem or difficulty, then go to where the fees are earned!

2. Partnership Unsecured Debt

The proposed rules are indeed unworkable, as the discussion clearly recognizes. Why should a bank have to determine the location, let alone the number of partners? How can it be expected to track changes in the location and number of partners? What would be the effect of changes during a taxable year, and would the effect be time-sensitive? The proposals would generate totally unfair compliance burdens. These proposals illustrate the unfair burdens which would occur in any situation where compliance depends on obtaining information from customers - it is virtually unauditible, it imposes reporting-burdens on two persons (or corporations) rather than just the taxpayer and would require attempting to obtain information from persons totally outside the taxing jurisdiction of the state.

3. Corporate Unsecured Debt

The concerns regarding the possible effects and problems with the "statement rule" are very appropriate. However the Committee's objective - to determine the state "which has a logical relationship to the lending activity" - is not consistent with the location of the borrower as the basis for sourcing receipts and property. Lending activity takes place where the lender conducts its business activities, not where the borrower is located. Thus the proposed rule based on the location of the borrower's negotiator is not consistent with the objective. For example, a bank in State A lends money to Corporation X through the latter's officer located in state B, its headquarters, but the loan proceeds are for the use of the corporation's subsidiary in state A. Why should the interest income be sourced in state B? Neither is the proposal based on "where the proceeds of the loan were applied". More consistent is the alternative proposal, based upon the office of the lender which generated the loan.

The comment on the alleged simplicity of obtaining information from the customer misses two important points:

1. There is very a significant distinction between obtaining information and utilizing it. In the case of banks with many commercial loans, computer systems would have to be modified to code loan interest by states - existing accounting systems could not even be utilized without substantial review of the underlying details in order to utilize the material for tax purposes.

2. No sourcing rule should be dependent on actions of, or obtaining information from, a customer. The various layers of the proposed rule would make auditing impossible, or very time-consuming and expensive. The proposed rule would require not only a loan-by-loan analysis, but also tracking of loan receipts to individual loans. Obtaining information from the customer would be vastly aggravated under the use of proceeds test.

It is interesting to observe that when the location of customer test fails to provide an acceptable result, the proposal reverts to a location of service test, which ought to be the general rule!

4. Receipts from Securities

Income is earned from securities where they are purchased, held and managed. Use of deposits as the sourcing factor fails to recognize the fungibility of a bank's sources of funds. In addition, using the residence of depositors is illogical and a serious matter of overreaching, since there is no real relationship between residence of depositors and how a bank utilizes their deposited funds, especially since those funds cannot be traced to investments in securities or any other assets.

To throw out such receipts is also undesirable, since they are a significant element of a bank's business, and throwing them out would then create issues in determining whether an asset is a "loan" or a "security".

The most logical, consistent and easily audited and determined rule would be to source receipts where the securities are managed.

5. Government Obligations

The dilemmas discussed under this topic appear to be a summary of all the fundamental problems created by a location of borrower test. This issue thus epitomizes the fallacy of sourcing income anywhere other than where it is earned by the recipient. The criticisms of the alternative proposals further emphasize the fallacy.

It is particularly curious that concerns are expressed that the throw-out rule not only would not reflect the bank's "lending activity", but neither would it reflect "the location of risk". Both those elements must be based on the activities of the lender, not the location of the borrower. The location of the lender's activities as the basis for sourcing would solve most of the problems raised, except the problem of giving the market states a greater share of the pie!

6. Purchased obligations

It is indeed remarkable that Constitutional concerns are raised here, since the basic MTC position is understood to be that no physical nexus is required to support taxing jurisdiction so long as the income is derived from a customer in the state.

It should be noted that the purchase of bank loans by a bank from another bank which generated the loan is becoming very common, and expanding dramatically. Such purchases involve individual loans, "pools" of loans and mutual fund type sales (several banks purchasing interests in a group of loans). To attempt to tax the purchasers on any type of look-through basis will create massive compliance and auditing burdens.

Haskell Edelstein
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EXHIBIT B: 4

**Letter from Henry Ruempler
(American Bankers Association) (October 4, 1988)**

October 4, 1988

Mr. Eugene F. Corrigan
Executive Counsel
Multistate Tax Commission
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024

Dear Mr. Corrigan:

The purpose of this letter is to provide the comments of the American Bankers Association ("ABA") on the issues raised in your letter of June 20, 1988 concerning the Multistate Tax Commission ("MTC") Draft Financial Apportionment Regulations. The ABA is the national trade and professional association for America's commercial banks of all sizes and types. Assets of ABA member banks are about 95 percent of the industry total. These banks, operating under both state and national charters, comprise the vast majority of the commercial banking system of the United States. Commercial banks are subject to state taxation in the states in which they are doing business, with many institutions filing tax returns in several states.

Nexus

Banks are currently faced with a trend towards market state taxation, based on extremely low nexus standards, while still paying high home state taxes. There is no federal statute protecting banks from "doing business" taxes on out-of-state depositories since the expiration of the moratorium under P.L. 93-100 and P.L. 94-222 in 1976. The trend towards possible double taxation, with neither a federal statute nor uniform rules, is grounds for concern. The possibility of Congressional intervention appears remote since Congress prefers not to interfere with the states' autonomy in state tax matters.

Low nexus standards such as the MTC draft based on a specified amount of dollars or number of customers within the nondomiciliary state are unreasonable--especially where the financial institution does not otherwise have a physical presence within the state. For example, a state may define "doing business" for nexus purposes as having "x" amount of customers--i.e., credit cardholders residing in the taxing state. Yet, the financial institution may not have a branch or representative within the state--all contact is via the telephone or mail service. For a state to claim that that bank owes taxes and/or must file a report so the bank can have access to the state's court

system appears at odds with the Supreme Court's interpretation of going business. If this was a sales and use tax claim, the state would not be able to assess a tax on the financial institution because the bank does not have a presence.

In the case of a typical large regional bank, twenty credit card customers in an MTC state with average balances of \$1,500 or \$30,000 of loans at 18 percent (\$5,400 interest income) would result in a tax liability of \$36 assuming a ten percent tax rate.

Assume:

Total Gross Receipts	\$1	Billion
Total Assets	\$10	Billion
Total Pre-Tax Income	\$130	Million
Total Payroll	\$180	Million

$$\frac{5,400}{1 \text{ Billion}} + \frac{0}{180 \text{ Million}} + \frac{30,000}{10 \text{ Billion}} \times 130 \text{ Million} \times 10\% =$$

$$.0000028 \times 130 \text{ Million} \times .1 = \underline{\$36}$$

No bank should be subject to tax in a state where it has no physical presence--i.e., brick and mortar and/or employees. Nexus should not be based on unsecured loans--e.g., credit card customers or depositors. In the latter circumstances, merely having twenty depositors move from your state to a contiguous state which adopted the MTC standard would trigger nexus, yet there would be no tax liability as there would be no numerators under the three-factor formula. A deposit, though valuable to the bank, does not, by itself, earn the bank income. Therefore, states should not measure the nexus to tax a bank when it involves a non-income producing activity.

As the present time, the nexus rules in the MTC draft will likely lead to double taxation. The only way to prevent this occurrence is for each state to recognize this inequity and modify their state laws. The ABA recommends that the MTC communicate with each state's Tax Commissioner to see whether and how modifications could be made to prevent double taxation.

Sourcing Income

As a general rule, the MTC regulations "tilt" toward a market state approach, without sufficient concern for the complexity of the rule. If the U.S. Supreme Court broadens the nexus rules so as to permit some amount of service fees to be apportioned to the market state, then the ABA would recommend that only those fees related to loans of individuals or deposits of individuals should be sourced that way. These types of fees are usually associated with loans/deposit interest on the general ledger and management information systems of banks and will be easier than other types of fees to break out by state. With respect to other types of fees and the current rules of the law, the ABA believes a

"where the services are performed" rule is the practical approach, because the location of the customer or user of services is not necessarily an appropriate indicator of where the business of rendering those services was done, or indeed whether the corporation rendering those services was "doing business" at the location of the use of the services. Applying this approach to the service fees listed in your letter,

- a. Deposit Fees -- sourced based on where the bank is domiciled unless a service center is located in the depositor's state.
- b. Points -- sourced based on where the bank is domiciled unless a service center is located in the borrower's state.
- c. Loan Service Processing Fee -- sourced based on where the service is performed. Otherwise, there would be a completely arbitrary allocation of the service fee depending on whether or not the mortgage servicer originated the loan or did not. Even if a mortgage lender originated the loan, it is probably packaged into a security which is then marketed by a brokerage firm and sold to many hundreds or thousands of investors. Therefore, the amounts earned by the holders of the securities have nothing to do with where the loan was originally located. In addition, once a loan is put on a servicing system, it generally is not determined whether it was originated by the mortgage servicer or obtained through some other means. Therefore, to have a different rule for those originated and those purchased would be next to impossible to track. It makes much more sense, in these situations, to have the income taxed where the servicing takes place; where the service is performed; and the income earned.
- d. Check Processing Fee -- sourced based on where the services are performed. The bank may be processing customers' checks from many branches located in more than one state. One address may be utilized for correspondence and billing, so the location of each branch is irrelevant. It would be next to impossible to track each branch location for checks processed.
- e. Check Charges -- sourced based on where the bank is domiciled unless a service center is located in that state.
- f. Trustee Fees -- sourced based on where the service is performed. Trying to track trustee fees by an address other than the address of the commercial domicile of the bank can be very difficult. Your letter indicates that trust fees should be taxed in the state of the grantor's residence. However, there could be more than one grantor to a trust living in more than one state. Any way to track this item would be completely arbitrary and cost prohibitive.
- g. Brokerage Fees -- sourced based on where the service is performed.
- h. Guarantee Fees -- sourced based on where the service is performed.
- i. Other Fees -- sourced based on where the service is performed. Other fees or items that cannot be identified should default to the

residence of the bank receiving the fee. It is the only practical way to track that information.

Partnership Unsecured Indebtedness should be assigned to the partnership's commercial domicile. It is completely unrealistic to require a lender to keep track of money it loaned to a partnership based on the location of the partners. The bank keeps track of the partnership location, not the partners. It would be completely uneconomical for a bank to keep track of that information. It should not make any difference whether there is one or two partners or 5,000. If a customer location criteria is to be used, it should be the address used for the business relationship.

The regulations and your letter quite often refer to the residence of individuals. Residence is defined as where an individual spends more than 180 days in the relevant tax period. How is a bank suppose to track this? Many customers of a bank are multi-state residents. They spend up to six months of time in one state, e.g., Florida and then spend the rest of the year some place else in the country. They may maintain their banking relationship with their Florida banks for the entire year and may or may not change their address with the bank. Even if they do, how are banks suppose to keep track of the 180-day cycle of thousands of customers? Since a bank cannot compel a customer to provide his whereabouts, it would be impossible for a bank to track the residence as defined in these regulations.

Corporate Unsecured Debt should be based on the "residence" of the borrower. The MTC regulations are too concerned about companies playing with addresses to avoid state taxes. The regulations make it unduly complicated by trying to throw in the address of an employee or a customer's employee to try and tie down a particular item. The tax department of a very large bank is not going to get involved in the thousands of customer's addresses in order to manipulate state taxation. To think this can be done, on a practical basis, is very far fetched. Bank tax departments do not have the resources to start tracking addresses or manipulating addresses of customers to avoid or minimize state taxes. A bank's information system is set up to handle one address per customer. In the overwhelming majority of cases, "where the proceeds of loans were applied", location of the officer responsible for applying for the loan, and the place where the statement of account is mailed will be the same. States would always be free to challenge abusive situations.

Assignment of Receipts from Securities is unduly complicated based on the rules that are proposed in your letter. Utilizing deposits as a criteria for allocating interest income of securities is unreasonable since no direct relationship exists between deposits and interest income from securities. Either a state is going to tax federal and/or state obligations or not. If they are going to tax them, they should be left in the net income figures and if they are not going to be taxed, they should be subtracted out. If the income from securities is considered business income, it should be apportioned to a particular state based on the other factors that make up the business income factor. In addition, your definition of deposit on page 4, item 15 of the regulations would

be almost impossible for a bank to track. Some of those items do not even appear on the balance sheet (i.e., letter of credits) and others are not easily obtained from a bank's chart of accounts.

Government Obligations receipts and property apportionment could best be resolved by a throw-out rule (proposal #2 of your letter) whereby securities and note receipts and value would be excluded from both the numerator and denominator of both the property and receipts factors. However, banks with substantial foreign government loans may be unduly burdened by this proposal.

Purchased Obligations do present the need for a special rule that would bring conformity to this issue, e.g., the California statute. The ABA suggests an allocation to the home state as purchases are not a regular activity of banks. Usually, the situs for the booking is the same as the home state.

Although your letter does not solicit the ABA's comments with respect to particular sections of the MTC Draft Regulations, the following comments may facilitate your endeavor:

- Regulations, page 7, item E, Interest on Participations. The information on the original customer of a participation is generally not kept on the system since it is not necessary. A receipt for this item, under a market concept, should be at the location of the bank from which the participation was purchased.

- Regulations page 8, item G, Merchants Discount. If the merchant operates in more than one state, it seems a little far fetched for the merchant to provide his sales factors to the bank.

- Regulations page 9, item F, Assets in the Form of Deposits. In this particular item, the letter has reversed the situs compared to all the other items. In order for this to be an asset, the depositor would have to be the taxpayer and therefore you are allocating this asset to the residence of the taxpayer. These assets ought to be allocated to the state where the financial institution receiving the deposit is located.

- Regulations page 10, item I & J, Assets in Nature of Securities. The same comments apply to this as they do under the receipts section.

- Regulations page 10, item J. The ABA is not sure what this item means because we do not know a state without the jurisdiction to tax. Why is this included in the regulations?

To implement the suggestions in both your letter and the MTC Draft Regulations would necessitate a massive system. Trying to allocate a multitude of different rules will create system nightmares. The proposed rules would necessitate the collection of information, much of which is not readily available, and would not have any use other than tax requirements. The data problem is also compounded because the information is only obtainable from the customers. Determining the tax liability of any business taxpayer, either by requiring it to solicit

information, not otherwise needed in its business from its customers, or making tax liability dependent on the action of customers, is highly questionable tax policy. Furthermore, the approach envisioned in your letter is so different from what currently is done in most states that it could generate a large duplication of income tax. For instance, if your home state taxes income based on commercial domicile that includes sales where there is not a fixed place business or employees in another state, you end up paying tax in your home state as well as the state where the customers are located; or end up in court battles to decide whose income it should be, if not both. Without incurring tremendous cost, these rules are far too complex to adequately track in a computer system. The ABA urges the MTC to reconsider the nexus question as well as devising a simplified method to apportion sales. There is no record to show that the market approach necessarily results in any fairer multi-state income taxation scheme.

Our Association appreciates the opportunity to comment and participate in the Multistate Tax Commission's project on the Financial Apportionment Regulations. The ABA is currently working with State Bankers Associations in the areas of multistate jurisdiction and nexus. As the data becomes available to our office, we would appreciate the opportunity to develop further comments for your organization. We are willing to work with your staff and other interested parties in monitoring states' activities. If you need any additional information, please contact me at (202) 663-5317 or Joanne Ames at (202) 663-4986.

Sincerely,



Henry Ruempfer

EXHIBIT B: 5

**Letter from Philip M. Plant
(Bank of America) (October 14, 1988)**

PHILIP M. PLANT
Vice President and
Assistant General Tax Counsel

October 14, 1988

Eugene F. Corrigan
Executive Counsel
Multistate Tax Commission
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024

Re: MTC Proposed Regulations for the Attribution
of the Income of Financial Institutions

Dear Gene:

Enclosed are the comments of the ABA Tax Section Committee on Banking and Savings Institutions regarding the above-referenced proposed regulations. These comments broadly address the six areas of concern outlined in your letter dated June 20, 1988. They represent the individual views of the Committee members and do not represent the position of the American Bar Association or the Section of Taxation.

At the outset, we wish to emphasize that while we acknowledge the MTC's approach to adopt destination sourcing and minimal nexus rules for financial institutions, it is likely that taxpayers will continue to resist these policy changes. First, the adoption of minimal jurisdictional standards has yet to be constitutionally validated and, as such, is an area of great concern for financial institutions. Second, the proposed destination sourcing rules create potentially onerous compliance burdens from a systems perspective and may be administratively unworkable. We believe that these concerns would be shared equally by state tax administrators.

We appreciate this opportunity to comment on the proposed regulations and hope that we will have the opportunity to provide further input. In that regard, I look forward to meeting with you and representatives of the Uniformity Committee next week in Seattle. At that time,

Eugene F. Corrigan
Page Two

we will be able to further explore destination sourcing
rules from both a systems capability and business
operational point of view.

Very truly yours,



Philip M. Plant
Vice President &
Asst. General Tax Counsel
(415) 622-2877

Enclosure

mgd1:102:cnc

COMMENTS ON JUNE 20, 1988 GENE CORRIGAN LETTER

Prepared on behalf of ABA Tax Section, Committee on
Banking and Savings Institutions

1. Receipts Factor--Assignment of Service Fees.

The Uniformity Committee of the Multistate Tax Commission ("Committee") has proposed to designate nine categories of service fees with different sourcing rules. While this approach is instructive and gives the impression of great precision, the compliance problems associated therewith far outweigh any advantage to be gained. Moreover, it is illogical to apply different standards for separate items of income growing out of a single transaction as the proposed approach would do. Fees associated with a single transaction should be sourced under one rule.

We acknowledge the need to emphasize market states' contributions to profitability and understand the Committee's preference for a destination sourcing approach. It is our view, however, that such an approach is counterproductive in the fee generating area as evidenced by the complexity and compliance difficulties inherent in the proposed approach. Furthermore, it is unlikely that application of these rules would result in an attribution of service fees--or the ultimate sourcing of income--in a materially different fashion than would result from the use of more simplified rules.

In recognition of these concerns and in the interests of simplicity, we recommend reducing the number of service fee categories to the following five:

a. Loan fees. This would include loan service processing fees and points. Such fees should be assigned in the same manner as interest income associated with the loans.

b. Deposit fees. Deposit fees arising from both individual and corporate customers should be assigned based on the customer's mailing address. For many banks, certain extraordinary deposit fees (e.g., stop payment and NSF fees) are collected "manually" and are not captured or recorded on the particular deposit accounting system. Where this is the case, such fees should be subject to a "throwout rule" and excluded from both the numerator and the denominator of the receipts factor.

c. Trustee fees. It is illogical to source trustee fees from a living trust differently from other trusts and this distinction should be dropped. We recommend that all

trustee fees be assigned to the customer's residence (presumed to be the address to which its statement is regularly mailed).

d. Brokerage fees. In our view, the most logical approach would be to assign brokerage fees to where the account is maintained. If this is not acceptable under the market state approach, such fees could be sourced to the state where the order originated.

e. Other fees. Bearing in mind the above comments and the goals of simplicity and ease of compliance, we recommend that all other fees be sourced to the state where the services are performed. If such a rule is not acceptable, we recommend that all such fees be subject to the "throwout rule" described above. Adoption of a throwout rule for these fees would have no significant impact on a taxpayer's apportionment factors since such fees make up only a small portion of the total receipts.

2. Partnership Unsecured Indebtedness.

We agree with your concern that a "pass-through" approach to sourcing unsecured partnership debt for property and receipts factor purposes would create impossible compliance burdens for taxpayers. This approach is also unacceptable in the case of small partnerships, where residency information may not be contained on current bank systems. For that reason, we recommend the rejection of the proposal to create a de minimis rule which would apply where there are ten or fewer partners.

It is our view that partnership indebtedness should be treated in the same manner as corporate indebtedness and sourced to the "residence" of the borrower. Creating a differentiation between partnerships and corporations for attribution purposes could have an effect on the business decision of what form of entity to use. State tax concerns of the business' lender should not be a part of any such decisions. Lastly, we note that the abandonment of the passthrough approach for partnership unsecured debt is unlikely to have any material impact on a financial institution's apportionment factors.

3. Corporate Unsecured Debt.

The draft regulations would assign receipts from unsecured commercial loans to the borrower's "residence" which, in the case of a corporation, is presumed to be where the statement of account is regularly mailed. This approach is both workable from a systems perspective and

information not otherwise called for in the regulation, this approach is unnecessarily complex and burdensome.

As an alternative, we recommend that assets and receipts be assigned to the state where the greater portion of the investment activity is performed. Such a rule parallels the UDITPA sales factor rule for sales of intangible property contained in UDITPA §17 and further defined in MTC Reg. IV.17. Under that rule, sales, other than sales of tangible personal property, are attributed to the state if the income-producing activity is performed in the state. Where the income-producing activity is performed within and without the state, attribution is to the state where the greater proportion of such activity is performed based on costs of performance.

A throwout rule may be appropriate where the percentage of securities is minimal.

5. Government Obligations.

The provisions of the current draft regulation operate in such a manner that both foreign government lending by U.S. banks and lending to the U.S. government by foreign banks will be assigned, for the most part, outside the U.S. You have expressed concern because all such income and property will be excluded from the states' factors.

In our view, neither of the proposed solutions suggested in your letter is workable. The proposal to adopt a throw-out rule is problematical because it disregards significant values and would inflate the factors for large financial institutions which have substantial foreign government exposures.

As a solution to this problem, we recommend the following. First, the definition of "securities" in Paragraph (A)(3) should be amended to delete loans. As a result, paragraph (C)(2)(j) will no longer encompass foreign government loans. Second, the phrase "other securities" should be eliminated from Paragraph (C)(2)(k) as this phrase appears to be meaningless. Paragraph (C)(2)(k) should operate as a money market instrument rule only. Third, in keeping with the comments set forth above, the deposits ratio for assigning such receipts should be eliminated. In its place, we recommend the use of a greater portion of investment activity rule, as described in the previous comment.

6. Purchased Obligations.

As noted in your letter, the draft regulation does not address the question of the assignment of purchased obligations and such obligations would therefore be sourced under the general sourcing rules (i.e., to the location of property securing the debt or to the borrower's residence). It is our view that this is appropriate and that a separate rule for purchased obligations is unnecessary.

We do not share your concern that there may be constitutional nexus problems for states which do not provide a throwback rule. Whether a market state asserts its prerogative to tax the activities of a non-domiciliary financial institution should not affect any other states' taxing scheme. To conclude otherwise is to say that a market state may dictate the tax effect of an activity in another jurisdiction--a clear instance of extra-territorial taxation. This principle has been acknowledged in the UDITPA "throwback rule" context. For purposes of the UDITPA throwback rule, a taxpayer is taxable in another state if the state has jurisdiction to subject the taxpayer to tax regardless of whether the state does so in fact.

mgdl:100:sv

EXHIBIT B: 6

**Letter from Jim A. Peterson
(Moore Financial Group) (October 17, 1988)**

MOORE FINANCIAL GROUP

October 17, 1988

ADMINISTRATIVE OFFICE

Mr. Eugene F. Corrigan
Executive Counsel
Multistate Tax Commission
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024

Mr. Corrigan:

I received a copy of your September 2, 1988 letter to Berne Jensen of the Idaho Bankers Association. After reading the letter and discussing it with our tax advisors, I offer a few general comments.

Moore Financial Group presently files income tax returns in four states, Idaho, Oregon, Utah and California. We have recently purchased a bank in the state of Washington which does not have a corporate income tax. We have filed unitary in these states using a property, payroll and sales factor. Our general ledger system is set up on a cost center basis that enables us to track where property, payroll or sales are booked by state. This system allows us to prepare and file our state income tax returns efficiently without the use of an excessive amount of systems support, manpower and other administrative overhead. We also feel that the apportioned income to each state accurately reflects our presence in each state.

The issues in your letter, if implemented as written, would require significant additional manpower and systems support at Moore Financial to prepare our state income tax returns. In addition, we do not feel that our tax liability would materially change in the states we are presently filing in. We would also pay higher fees to our outside tax advisors to implement the regulations.

Moore Financial's position would be to apportion interest income and noninterest income to the state where the facilities and manpower were located that obtained the income. Moore Financial's general ledger reflects this position and we file our state income tax returns accordingly. If all other financial institutions filed under this method, we feel preparation costs would be minimal and all states would share tax revenues in an equitable manner.

All of my comments are general in nature. Before Moore Financial analyzes each of your issues in detail, and the MTC Financial Apportionment Regulations as a whole, we would like to know the status and timing of your proceedings on these regulations. I have spoken with Phil Aldape of the Idaho Department of Revenue and Taxation and he has indicated that he would like to meet with the Idaho banks on these issues. We plan to have a meeting with Phil and would also like to be included in any other proceedings and issues the Multistate Tax Commission is involved in with regard to financial institutions.

Mr. Eugene F. Corrigan
Page Two
October 17, 1988

If you would like to discuss my comments in more detail, please feel free to write or call me at Moore Financial Group, P. O. Box 8247, Department #3-2001, Boise, Idaho 83733, or phone (208) 383-7498. We appreciate the opportunity to comment.

Jim A. Peterson

Jim A. Peterson
Vice President

JAP:kp



Oregon League of Financial Institutions

1201 SW 12th Avenue, Suite 200
Century Tower
Portland, Oregon 97205
(503) 227-5591

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November 23, 1988

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Mr. Eugene F. Corrigan
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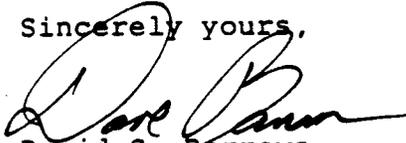
Dear Mr. Corrigan:

Enclosed you will find a letter written to me by the tax manager of the largest thrift institution in Oregon, with offices in three other states. I hope the information contained in this letter will be helpful to you in your deliberations.

Please let me know if we can be of any further assistance to you.

We are very grateful for the opportunity to comment on your proposal.

Sincerely yours,



David S. Barrows
President

Enclosure

David S. Barrows
President

EXHIBIT B: 7

**Letter from Robert W. Shank
(Benjamin Franklin Federal Savings and Loan Association)
(November 2, 1988)**



Benj Franklin

FEDERAL SAVINGS AND LOAN ASSOCIATION

BENJ. FRANKLIN FINANCIAL CENTER
501 S.E. HAWTHORNE BLVD.
PORTLAND, OREGON 97214-3598

November 2, 1988

Mr. David S. Barrows
Oregon League of Financial Institutions
1201 S.W. 12th Avenue
Portland, Oregon 97205

Dear Dave:

You have asked us for our comments on the proposed regulations of the Multistate Tax Commission dealing with the apportionment of income for multistate institutions. While there are several of the items in the proposed regulations that will not have a great effect on The Benj. Franklin, there are also several items that will be difficult to comply with, given the current information available to us.

Interest Attribution

We would have no problem complying with the interest attribution rules on any loan that we are currently servicing. However, we have been buying more loans than we originate, and do not service the purchased loans or participations. When we buy a participation in a group of loans, we receive a state by state distribution percentage as of the date of purchase. Currently, we continue to apply these percentages to the interest received on the participation, even though, as time goes on, this may be a less accurate indication of the actual loan balances in any given state. We receive no current "loan by state" percentages. It may be better from our point of view (and certainly easier) to treat participations as securities instead of as individual loans. This would allow us to use the "deposits ratio" approach to attributing both the income (for the gross receipts factor) and the asset (for the property factor). Since we have deposits in basically four states, this would attribute the income to just those four states, instead of the fifty states where the properties securing the loans are located.



Mr. David Barrows
November 2, 1988
Page 2

Property Factor

In reading the proposed regulations, an apparent area of potential problem is corporate or partnership unsecured indebtedness. At this point in time, this is not a big issue for us, but we are moving into the commercial loan area more aggressively, and find the problem of defining the borrower's residence (in the case of a corporation) or maintaining records of the residences of all the partners in a partnership a bit burdensome. We would prefer a simpler approach, such as attributing the loan and its interest to the state where the loan was originally made. An alternative would be to attribute the loan to the state having either the corporate office from which the loan application originated or the commercial domicile of the partnership.

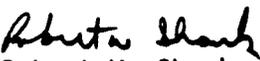
Even after reading the proposed regulations, I still have questions on how certain assets and their income should be attributed to a given state. We currently have several REMIC's and CMO's, the asset and the income on which we are currently attributing to Oregon for lack of any other guidance. Has the Multistate Tax Commission addressed some of the newer "securities" in the thrift industry?

Our largest concern if the proposed regulations are adopted as they stand is our risk of double taxation. Currently we are filing returns in mostly MTC states where there is not any doubling up on any of the factors. We are concerned, though, if we are required to file tax returns in many more states who are not members of the Multistate Tax Commission, that their particular attribution rules may cause receipts or assets to be counted twice, and thus subject us to double taxation. This is one reason why we would favor treating participations as securities subject to the deposits ratio attribution.

We would also like to minimize the complexity of recordkeeping involved to maintain the data needed to file complete and accurate tax returns under the proposed regulations. Our current systems would have to be expanded in order to produce the necessary data under the new regs. And as I stated earlier, we do not currently have all of the information available to us which we would need to comply with the proposed regs.

If you have any questions or comments on this letter, or want to discuss any of these areas further, please contact me.

Very truly yours,


Robert W. Shank
Tax Manager

RWS/rp

EXHIBIT B: 8

**Letter from Sheila J. Slaughter
(California League of Savings Institutions)
(November 11, 1988)**



**CALIFORNIA LEAGUE OF
SAVINGS INSTITUTIONS**

November 11, 1988

Mr. Eugene F. Corrigan
Executive Counsel
Multistate Tax Commission
1790 - 30th Street, Suite 314
Boulder, Colorado 80301-1024

Re: Proposed Regulations for the Attribution
of the Income of Financial Institutions
(Draft of July 1987)

Dear Mr. Corrigan:

The California League of Savings Institutions (League) appreciates the opportunity to once again provide the Multistate Tax Commission (MTC) with its views on the MTC's Proposed Regulations for the Attribution of the Income of Financial Institutions (Draft of July 1987) (Regulations). As you may recall, the League previously commented on a limited number of technical and administrative issues raised by the prior draft of the Regulations.

While the following comments are intended to be responsive to the specific issues raised in your letter of June 29, 1988, the League does wish to take this opportunity to express its concerns with the destination sourcing approach that underlies the Regulations. In an area as complex as the apportionment of income from multistate operations, particular care needs to be given to adopting an approach that is administrable for the taxpayer and taxing agencies alike. As will be discussed below, the League believes that most of the problems raised in your letter relate directly to the destination sourcing approach underlying the Regulations.

We think it is important to stress, however, that the comments set forth hereinafter are not based on the League's philosophical objections to destination sourcing, but rather reflect the concerns of its members that such an apportionment is generally difficult to apply in practice and represents a dramatic departure from the way that corporations with multistate operations are currently taxed. As such, the implementation of the Regulations by less than a substantial majority of the states is virtually certain to result in financial institutions being subject to conflicting state tax claims on amounts that exceed their actual income.

The foregoing concern is based to a substantial degree on the perceptions of our members regarding the situation in California. California has informally indicated that it is currently undecided as to whether a money center or market state approach most accurately allocates income to California, and that it is likely to adopt the approach that best

serves its objectives regardless of whether it conforms with the approach adopted by the MTC. We have recently heard suggestions that California is actively considering adopting an intermediate approach under which destination sourcing would only be applied to the interest on loans secured by tangible property, and current sourcing rules would continue to apply to all other types of income. The League would strongly support this type of approach over that currently contained in the Regulations, both because it addresses the two principal concerns of our members, administrative feasibility and avoidance of conflicting state claims, and because it results in the apportionment of the income of financial institutions to those states that provide such institutions with meaningful services and projections.

In the area of service fees and receipts, the League is particularly concerned about the wisdom of treating financial institutions differently from other service providers. Our members can see no legally meaningful distinction between the role they play in providing services to their customers and the role played by non-financial institutions in providing services to theirs, and therefore see no basis for abandoning the well established and easily administered rule that service charges should be attributed to the state in which the services are performed. Destination sourcing of service fees raises problems of administration that could cause compliance costs to exceed the tax revenues received by the market states, due in large part to the need for financial institutions to accumulate and/or process data not currently required in order to conduct their businesses and comply with existing tax laws, without any assurance that such approach would, over time, either attribute significant additional income to market states or produce a result that is more clearly reflective of their true income.

Most of the League's members do not have out-of-state operations, but would, nevertheless, be required to apportion income to market states under the nexus standards in the Regulations. Even those institutions that engage in substantial multistate operations, and that would save taxes under an approach that apportions income away from high tax states like California to lower tax market states, have expressed severe reservations with the administrative problems created by destination sourcing. The League questions the wisdom of an apportionment approach that is likely to distort business decisions and dramatically add to the burdens of tax administration in the absence of an overriding public policy justification.

A. Receipts Factor -- Assignment of Service Fees

1. Deposit Fees. The approach to the apportionment of deposit fees suggested in your letter points out a basic concern raised by a number of the proposals for sourcing service fees - the use of different rules for different classes of customers. The use of separate rules for individuals, corporations and other entities requires each financial institution's data processing systems to differentiate between categories of customers based on criteria that is not currently utilized for most business and tax purposes. With respect to existing accounts, this may be impossible to do based on the information currently in the institution's files, and would require the institution to acquire, retain and process a substantial volume of additional information with respect to future accounts. While the League's members favor retention

of the current approach of assigning deposits to the office where they are maintained for administrative reasons, if a destination sourcing approach to apportionment is to be utilized, all accounts should be sourced in the state to which the customer's statement is regularly sent. The League believes that the MTC's concerns about tax avoidance in connection with corporate accounts are overstated with respect to financial institutions in general, and are clearly inappropriate with respect to its members, most of which have a relatively small percentage of corporate deposits.

2. Points. Conceptually, points are part prepaid interest and part loan origination fees and expense reimbursements. As such, under a destination sourcing approach, your suggestion that they be apportioned in the same manner as the loan to which they relate has some theoretical support. Unfortunately, however, such an approach disregards the manner in which points on mortgage loans are handled by thrift institutions. Most thrifts treat points on a pooled basis and recognize income thereon for both book and tax purposes over the life of the loan. For tax purposes, points are generally taken into income using methods such as the loan liquidation or the composite average life method. These deferral methods generally look to the aggregate amounts of deferred points and the aggregate principal balance of the related loans, but do not attribute points to specific loans. For this reason, it would be impossible for our members to directly apportion points to the states to which the Regulations require interest income on the related loan to be sourced.

As an alternative, the League suggests that the MTC permit lenders to allocate the annual amount of points taken into income based on the year and principal balances of the outstanding loans attributed to each state under the normal rules, or in the alternative, to exclude points from consideration. The latter approach is clearly the easiest to administer, and should result in an allocation that approximates, in most cases, the result that would be produced by your suggested loan by loan allocation.

3. Loan Service Processing Fees. The League believes that as a business matter a portion of the interest received on each loan originated by a financial institution is properly allocable to servicing the loan. However, mortgage lenders almost never charge a separate fee to borrowers to service a mortgage loan, and the League thus feels it is administratively appropriate to ignore this imputed charge and treat all interest payments as "interest" for apportionment purposes as long as the originating institution holds the loan. A similar approach also seems appropriate where a financial institution purchases a loan on a "servicing released" basis (i.e., where the originating lender doesn't continue to service the loan for a fee). We assume that this is the approach currently favored by the MTC.

As regards servicing fees received by a financial institution that does not hold the related loan, no distinction should be made between purchased servicing rights and rights retained upon the sale of loans originated by the servicer. Consistent with its general position on the sourcing of fee income, the League favors a rule that allocates such income to the state in which the office that collects the loan payments is located. If, however, the MTC is committed to sourcing fee income where the "benefits" of the services are received, the first order of business is necessarily to determine the party that benefits from the loan servicing performed by the financial institution. We believe that

it is indisputable that loan servicing primarily benefits the owner of the loan rather than the obligor, and that a destination sourcing approach therefore requires that such fees be sourced in the state in which the owner of the loan resides, and not in the obligor's state of residence. Furthermore, as discussed above, regardless of whether the owner is an entity or an individual, the fees should be sourced in the state to which the servicer regularly remits payments of principal and interest to avoid severe administrative problems.

The presence of a massive secondary market for mortgage loans and mortgage backed securities raises an additional complicating factor in designing a workable apportionment rule based on destination sourcing concepts, since it is often impossible for the servicer to determine where the owners of a pool of mortgages reside. With respect to a large percentage of privately packaged mortgage securities, brokerage firms distribute the securities to their customers and the servicer remits payments to the broker. A similar problem exists in the "agency" market (i.e. , loans packaged and sold through FNMA, FHLMC and GNMA), where the servicer remits payments to the agency and not to the ultimate holder of the loan participation certificate. Because of these problems, the League sees no feasible alternative to sourcing mortgage servicing income in the states to which payments of principal and interest are remitted.

4. Check Processing Fees. Since thrift institutions do not currently process checks, the League does not feel it appropriate to express a view on this particular issue. The League does feel, however, that many of the same types of issues are raised by the apportionment of fees for handling transactions at automated teller machines (hereinafter "ATMs"). Relatively few thrift institutions charge their own customers for using their ATM's, but most charge other institutions a service fee when their customers use the institution's ATMs. In some cases, this fee is passed on by the payer to its customers, and in some cases it is absorbed by the payer as a cost of doing business. Regardless of how the fee is handled by the payer, the institution charging the fee typically knows only the name and card number (but not the address) of the person using the ATM and the name and billing address of the institution that issued the card. The League therefore feels that these fees should be treated in the same manner as interest income and other receipts from credit cards, i.e. , attributed to the state to which the fees are regularly billed.

5. Check Charges, Trustees and Brokerage Fees. As discussed above with respect to deposits, the League is vigorously opposed to the use of different sourcing rules for individuals and corporations and other entities, and thus sees no justification for extending this approach to grantor and non-grantor trusts. If the MTC is unwilling to source these fees to the place where the services are performed, they should be sourced in the states to which the financial institution regularly sends its fee statements, regardless of the customer's form of organization.

6. Guarantee Fees. When a financial institution guarantees a note, it is providing a service to the borrower, since the guarantee enhances the borrower's creditworthiness and presumably provides a direct benefit (e.g. , qualification for the loan, lower rates, more favorable terms, etc.) to the borrower. As such, under a destination sourcing approach such fees should be sourced in the state where the borrower

resides, and not in the state where the interest on the related note is sourced.

7. Other Fees. As noted above, the League believes that the appropriate treatment of fees for services rendered to customers is to source them where the services are performed. The rapid increase in the number of and types of fees being charged by financial institutions makes it imperative that the MTC adopt sourcing rules that treat true fees (as opposed to disguised interest charges or charges that are, in reality, for the use or forbearance of money) in a consistent manner. If destination sourcing is to be applied, the MTC should adopt a uniform "statement" rule that sources fee income in the state to which statements are regularly sent.

B. Partnership Unsecured Indebtedness

The League opposes any look-through rule, regardless of whether the partnership involved has two partners or thousands of partners, due to the tremendous administrative burdens that such an approach would place on lenders. Furthermore, almost all unsecured loans to partnerships are for the purpose of acquiring business or investment assets, or meeting the cash flow needs of an ongoing business. For these reasons, the League feels it appropriate to source unsecured partnership debt in the state where the partnership maintains its commercial domicile which, absent evidence to the contrary, would be presumed to be the place to which the financial institution regularly sent its statements.

C. Corporate Unsecured Debt

The League similarly favors the "statement" rule as being the only administratively feasible way to source unsecured corporate debt. The suggestion by some of the member states that the MTC return to the approach of sourcing unsecured debt to the location where the loan proceeds are applied totally ignores the realities of the business world, both from the perspective of the lender as well as that of the borrower. Putting aside the immense administrative burden that would be imposed on lenders if they are required to solicit information from their borrowers as to the application of loan proceeds, such an approach ignores the fundamental fact that money is fungible. For the great majority of corporations, it would be virtually impossible for them to determine the states in which specific borrowings were expended.

The League applauds the desire of the members of the MTC Uniformity Committee to adopt an apportionment rule that focuses on a single identifiable event bearing a logical relationship to the lending activity. The League does not believe, however, that it is appropriate for the MTC to place so much emphasis on the possibility that the sourcing rules might be manipulated that it adopts rules that serve little purpose other than to prevent such manipulation. On a related point, we were confused and troubled by the suggestion that a Form 1099 type of reporting might be required in order for state taxing authorities to determine on audit the states to which customer statements were mailed. The League believes that the use of certifications would substantially increase the paperwork involved in processing loan applications and would increase, rather than decrease, the opportunity for manipulation. Our members continue to feel that it is entirely appropriate and con-

sistent with normal tax auditing procedures, to obtain this type of information from the books and records of the lending institution and, where appropriate, to obtain representations from responsible corporate officers as to the accuracy of such records.

In your letter, you suggest that most of the Committee members favored sourcing unsecured corporate loans in the state in which the responsible office of the borrower is located. Since most major borrowing decisions are made in the headquarters office of the borrower, the League believes that in most cases such a rule is likely to source the loan in the same state as a statement rule. As regards the proposed fallback position of sourcing the loan to the office of the lender that was primarily responsible for its origination, as noted several times above, the League is clearly in favor of this type of rule. The League nevertheless remains concerned about the administrative burdens of requiring financial institutions to apply alternative sourcing rules to a single class of income.

D. Assignment of Receipts from Securities -- General Rule

The League agrees with those members of the Committee who do not feel it appropriate to resurrect a deposits factor solely for the purpose of sourcing the income from certain types of investments such as securities. The League favors a rule that would source the income from securities in the state of the financial institution's commercial domicile (the same rule applied to non-financial companies) or, as suggested by other members of the Committee, to throw out the receipts from securities for apportionment purposes.

E. Government Obligations

In view of the special problems created by U.S. and foreign government securities, the League agrees with those members of the MTC that favor a throw-out of the income from such securities. Where state and local government securities are involved, however, the use of a commercial domicile rule seems clearly justified and easy to administer.

F. Purchased Obligations

The purchase of secured debt by thrift institutions is a common practice, especially pools of residential mortgage loans. As discussed above in connection with loan service processing fees, much of the market in mortgage loans involves the purchase and sale of mortgage participation certificates and mortgage-backed securities. Typically, these securities are either acquired in the market (e.g., "publicly traded" securities registered by the issuer with the SEC or other governmental agency, or "agency" securities, such as those issued by GNMA, FNMA or FHLMC) or in privately negotiated transactions entered into with other financial institutions. In the former case, the securities are generally purchased based on their credit rating and not based on any detailed underwriting by the purchaser with respect to the underlying loans. Furthermore, specific information as to the location of the properties securing the loans, while retained by the loan servicer, is generally not readily available to the purchaser. Conversely, in privately negotiated transactions, it is common for the purchasing institution to thoroughly underwrite the loans in the pool and information on the location of the

Eugene F. Corrigan
Multistate Tax Commission
November 10, 1988
Page 7

properties securing the loans is generally readily available from the servicer.

The League believes that the sourcing rules applied to purchased loans should reflect the foregoing commercial realities, and that publicly traded mortgage securities should therefore be treated in the same fashion as other types of securities. Where loans are purchased in privately negotiated transactions, however, regardless of the form utilized (e.g. , participations, whole loans, etc.), it is reasonable to source the income from such loans as if the loans had been originated by the purchaser - i.e. , to require the purchaser to allocate income to the states in which the related security is located. In order to achieve this result, it will be necessary to revise the definition of a security currently contained in the Regulations to limit its coverage to publicly traded mortgage securities.

F. Prospective Application of Regulations

Regardless of the manner in which the specific problems raised by the current draft of the Regulations are resolved, it is clear that the final Regulations will represent a marked departure from the current apportionment rules applicable to financial institutions. The League therefore strongly urges that the final Regulations not be applied on a prospective basis sooner than the start of the second taxable year following their promulgation, and that transactions that occur prior to such promulgation be grandfathered in circumstances where the Regulations require income to be apportioned based upon information that was not obtained by the institution at the time of the transaction, or was not retained in a form that makes it reasonably accessible. Anything less would deny financial institutions the basic administrative due process to which they are entitled.

The foregoing comments were prepared by the members of the Tax Issues Committee of the League. The Committee would welcome the opportunity to meet with the MTC staff if that would further the process of developing the Regulations. Please feel free to contact Michael J. Palko of Great Western Bank, Phone: 213/852-3349, for further assistance or for any questions regarding this letter.

Very truly yours,


Sheila J. Staughter
General Counsel and
Senior Vice President

SJS:jer

EXHIBIT B: 9

**Letter from Albert A. Wolf
(Wheeler, Wolf, Peterson, Schmitz, McDonald & Johnson)
(November 14, 1988)**

Wheeler, Wolf, Peterson, Schmitz, McDonald & Johnson

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November 14, 1988

Eugene F. Corrigan
Executive Counsel
Multistate Tax Commission
1790 30th Street, Suite 314
Boulder, CO 80301-1024

Re: Pending Banking Regulation Matters

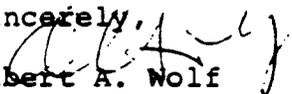
Dear Mr. Corrigan:

I have reviewed your letter to Arlene Melarvie, Independent Community Banks of North Dakota, dated October 7, 1988, regarding the MTC draft financial apportionment regulations.

While we have followed the implementation of the tax consequences of a bank merger bill in North Dakota recently, we have not had occasion to consider the ramifications of the interstate banking activities. Without attempting to comment on each of the items considered, I would hope that the residence of the customer making the loan would predominate in a decision-making process as to which bank facility should be credited with the transaction, and which state should be allowed to impose a tax.

Secondly, the location of the facility where checking and other accounts may be maintained should again be primarily considered as the location where taxes can be imposed. Out of necessity, the banking institution may be relied upon to make an allocation of bank activity or profits to the various locations, recognizing that this may be somewhat arbitrary at times. The use of a pro forma income tax return based on the bank's determination of income and expense allocated to each facility could form the basis for further clarification and application of the location where the tax may be imposed.

If there are specific areas of inquiry that we could be of assistance with, please advise.

Sincerely,

Albert A. Wolf

dt

cc: Arlene Melarvie

EXHIBIT B: 10

**Letter from Richard L. Sprunger
(California Federal Savings and Loan Association)
(November 16, 1988)**



5670 Wilshire Boulevard
Los Angeles, California 90036
Telephone 213 932 4151

November 16, 1988

Eugene F. Corrigan
Executive Counsel
Multistate Tax Commission
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024

Re: July 1987 Draft of the Proposed Regulations for the
Attribution of the Income of Financial Institutions

Dear Mr. Corrigan:

California Federal Savings and Loan Association appreciates the opportunity to provide its comments on the July 1987 draft of the Proposed Regulations for the Attribution of the Income of Financial Institutions.

Prior to addressing the specific issues raised in your letter dated June 29, 1988, we feel that it is necessary to comment on the underlying sourcing rules on which the system of apportionment in the proposed regulations is based.

A workable system of apportionment must reconcile several competing concerns: (1) taxpayer's desire to control and manage its overall state tax liabilities and avoid double taxation (2) desire of the various states to get their "fair share" of overall state tax revenues, and (3) elimination of any excessive administrative burdens and resulting costs imposed on both taxpayers and the states in complying with an apportionment formula.

To be perceived as "fair" by states and taxpayers alike, a system of apportionment must balance these competing concerns. The system of apportionment in the proposed regulations is based on destination sourcing. Destination sourcing, in our opinion, cannot balance the competing concerns mentioned above because:

(1) Destination sourcing is heavily biased in favor of consumer states as opposed to money center states. As a result, MTC member states which view themselves as money center states appear to be in direct conflict with consumer states and may refuse to adopt the regulations, thereby exposing the taxpayer's income to double taxation.

(2) Destination sourcing will conflict with pre-existing sourcing rules in use by some nonmember states. Therefore, taxpayers could be subject to multiple state taxation on the same activities.

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(3) Destination sourcing appears to inhibit a taxpayer's ability to control tax liabilities in those states which establish nexus and determine tax liability based on the consumer's activities and would greatly increase the administrative costs in collecting data and maintaining adequate records to satisfy the resulting reporting that would be required under the proposed regulations.

Under any sourcing system, the administrative burden placed on both the taxpayer and the state is reduced if an apportionment rule is linked to a single identifiable event that bears a logical relationship to the service being provided by the taxpayer. The identifiable event should not be capable of undue manipulation by the taxpayer but should also not penalize the taxpayer. In addition, the identifiable event should not be subject to manipulation by third parties which would increase the administrative burden to the taxpayer and cause uncertainty with respect to reporting requirements.

Destination sourcing which looks to the location of the customer activity or to the customer's residence or the customer's statement mailing address will invariably produce high administrative costs and reporting uncertainties because it places in the control of the customers the factors that determine the taxpayer's reporting requirements. The location of the customer activity or the residence or mailing addresses of the customer may bear no logical relationship to the activity performed by the taxpayer nor the benefit derived by the consumer and monitoring these factors will greatly increase both the taxpayer's and the state's compliance costs.

For these reasons, we believe that destination sourcing is generally inappropriate as the primary conceptual basis for a system of apportionment for financial institutions.

As an alternative to destination sourcing, consideration should be given to developing sourcing rules which source income in the state in which the taxpayer performs its activities. Since financial institutions are primarily providers of services, it is logical to establish nexus and be subject to tax in the jurisdiction in which those services are performed by the financial institution. Under such a system, apportionment would be based upon where expenses generating the income are incurred. Such a system would be much easier and less costly to administer and would provide much greater certainty in identifying those jurisdictions in which the activities of a financial institution would be taxable.

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Consideration should also be given to whether the three-factor apportionment formula is appropriate for financial institutions. A single factor formula which apportions income to those states in which the taxpayer performs activities as measured by the incurrence of operating expenses would appear easier to administer and may, because of the service-intensive nature of the financial services industry, provide a more equitable result not significantly different from the more complex three-factor formula.

Unlike the manufacturing industry in which the primary source of income is typically sales of finished products and which may result in manipulation of apportioned income resulting from distinct facilities for production, storage, sales and administration, income in the financial services industry is generated by many different types of services each of which may be traced to a specifically identifiable and self-contained location. Therefore, use of a three-factor formula may do little more than provide an element of redundancy in the apportionment of income.

The following comments regarding the specific issues which you raised in your letter reflect our preference for a system based on sourcing in the state in which the taxpayer incurs expenses in performing its activities, (hereinafter referred to as "origination sourcing"), rather than a system based on destination sourcing.

1. Receipts Factor

a. Interest on loans. Although you have not asked for specific comments on the apportionment of interest income, you have suggested that several items could be treated in the same manner as interest on loans. As indicated above, we would prefer an overall system based on origination sourcing. Under such a system, interest income on loans originated by the taxpayer, whether secured or unsecured, could be sourced in the state in which the loan was originated (i.e., the state in which is located the office through which the customer initially applied for the loan). Interest income on purchased loans, however, would be sourced in the state in which the taxpayer's office through which loans are purchased is located because that would be where the expenses supporting such activity are incurred.

b. Deposit fees. The proposed regulations have raised the issue of the use of different rules for different classes of accounts. Identification of the different proposed classes of customers would not create an additional administrative burden because current federal information reporting regulations impose a similar requirement. Additional administrative expense would be incurred, however, in capturing the fee detail relating to each account.

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Even if the issue of additional administrative burden is disregarded, there is no apparent justification for treating different classes of accounts differently. Unless a logical justification can be found, all classes of accounts should be treated in the same manner.

Assuming that all accounts are to be subject to the same sourcing rules, we would prefer a system based on origination sourcing. Under such a system, deposit fees should be sourced to the state in which the account is maintained because that is where the expenses supporting the taxpayer's activities generating the income are performed.

Destination sourcing in which the customer's residence is used to determine source clearly exposes the taxpayer to taxation in states which may otherwise have no logical nexus to the taxpayer's activities. For instance, an individual who is a resident of a state having no nexus with the taxpayer's activities could come into the taxpayer's state and for many different reasons, (e.g., vacation travel), open an account at the taxpayer's local office. Under a sourcing rule assigning fees on the basis of the customer's residence, the taxpayer would assign the fees to the customer's state of residence and the taxpayer would presumably be taxable in that state even though it conducts no business activity in the state and did not solicit the account in that state. The taxpayer would incur significant administrative costs in attempting to monitor the customer's state of residence. Effectiveness in monitoring changes in residence would depend entirely on the customer's willingness to provide such information to the taxpayer. If customers do not cooperate, assignments could quickly become inaccurate as customers change states of residence, and as a result apportionment factors could quickly become distorted. In addition, the taxpayer would incur additional compliance costs in preparing and filing returns in the customer's state of residence. The taxpayer's only method of avoiding additional state compliance costs would be to refuse to open accounts for customers who reside in states which currently have no nexus to the taxpayer's activities. This would not only be contrary to the functions which the taxpayer was chartered to perform but may be in violation of Federal law and have a chilling effect on interstate commerce and interstate travel.

Destination sourcing in which the customer's statement mailing address is used would impose a lesser administrative burden than residence-based destination sourcing because the customer would normally inform the taxpayer of changes of address to continue receiving statements. This would, in turn, lead to greater accuracy in the assignment of fees to the proper states than a residence-sourced system. A mailing address sourcing would, however, contain the same limitations on the taxpayer's ability to control nexus and could raise the same constitutional issues regarding violations of Federal law and impact on interstate commerce and travel.

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Under origination sourcing, deposit fees would be assigned to the state where the costs are incurred to maintain the account and process the customers activities with respect to the account. This would be clearly preferable to either a residence-based or a mailing address-based system because (1) administrative costs would be significantly lower, (2) the taxpayer has greater control over states having nexus to the taxpayers activities, and (3) actions by customers which have no relationship to the taxpayer's activities will have no impact on the taxpayer's reporting requirements and resulting state tax liabilities.

c. Points. For income recognition purposes, financial institutions frequently aggregate and amortize points as part of a pool rather than track the points on a loan-by-loan basis. As a result, although the proposal to assign points in a manner consistent with the assignment of interest on the loan may be theoretically sound, it is unworkable in practice and would cause financial institutions to incur a significant administrative cost to develop systems that could track points on a loan by loan basis. In addition, there is a conceptual difference between interest and fees in that fees generally relate to the costs incurred in the loan origination process whereas interest primarily relates to the investment of debt proceeds with minimal on-going operating costs.

As an alternative, lenders should be permitted to allocate the amount of points taken into income under the lender's income recognition method based on the principal balances of the outstanding loans attributed to each state. For this purpose, loans should be sourced in the same manner as interest on loans, as discussed above. Regional variations due to differing market conditions or promotional rates would, over time, probably tend to disappear and would therefore cause no significant distortion of income to the various states.

d. Loan Service Processing Fee. A loan service processing fee arises out of the right to service loans rather than out of the lending activity that created the loans. Residence of the borrower, location of any security for the loan, and residence or commercial domicile of the holders of the notes have no impact on where the taxpayer performs its servicing activities and, therefore, should be irrelevant to sourcing the servicing fees. The only factor which should be considered in sourcing the fees is the location of the office of the servicer at which the servicing function is performed as servicing is the sole activity producing the fees.

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If the destination-sourcing goals of the proposed regulations are adopted, the proposal to assign fees arising from servicing rights acquired from other note holders to the state of the commercial domicile of the holder would require the capture of information not normally captured on a loan-by-loan basis by the servicer, especially in large loan pools which are common in the mortgage securities industry. Under the proposed regulations, the servicer would also lose control over the states which would have nexus to the servicer's activities if the holder with whom the servicer contracted subsequently transfers the loans to another holder in a different state. In that situation, the servicing fees would be assigned to the subsequent holder's state and the servicer would become subject to tax in that state even though the servicer took no action which would have directly subjected it to taxation in the subsequent holder's state. Furthermore, assignment to the state in which the holder is located may make it difficult for holders of small quantities of loans to find out-of-state servicers willing to assume the servicing on such loans because, if the servicer is not already taxable in the holder's state, the servicer's compliance costs for that state may be greater than the anticipated fees to be earned. In that situation, the servicer may have to either refuse to accept the servicing or charge a fee that could make mortgage loan investment unprofitable for small holders.

The alternative which is the simplest to administer, provides the most consistency and predictability to both the states and the servicer, and does not act as a restraint on business to either the servicer or the holder is to assign servicing fees to the state in which the office of the servicer at which the servicing function is performed is located.

e. Check Processing Fees. Such fees should be sourced in the state in which the processing services are performed as such services are the primary activity generating the fee income.

Sourcing based on the location of the branch of the customer at which the checking accounts are maintained could create a significant administrative burden and may have no logical relationship to the activity being performed.

f. Check Charges. These fees should be sourced in the same manner as deposit fees. No distinction should be made between types of accounts and fees should be assigned to the state in which the account is maintained.

g. Trustee Fees. The proposal would assign fees from living trusts to the state of residence of the grantor, while fees from all other trusts would be assigned to the state in which the trust is administered.

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Creation of two such classes of trusts would create an additional administrative burden for the trustee and has no logical justification as living trusts are considered to be separate legal entities for most purposes other than income tax reporting. Trusts, whether living, testamentary, or of any other kind, are generally administered in the state under whose laws they are formed and where most of the tangible assets tend to be located. Consequently, trustee fees should be assigned to the state in which the trust is administered, regardless of the type of trust or the residence of the grantor. In addition, it is logical to assume that the benefits of the administration provided by the corporate trustee are received in the state of administration. Therefore, such assignment satisfies both destination-sourcing goals and origination-sourcing goals.

h. Brokerage Fees. These fees should be treated in the same manner as deposit fees. No distinction should be made between type of accounts and fees should be assigned to the state in which the account is maintained or to the state in which the office performing the brokerage activity generating the fee income is located.

i. Guarantee Fees. Under a system based on origination sourcing, guarantee fees should be assigned to the location of the office of the financial institution at which the customer initiated the request for the guarantee.

Under a destination-sourcing system, it could be argued that the benefit of the service is realized in any of several locations - including the residence of the borrower, the residence of the holder of the note being guaranteed, or the location at which the funds being obtained by the borrower will be expended - none of which may bear any logical relationship to the activity being performed by the financial institution.

j. Other Fees.

Loan Origination Fees. These fees which are charged to customers in addition to points are generally accumulated in pools and recognized as income through a loan liquidation method, similar to points. As a result these fees should be treated in the same manner as points and, unless an origination sourcing concept is adopted, assigned to states based on the principal balances of the outstanding loans attributed to each state at year-end.

ATM Transaction Fees. These fees should be treated the same as deposit fees and assigned to the state in which the account is maintained.

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A system using destination sourcing, whether based on the residence of the customer or the state in which the transaction giving rise to the fee occurs, would expose the taxpayer to unnecessary administrative burden and uncertainty regarding the taxpayer's reporting requirements. For instance, if a resident of Oregon opens an account at a financial institution in California and subsequently uses the ATM card in a transaction in Nevada which generates a transaction fee (e.g., uses the card for a cash withdrawal at the ATM of a different financial institution who participates in a national ATM system network), the ultimate benefit of the transaction may arguably occur in one of several different places including: (1) Nevada, where the transaction occurred (this result would create an overwhelming burden on the financial institution to try to source each ATM fee in the state where the transaction took place), (2) the residence of the customer (which has no apparent relationship to this transaction), or (3) in California where the activities are incurred to process the interbank settlement and charge the customer's account.

Under a system based on origination sourcing, any transaction fees would be assigned to the office of the financial institution where the account is maintained (where the ultimate liability falls on the financial institution to honor the ATM transaction, charge the customer's account and process the interbank settlement to make reimbursement to the Nevada institution which honored the original ATM transaction). Clearly, this alternative is the simplest to administer, bears the most direct relationship to the activity performed by the financial institution, and provides the greatest reporting certainty.

Other Fees. As a general rule, it will be appropriate to source other miscellaneous fees to the state in which the services are performed. Destination sourcing based upon either the customer's residence or the customer's mailing address is inappropriate as it is administratively impractical and exposes the financial institution to continuing uncertainty as to which states in which it may be required to file returns.

2. Unsecured Debt.

a. **Partnership Unsecured Debt.** As discussed above, interest and related fees on unsecured debt or debt secured by moveable security should be assigned to the state in which is located the office of the taxpayer or its agent in which the taxpayer's agent, loan officer or comparable employee responsible for making initial contact with the borrower for purposes of making or soliciting the loan is located, or if the agent or employee does not operate from an office, the office at which such loan

Eugene F. Corrigan
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will be administered. The proposal to assign the loan to the state of residence of the employee or agent in the absence of an office creates an unnecessary administrative burden and subjects the taxpayer to taxation in a state for reasons that are unrelated to the activities of the taxpayer and outside of the control of the state. For example, if a loan agent resides in Delaware and his only business for the financial institution is the solicitation of loans in Connecticut, all such loans would be assigned to Delaware and the financial institution would be subject to taxation in Delaware. If, in the following year, the agent moved to Rhode Island, but his only business for the financial institution again consists of soliciting loans in Connecticut, the loans solicited that year would be assigned to Rhode Island, and the financial institution would be subject to taxation in Rhode Island. Such exposure would occur without any action on the part of the financial institution, such as qualifying to do business in Rhode Island or recording security interests in Rhode Island. Furthermore, there have been no actions taken which would provide Rhode Island with any independent means of being on notice that it may be entitled to tax receipts from the financial institution.

b. Corporate Unsecured Debt. Corporate unsecured debt should be assigned in the same manner as partnership unsecured debt, for the same reasons discussed above.

c. Individual Unsecured Debt. Individual unsecured debt, whether in the form of credit cards, lines of credit, consumer loans or installment loans, should be assigned in the same manner as partnership debt, for the same reasons discussed above.

3. Assignment of receipts from securities. If it is the intent of the Committee to eliminate the use of a deposits factor, it would seem unnecessarily burdensome to require financial institution to continue to calculate a deposits factor in order to assign receipts from securities. Therefore, we would favor a rule that would source income from the securities in the state of the financial institution's commercial domicile. In the alternative, income from securities could be eliminated from the apportionment factor.

4. Government Obligations. Income from such securities should be assigned in the same manner as all other securities, as discussed above.

5. Purchased Obligations. The purchase of secured debt has become very common with the growth of the mortgage-backed securities industry and continuing interest in the purchase and sale of whole loan portfolios. Because these types of obligations are purchased based on the overall

Eugene F. Corrigan
November 16, 1988
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credit rating and assessment of risk of the entire pool rather than July specific knowledge of the characteristics of the underlying loans, assignment for purposes of the receipts factor and the property factor based on location of the underlying security would be administrative burdensome and could be prohibitively expensive. In addition, such a rule could subject the taxpayer to taxation in a state simply because a large pool contains a loan secured by property located in that state even though the taxpayer did not actively seek to acquire loans secured by property in such state.

We suggest that purchased obligations and the interest therefrom be assigned to the state in which is located the taxpayer's office which was responsible for the acquisition of the purchased obligations as that is the location at which the primary activity resulting in acquisition of the obligations and the resulting income streams occurred. Such treatment would be consistent with the manner in which originated secured loans and the interest therefrom are treated.

We would welcome the opportunity to discuss these comments with the MTC staff. Please do not hesitate to contact us if we can be of any further assistance in development of the proposed regulations.

Very truly yours,

Richard L. Sprunger

Richard L. Sprunger
Vice President
Director of Tax Research

cc: Mr. James R. Wegge, Jr.
Senior Vice President
California Federal Savings
and Loan Association

088804

EXHIBIT B: 11

**Letter and Minutes from Philip M. Plant
(Bank of America) (December 30, 1988)**



TAX DEPARTMENT
(415) 622-2877

PHILIP M. PLANT
Vice President and
Assistant General Tax Counsel

December 30, 1988

Eugene Corrigan, Esq.
Multistate Tax Commission
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024

Alan Friedman
386 University Avenue
Los Altos, CA 94022

RE: Consolidated Minutes of Meeting Between MTC and
Bank Representatives in Seattle on October 21, 1988

Dear Gene and Alan:

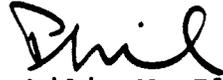
Enclosed is a draft consolidation of Gene's minutes and my November 2, 1988 draft minutes of the above captioned meeting. Both versions have for the most part been retained and blended together following a process of correcting discrepancies and inserting updates to alert you to certain instances in which our representations were since discovered to be inaccurate in some respect. I apologize for the tardiness of this submission. It took me longer to get all the bank group participants to comment on Gene's minutes than I expected.

I hope you find the minutes acceptable as a consensus approximation of what transpired at the meeting. I confess that my recollection of events has dimmed to the point that any further tinkering with these minutes would represent an attempt to clarify what I now think was intended to be said rather than what might have actually been said.

I am now turning my attention to formulate proposed amendments to the regulations to conform to the suggestions identified in the minutes. I will also be drafting a survey questionnaire to gather the data which has been identified in the minutes as requested by you. I will run a draft of the questionnaire by you to determine whether it will produce the data you have in mind.

I hope to have the draft amendments to the regulations to you by the end of January. Please advise if you have a problem with this. In the meantime, have a happy and fulfilling new year.

Sincerely,

A handwritten signature in cursive script that reads "Phil".

Philip M. Plant

pmp1:095:cnc

CONSOLIDATED
MINUTES
OF
MEETING
BETWEEN MTC AND
BANK REPRESENTATIVES
IN SEATTLE
ON
OCTOBER 21, 1988

These consolidated minutes summarize the matters touched upon and information requests made during the October 21, 1988 meeting between representatives of the MTC and the California/Washington Bankers Association regarding MTC Proposed Regulations for the Attribution of Income of Financial Institutions.

Present were:

Phil Plant
Bank of America
Chairman, California Bankers Association

Bruce Abbott
Bank of America

Murray Aston
Rainier Bank

Marcia Dieter
First Independent Bank
Chairman, Washington Bankers Association

Lee Edwards
Seattle-First National Bank

Barbara Ells
Seattle-First National Bank

Anne Marston
First Interstate Bank

Al Sodini
Bank of America

Eric Coffill
California Franchise Tax Board

Gene Corrigan
MTC

Kim Ferrell
Utah State Tax Commission

Alan Friedman
MTC

Manual Gallegos
New Mexico Taxation and Revenue Department

Rudy Gallegos
New Mexico Taxation and Revenue Department

John Malach
Minnesota Department of Revenue

Jeff Miller
Montana Department of Revenue

Phil Plant opened the discussion, saying that the bank group would limit the subjects discussed to whether the destination sourcing rules and minimum jurisdictional standards of the proposed regulations were reasonable and/or administrable from a compliance perspective. He said the banks understood that the MTC is committed to advocating jurisdiction to tax without physical presence and destination sourcing of factors to insure that market states secure tax revenues from the multistate activities of out-of-state banks. Accordingly, no discussion of these general approaches was attempted at the meeting. Nevertheless, he noted that the exclusion of these items from the agenda should not be construed as a concession by the banks that taxation without physical presence is either logical or constitutional or that destination sourcing is a reasonable approach to state taxation of multistate banking at this point in the evolution of deregulated, interstate branch banking.

He identified the banks' meeting objectives as follows: (1) to heighten MTC awareness of areas of near impossibility or extraordinary cost in systems conversions mandated by certain applications of destination sourcing; (2) to identify alternatives to complex destination sourcing rules which will greatly reduce compliance/audit costs without unacceptable distortion of factors; and (3) to mitigate MTC concerns regarding taxpayer manipulation of

destination sourcing rules such as customer billing addresses or partnership commercial domiciles.

He said that the banks would like to limit the types of service fees separately sourced for receipt factor purposes. The Uniformity Committee of the MTC, recognizing the unacceptable uncertainty surrounding an attempt to source service fees to the state where the services are "consumed or used" by the customer, has proposed specific sourcing by type of fee primarily to the individual customer's residence or, if the customer is another type of entity, to the state in which the account is maintained. The banks wholeheartedly endorse abandoning the unworkable rule of sourcing service fees to the state where the services are "consumed or used", but they would further urge reducing the fee types subject to alternative sourcing rules to the fewest possible.

Phil said that the simplified service fee sourcing rules would eliminate excessive compliance burdens by avoiding unnecessary distinctions in fee types but would not significantly distort the overall destination sourcing approach. The excessive compliance burdens would be minimized by the following proposals:

(1) Reduce types of fees with distinct sourcing rules to fewest possible. Each separate fee category adds an additional systems programming requirement with a multiplier effect based on the number of systems. It was shown that Bank of America, for example, had 18 loan systems and 10 deposit systems which would be affected.

(2) Avoid separate treatment of two or more types of fees arising from a single payment stream. This multiple fee breakout plays havoc with systems and adds little to increased accuracy in destination sourcing.

(3) Allow ratable assignment rather than a separate tracing of fees that are "pooled". "Pooled" fees are aggregated for collective financial accounting treatment (e.g., loan fees under FAS 91). Fees so aggregated lose their geographic identity and should be apportioned as separate tracing is impossible.

(4) Allow fees collected manually as extraordinary charges which do not regularly recur to be sourced on an apportioned basis. Such manually collected fees (e.g., nonsufficient fund charges, check printing fees and stop payment charges) are not

posted in adequate detail in the branch accounts.

An enormous amount of systems work would be required to capture, maintain and source such information by customer address.

In further discussion of the foregoing, Murray Aston said that, under FASB 91, loan fees are amortized over the life of the loan and banks now pool those fees so that they lose their identification with the loans to which they apply. Therefore, he proposed that the interest source should be used as the means of allocating income from the fee stream by category to the states. He said that there are ten to fifteen categories of such loans, such as real estate loans, construction loans, and commercial loans.

Lee Edwards said that the base accounting systems maintain customer addresses and balances to the general ledger in most instances. However, certain fees such as those to which Murray had referred may be entered directly into the general ledger and not through a subsystem which traces amounts back to the customer. Therefore, he said, neither gross fees nor net fees can be identified by customer location. Thus, he supported Murray's contention that such fees should be allocated in accordance with the allocation of interest income, the latter being the predominant type of bank income anyway.

Al Sodini said that checking account related charges such as nonsufficient funds fees, check printing fees and stop payment fees are often written up manually and processed directly to the general ledger. They are posted to checking accounts as miscellaneous debits and, as such, cannot be broken out separately by either fee category or customer account. He proposed that it would be logical to allocate them to locations to within and without the taxing jurisdiction in a ratio corresponding to deposits. The relationship between these fees and deposits is logical and utilization of this ratio should not produce meaningful distortions. While it was suggested at the meeting that these fees constitute from 1 to 5% of all gross income from deposit related fees, subsequent investigation reveals that a significantly larger percentage is most likely involved and data will be provided to more precisely substantiate this. Even if these fees are significant in amount, however, the proposed allocation should be acceptable insofar as it represents a destination sourcing approach attributing these receipts to the location of the depositor and does not produce distortion.

Barbara Ells said that paragraph 1c on the second page of the June 29, 1988 letter from Gene Corrigan to Phil Plant was incorrect in its definition of a processing fee. She said that her bank, SeaFirst, and presumably other

banks as well, do not impose any such processing fee as loan originators. Moreover, if SeaFirst sells the loan but continues to process the payments for the buying bank, it receives a fee from the latter for doing so. Thus, loans originated by SeaFirst are sold to Bank X, but servicing by SeaFirst continues and a new type of revenue is created between the new loan holder and the servicing bank.

Sourcing this new income in the same manner as interest on the note, as suggested in the Corrigan letter would to be counterintuitive. Therefore, she proposed attributing the processing fee either to the state in which the processing takes place or the state in which the buyer of the loan is located. Insofar as sourcing to the location of the buyer is a form of destination sourcing, this latter approach is recommended as more in keeping with the MTC market state preference.

Lee Edwards discussed the way that check processing fees are handled by the bank on behalf of correspondent banks and endorsed the proposal of attributing the fees to the location of the correspondent bank for whom the check processing service is performed.

Murray Aston proposed that for ease of administration and to reduce the possibility of error, there should be a single standard to source loan and

deposit related fees. To have two sourcing standards, one for businesses and another for consumers, creates substantial difficulties for the banks. It assumes that banks have adequate detail in their records to differentiate between business and consumer accounts and that they have the systems capability to accomplish this feat as well. This is not so in most instances.

In light of the above, the banks proposed:

(1) That basic service fee categories should be limited to:

- (a) loan related fees;
- (b) deposit related fees;
- (c) third party bank check processing fees;
- (d) brokerage fees;
- (e) trust fees;
- (f) other fees.

(2) That loan and deposit related fees and third party bank check processing fees be sourced as a single fee item to the customer residence, brokerage fees to where the brokerage account is maintained, trustee fees to trustee or beneficiary address and other fees either sourced to where the services are performed or thrown out.

(3) That "pooled" fees be apportioned rather than separately traced. Specifically, loan fees should be assigned in a manner consistent with the assignment of interest on the loan.

(4) That manually collected extraordinary charges, notably nonsufficient fund charges, check printing fees and stop payment charges, be assigned on an apportioned basis in a like manner as deposits.

(5) That the "other fee" category either be sourced to the place where the services were performed or thrown out. In this regard, Phil offered a hypothetical example illustrating that the impact on the market states of sourcing such other fees to the location where the services were performed would be minuscule as applied to a multistate banking activity. Under the example, a bank with \$100MM in net income and a taxable presence in 20 market states would experience a reallocation of no more than \$2,750 in taxes away from a given market state under a hypothetical tax rate of 10%. This example is attached.

In conjunction with the above proposals, Gene and Alan requested that the banks provide the following data regarding fees:

(1) Percentage of nonsufficient funds charges, check printing fees and stop payment charges expressed as a percentage of total gross receipts and total service fee income.

(2) Breakdown of fees by type discussed above as a percentage of total fee income for large and small banks as well as retail and wholesale banks.

(3) Percentage of "other fees" discussed in conjunction with the banks' proposal as a percentage of total fees.

As respects the concerns of small banks, Marcia Dieter said that her bank would qualify as such, having only \$360 million in assets and 18 branches. Although it does have customers and loans in Oregon it does not solicit business there. It places no ads there, and has no branch or sales people there. Its canned program computer system is operating at maximum capacity. It cannot now break out information for two states. She does all of the tax returns herself. In order to change the programming, she would have to have a Boise firm come in at great expense. Smaller banks have tax returns done by outside firms who are not necessarily sophisticated in state taxes. Although her bank is considered to be very profitable, its profits

total only 3-4 million a year. A bank having assets of less than \$500 million is generally considered to be a small bank. A small bank uses the reserve method for bad debts whereas a large bank will charge bad debts off directly.

Marcia indicated that banks with assets of less than \$500MM did not have to report to the Comptroller of the Currency in the same detail as larger banks. Further investigation has revealed a more complicated picture, however. Reporting requirements are the same for the Comptroller, state regulators, and FDIC. Every national bank, state member bank, and insured state non member bank is required to file consolidated reports of condition and income on a quarterly basis. The specific reporting requirements depend on the size of the bank and whether it has any foreign offices. The amount of detail required to be reported varies among four versions of the report with the report for banks with less than \$100MM in assets and with only domestic offices having the least amount of detail and the report for banks with foreign offices or greater assets requiring more. For those banks with no foreign offices, those with \$300MM or more total assets are required to report in the greatest detail.

Murray said that 6 of the 152 Washington banks pay

90% of the tax there and that 2 pay more than 50%.

Therefore, a higher nexus threshold than that presently provided would not cause significant revenue losses to the market states.

Phil expressed the hope that the MTC would attempt whenever possible to tie in state tax sourcing requirements with data that the banks already gather for other reporting purposes so that another administrative burden would not be laid on the banks unnecessarily.

As to partnerships sourcing issues, Lee Edwards commented that the banks do not have in their systems information reflecting the identity of all the partners. Therefore, Barbara said, the MTC partnership sourcing requirements would be totally new to the banks. In this regard, the treatment in the proposed regulations of partnerships as "look-through" entities has properly been recognized by the Uniformity Committee as impractical in its general application. Nevertheless, as some Committee members were said to prefer sourcing unsecured indebtedness to the residence of the individual partners of partnerships consisting of ten or fewer partners, the banks represented for the record that an attempt to track such multiple partner locations was plainly impossible. Existing bank loan records reflect no convenient basis for distinguishing

partnerships from other entities. Moreover, bank records or systems generally do not identify more than one partner and any attempt to do so prospectively would be prohibitively expensive. It was therefore urged that the commercial domicile of the partnership be the universal sourcing rule and that the location be presumed to be the same as the partnership billing address zip code.

Similarly, as respects sourcings corporate unsecured debt, the banks urged retention of the "statement rule" presently in the MTC proposed regulations. The suggestion that some MTC members preferred to regress to sourcing unsecured debt to "where the proceeds of the loan were applied" caused the banks great concern. Large corporate borrowers do not raise funds in a manner facilitating collection of detailed information as to where the proceeds of the loan were applied and, even if they did, banks couldn't gather and track such detail without extraordinary customer cooperation, impossible systems overhauls and ongoing compliance costs. The fear of taxpayer manipulation of values from one state to another under this rule was explained to be unfounded insofar as the conduct of lending activities have never been influenced by state tax considerations, and even if this were not so, such attempted manipulations, presumably accomplished by enticing corporate borrowers to designate a low tax rate

jurisdiction billing address in exchange for an interest rate reduction, would only be feasible as respects the largest corporate borrowers. Such borrowers would represent a very small fraction of the total borrowers and would be readily identified in state tax audits. It was agreed that the formulation of a rule that corporate unsecured debt would be sourced to the home office of the borrower's officer applying for the loan and that that location would be presumed to be located at the borrowers billing address by zip code would be a workable compromise and would permit appropriate audit adjustments. The banks are to provide proposed language for this presumption.

Barbara Ells observed that sourcing loans secured by real or tangible personal property to the location of the collateral rather than the borrower was counterintuitive and did not appear to materially enhance the market states' share of taxes. In addition to being more logical, the location of the security is currently not on an automated system whereas the borrower location is available. She distinguished healthy loans vs. foreclosed property. She made the argument that while a loan is healthy, the interest income should be sourced to the location of the borrower, regardless of whether the loan is secured or unsecured. The security should only become an issue when foreclosure/repossession actually occurs. At that point,

income from the foreclosed property would be sourced to the state wherein the property is located. Even if the MTC retained a collateral sourcing approach, a presumption that the collateral would be located in the state of the billing address of the borrower would be tremendously helpful to the banks from a compliance perspective. It was emphasized in passing that the potential for distortion under this approach was very small insofar as the vast majority of large bank loans are unsecured under the definitions of the MTC proposed regulations and virtually all secured loans are collateralized by property located in the same state as the borrower.

Marcia commented that collateral sourcing should be modified in any event where multiple properties securing a loan were located in two or more states. It would be extremely difficult to allocate interest from the loan to each state in such instances. All interest should therefore be sourced to the state with the greatest property values. The loan itself, as an asset for property factor purposes, should be similarly treated. The resultant distinction should be miniscule insofar as the proportion of such loans is negligible and a skewing toward money center states as distinct from market states would not appear to result in any event.

Anne Marston commented that there are already dozens of items for which accounting is different for tax purposes than for book purposes under FASB, that the banks cannot do a receipts factor based on tax accounting records, that to do so would require a completely new set of records, and that even the definition of accrued income for tax purposes differs from that for book purposes. It was noted that insofar as book numbers may be the only figures available under existing systems on a geographic basis and book figures would, over time, equate to tax figures, it made sense to permit the option to utilize book numbers for factor valuing purposes. Forcing a conversion from book to tax values on a geographically segregated basis would be exceedingly costly and complicated. The banks were requested to make a submission to the MTC enumerating how book-tax differences could be reconciled for sourcing purposes.

Alan said that the MTC staff hoped to have a final draft of the proposed regulation ready for their annual meeting in July, 1989, that the hearing process would take place after that and that, if all goes well, final adoption of the regulation by the Commission would probably take place at the July, 1990 annual meeting.

PMP:094:cnc

Hypothetical Computations
 State Tax Effect of Sourcing
 "Other Service Fees" to Locations
Where Services are Performed

- 1/3 - only sales factor impacted; property and payroll factors unaffected
- 1/3 - other 2/3ds gross receipts are interest and gain on sale rather than fee income
- 1/2 - deposits/loan related fees, trust fees and brokerage fees are at least 1/2 of total fees and are already destinations sourced to state of customer
- 1/10 - other 90% of service fees are charged to customers who reside in same state as where service performed

1/180 - .55 of 1% net income is thus attributed to state where service provided rather than market state.

1/20 of .55 - .0275 of 1% would be shift in assigned income out of a given market state if taxpayer is taxable in 20 states outside its commercial domicile (incredibly easy under existing minimum jurisdictional standards of MTC proposal).

Net income	\$100MM
Above %	<u>.0275%</u>
Apportioned net income	\$27,500
Hypothetical tax rate	<u>10%</u>
State tax effect	\$ 2,750

EXHIBIT B: 12

**Letter from Philip M. Plant w/ "Proposed Amendments 1/89"
(Bank of America) (January 6, 1989)**

March 1989 draft incorporating Phil Plant's recommendations
(strikeouts and underlining retained)

March 1989 Draft Proposal of

**PROPOSED REGULATION FOR THE ATTRIBUTION OF THE INCOME OF
FINANCIAL INSTITUTIONS**

- (A) **Definitions.** Except as specifically defined herein, all terms used in this regulations shall have the same meaning as such terms have under [here include your State ~~cite~~ citation to the Multistate Tax Compact or other applicable state law] and the rules and regulations promulgated thereunder.
- (1) "Receipts" for the purpose of the receipts factor, means gross income, including net taxable gain on disposition of assets (including securities, loans, personal and real property and money market transactions) when derived from transactions and activities in the regular course of the taxpayer's trade or business.
 - (2) "Participation Loan" means a loan in which more than one lender is a creditor to a common borrower.
 - (3) "Securities" means United States Treasury securities, obligations of United States Government agencies and corporations, obligations of State and political subdivisions, corporate stock and other corporate securities, participations in securities backed by mortgages held by United States or State government agencies, loan-backed securities and similar investments to the extent that such investments are reflected as assets under generally accepted accounting principles.
 - (4) "Money Market Instruments" mean Federal funds sold and securities purchased under agreements to resell, commercial paper, banker's acceptances, and purchased certificates of deposit and similar instruments to the extent that such instruments are reflected as assets under generally accepted accounting principles.
 - (5) "Property Located in this State"
 - (a) **Tangible Property: General Rule.** -- Except as otherwise provided in this section, tangible and real property which is security for a loan or property subject to a lease, shall be considered to be located in the state in which such property is physically situated. It shall be presumed, subject to rebuttal, that the property is physically situated in the same state as the billing address of the borrower or lessee.

(b) Moveable tangible property. -- Tangible personal property which is characteristically moving property, such as motor vehicles, rolling stock, aircraft, vessels, mobile equipment, and the like shall be considered to be located in a state if:

(i) the operation of the property is entirely within the state; or

(ii) the operation of the property is in two or more states, but the principal base of operations from which the property is sent out is in the state. It shall be presumed, subject to rebuttal, that the location of operation of the property and the principal base of operations from which the property is sent out shall be that duly certified in writing by the lessee or borrower in the same state as the billing address of the borrower or lessee.

(6) "Exercising a Corporate Franchise or Transacting Business in a State." A financial institution is exercising a corporate franchise or transacting business in this state if:

(a) it has a place of business in this state;

(b) it has employees, representatives or independent contractors conducting business activities in its behalf in this state; or,

(c) it engages in regular solicitation in this state (whether at a place of business, by travelling loan officers or other representatives, by mail, by telephone or other electronic means), and the solicitation results in the creation of a depository or direct debtor/creditor relationship with a resident of this state. For purposes of this regulation, mere processing or transfer through financial intermediaries of checks, credit card receivables, commercial paper and the like does not create a debtor/creditor relationship.

A financial institution is presumed, subject to rebuttal, to be engaged in regular solicitation within this state if it has entered into any of the relationships listed in subsection (c) above with ~~20~~ 100 or more residents of this state during any tax period or if it has \$5,000,000 or more of assets attributable to sources within this state at any time during the tax period.

(7) "Taxpayer" means a financial institution which is subject to taxation in a state because it is exercising its

corporate franchise or is transacting business in a corporate or organized capacity in the state and has gross income attributable under this regulation to sources within this state.

- (8) "Subsidiary" means a corporation whose voting stock is more than 50% owned, directly or indirectly, by a financial institution.
- (9) "Holding Company" means any corporation subject to [insert citation of the state law governing the creation of bank holding companies] or registered under the Federal Bank Holding Company Act of 1956, as amended, or registered as a savings and loan holding company under the Federal National Housing Act, as amended.
- (10) "Regulated Financial Corporation" means an institution the deposits or accounts of which are insured under the Federal Deposit Insurance Act or by the Federal Savings and Loan Insurance Corporation, any institution which is a member of a Federal Home Loan Bank, any other bank or thrift institution incorporated or organized under the laws of the United States, any State or any foreign country which is engaged in the business of receiving deposits or which holds a bank charter, any corporation organized under the provision of 12 U.S.C. sections 611 to 631 (Edge Act Corporations), and any agency of a foreign depository as defined in 12 U.S.C. section 3101.
- (11) "Business of a Financial Institution" includes the following:
 - (a) the business that a regulated financial corporation may be authorized to do under state or federal law or the business that its subsidiary is authorized to do by the proper regulatory authorities.
 - (b) the business that any corporation organized under the authority of the United States or organized under the laws of this state or any other state or country does/or has authority to do which is substantially similar to the business which a corporation may be created to do under [insert citations of state's laws governing the creation of banks and trust companies, industrial banks, savings and loan associations, etc.] or any business which a corporation or its subsidiary is authorized to do by said laws.
 - (c) the business that any corporation organized under the authority of the United States or organized under the laws of this state or any other state or country does or has authority to do if such corporation derives more than fifty percent of its

gross income from lending activities (including discounting obligations) in substantial competition with the businesses described in subsections (a) and (b) above. For purposes of this subsection, the computation of the gross income of a corporation shall not include income from nonrecurring, extraordinary items.

(12) "Financial Institution" includes the following:

- (a) A holding company.
- (b) Any regulated financial corporation.
- (c) Any other corporation organized under the laws of the United States or organized under the laws of this state or any other state or country which is carrying on the business of a financial institution.

~~(13) "Place of consumption or use of services" means the state in which the benefits of the services are received. If such benefits are received in more than one state, the receipts from these benefits shall be apportioned to this state pro rata according to the portion of the benefits received in this state.~~

~~(14)~~

(13) "Borrower" means the individual or entity who is primarily liable on a debt instrument. If more than one individual or entity is primarily liable on a debt instrument, each such individual or entity shall be considered the borrower to the extent of its interest in the debt instrument. For purposes of this regulation, a partnership shall be treated as a ~~group of individuals~~ separate entity.

~~(15)~~

(14) "Deposit" means:

- (a) the unpaid balance of money or its equivalent received or held by a financial institution in the usual course of business and for which it has given or is obligated to give credit, either conditionally or unconditionally, to a commercial, checking, savings, time, or thrift account whether or not advance notice is required to withdraw the credited funds, or which is evidenced by its certificate of deposit, thrift certificate, investment certificate, or certificate of indebtedness, or other similar name, or a check or draft drawn against a deposit account and certified by the financial institution, or a letter of credit or a traveler's check on which the financial institution is primarily liable; provided, that, without limiting the generality of

the term "money or its equivalent," any such account or instrument must be regarded as evidencing the receipt of the equivalent of money when credited or issued in exchange for checks or drafts or for a promissory note upon which the person obtaining any such credit or instrument is primarily or secondarily liable or for a charge against a deposit account or in settlement of checks, drafts, or other instruments forwarded to such bank for collection;

- (b) trust funds received or held by such financial institution, whether held in the trust department or held or deposited in any other department of such financial institution;
- (c) money received or held by a financial institution, or the credit given for money or its equivalent received or held by a financial institution in the usual course of business for a special or specific purpose, regardless of the legal relationship thereby established, including, without being limited to, escrow funds, funds held as security for an obligation due the financial institution or others (including funds held as dealers reserves) or for securities loaned by the bank, funds deposited by a debtor to meet maturing obligations, funds deposited as advance payment on subscriptions to United States Government securities, funds held for distribution or purchase of securities, funds held to meet its acceptances or letters of credit, and withheld taxes; provided that there shall not be included funds which are received by the financial institution for immediate application to the reduction of an indebtedness to the receiving financial institution, or under condition that the receipt thereof immediately reduces or extinguishes such an indebtedness;
- (d) outstanding drafts (including advice or authorization to charge a financial institution's balance in another such institution), cashier's checks, money orders, or other officer's checks issued in the usual course of business for any purpose, but not including those issued in payment for services, dividends, or purchases or other costs or expenses of the financial institution itself;
- (e) money or its equivalent held as a credit balance by a financial institution on behalf of its customer if such entity is engaged in soliciting and holding such balances in the regular course of its business.

(15) "State" means a state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, or any territory or possession of the United States or any foreign country.

~~(17)~~

(16) "Taxable in a State." For the purpose of the receipts factor, a taxpayer is taxable in another state if: (a) in that state, he is subject to a franchise tax measured by net income, a net income tax, a franchise tax for the privilege of doing business, or a corporate stock tax, or (b) that State has jurisdiction to subject the taxpayer to such a tax regardless of whether, in fact, the State does or does not.

~~(18)~~

(17) "Resides/Residence/Resident." A person shall be considered to reside or make his or her residence in or be a resident of a state if, in the case of an individual, he/she resides there for more than ~~100~~ 182 days of the relevant tax period. For purposes of this regulation, a partnership shall be treated as a ~~group of individuals, each of whom is subject to the above residence rule~~ resident of the state of its commercial domicile. A corporation shall be considered a resident of the state in which it has an of the office out of which works the corporate officer making the deposit or applying for the loan. or other place of business during the relevant tax period. For purposes of this regulation, a corporation may be a resident of more than one state. An individual, a partnership or a corporation shall be presumed, subject to rebuttal, to reside at (i.e., be a resident of, make his residence at) the address to which the statement of account is regularly mailed.

(18) "Loan Related Fees." For purposes of the receipts factor, loan related fees include all fees associated with the generation and administration of loans. Receipts from loan related fees which are either (a) "pooled" or aggregated for collective financial accounting treatment or (b) manually written as non-recurring extraordinary charges to be processed directly to the general ledger shall be attributed to a state based upon the ratio that total interest sourced to that state bears to total interest from all sources.

(19) "Deposit Related Fees." For purposes of the receipts factor, deposit related fees include all fees associated with the administration of deposit accounts. Receipts from deposit related fees which are either (a) "pooled" or aggregated for collective financial accounting treatment or (b) manually written as non-recurring extraordinary changes to be processed directly to the

general ledger shall be attributed to a state based upon the ratio that total deposits sourced to that state bear to total deposits from all sources.

(20) "Third Party Check Processing Fees." For purposes of the receipts factor, third party check processing fees include fees charged by a loan originating financial institution to a third party financial institution buying the loan in instances where the loan originating financial institution continues to process loan payments.

(21) "Presumption." A presumption subject to rebuttal, as provided in this regulation, shall be rebuttable by clear and convincing proof established by either the financial institution or [here include title of your State taxing agency].

(B) **Business Income.** All income (taxable under the laws of this State) which arises from the business of a financial institution shall be deemed derived from transaction in the regular course of the taxpayer's business and subject to apportionment under this regulation. All such income which arises from activities of a financial institution which are not the business of a financial institution as defined in this rule shall be apportioned or allocated in accordance with the rules set forth in [here include your State eite citation to UDITPA or the Multistate Tax Compact].

(C) **Apportionment of Business Income.**

(1) **General Method.**

(a) If a financial institution is carrying on the business of a financial institution both within and without this state and if, by reason of such business activity, it is taxable in another state, the portion of the net income (or net loss) arising from such business which is derived from sources within this state shall be determined by apportionment in accordance with this regulation.

(b) The tax applicable to financial institutions whose net income (or net loss) is apportionable according to the rules in this section shall be determined by multiplying the tax base by a fraction the numerator of which is the sum of the receipts factor, the property factor, and the payroll factor as defined in this regulation and the denominator of which is three. If any factor(s) is missing, the remaining factors are added together and the sum is divided

by the number of remaining factors. A factor is missing if both its numerator and denominator are zero, but it is not missing merely because its numerator is zero.

- (2) Receipts Factor. In general. -- The receipts factor is a fraction the numerator of which is the receipts of the taxpayer within this state during the tax period and the denominator of which is the total receipts of the taxpayer from all states in which the taxpayer is taxable during such tax period. The numerator of the receipts factor shall include, in addition to items otherwise assignable under [here include your State ~~cite~~ citation to the Multistate Tax Compact or other applicable state law]:
- (a) Receipts from the lease or rental of real or tangible personal property (including both finance leases and true leases) ~~shall be attributed to this state~~ if the property is located in this state;
 - (b) Interest income and other receipts from assets in the nature of loans which are secured primarily by real estate or tangible personal property ~~shall be attributed to this state~~ if such security property is located in this state; in the event that such security property is located in two or more states, it shall be deemed to be located in the state having the greatest property values;
 - (c) Interest income and other receipts from consumer loans not secured by real or tangible personal property that are made to residents of this state (whether at a place of business, by travelling loan officer, by mail, by telephone or other electronic means) ~~shall be attributed to this state;~~
 - (d) Interest income and other receipts from commercial loans and installment obligations not secured by real or tangible personal property ~~shall be attributed to this state~~ if and to the extent that the borrower is a resident of this state;
 - (e) Interest income and other receipts from a participating financial institution's portion of participation loans ~~shall be attributed~~ under the rules set forth in subsections (a) through (d) above;
 - (f) Interest income and other receipts, including service charges from financial institution credit card and travel and entertainment credit card receivables and credit card holders' fees ~~shall be~~

~~attributed to the state to which~~ if such card charges and fees are regularly billed to this state.

- (g) Merchant discount income derived from financial institution credit card holder transactions with a merchant ~~shall be attributed to the state in which the merchant is located in this state.~~ In the case of merchants located within and without this state, only receipts from merchant discounts attributable to sales made from locations within ~~the~~ this state shall be attributed to this State. It shall be presumed, subject to rebuttal, that the location of a merchant is the address shown on the invoice submitted by the merchant to the taxpayer.
- (h) Receipts from the performance of ~~fiduciary and other~~ services are attributed to this state if ~~the services are consumed or used in this state:~~
- (i) the service receipts are loan related fees and the borrower resides in this state;
 - (ii) the service receipts are deposit related fees and the depositor resides in this state;
 - (iii) the service receipts are third party financial institution check processing fees and the third party financial institution resides in this state;
 - (iv) the service receipt is a brokerage fee and the brokerage account is maintained at an office of the financial institution located in this state;
 - (v) the service receipts are fees related to estate or trust services and the executor or trustee resides in this state or, if there are two or more executors or trustees, the executor or trustee primarily responsible for administering the estate or trust is located in this state;
or
 - (vi) the service receipt is associated with the performance of any other service not identified above and the service is primarily performed in this state.
- (i) Receipts from the issuance of travelers checks and money orders ~~shall be attributed to the state in which~~ if such checks and money orders are purchased in this state;

- (j) Receipts from investments of a financial institution in securities of this state, its political subdivisions, agencies and instrumentalities shall be attributed to this state;
- (k) Receipts from investments of a financial institution in other securities and from money market instruments, shall be apportioned to this state based upon the ratio that total deposits from this state, its residents, its political subdivisions, agencies and instrumentalities bear to the total deposits from all states, their residents, their political subdivisions, agencies and instrumentalities. In the case of an unregulated financial institution subject to this regulation, such receipts shall be apportioned to this state based upon the ratio that its gross business income earned from sources within this state bears to gross business income earned from sources within all states. For purposes of this subsection, deposits made by this state, its residents, its political subdivisions, agencies and instrumentalities shall be attributed to this state, whether or not such deposits are accepted or maintained by the taxpayer at locations within this state.
- (l) All receipts located by this rule in a state without jurisdiction to tax shall be excluded from both the numerator and the denominator of the receipts factor.
- (3) Property Factor. In general. -- The property factor is a fraction the numerator of which is the average value of the taxpayer's real and tangible personal property owned or rented and used in, and intangible property attributed to, this state during the tax period and the denominator of which is the average value of all of the taxpayer's real and tangible personal property owned or rented and used in, and intangible property attributed to, all states during the tax period. For purposes of this regulation, the value of property owned by the taxpayer shall be its federal income tax basis, without diminution for bad debt reserves; the value of property rented by the taxpayer shall be eight times its net annual rental rate. The net annual rental rate for any item of rented property is the annual rate paid by the taxpayer for such property less the aggregate annual subrental rates paid by subtenants of the taxpayer. Intangible personal property shall be included at its tax basis for federal income tax purposes. Goodwill shall not be included in the property factor. The numerator of the property factor shall include, in addition to items otherwise assignable under [here

include your State ~~eite~~ citation to the Multistate Tax Compact or other applicable state law], the following:

- (a) Coin and currency located in this state ~~shall be attributed to this state;~~
- (b) Lease financing receivables ~~shall be attributed to this state~~ if and to the extent that the property is located within this state;
- (c) Assets in the nature of loans which are secured by real or tangible personal property ~~shall be attributed to this state~~ if and to the extent that the security property is located within this state; in the event that such security property is located in two or more states, it shall be deemed to be located in the state having the greatest property values;
- (d) Assets in the nature of consumer loans and installment obligations which are unsecured or secured by intangible property, ~~shall be attributed to this state~~ if the loan was made to a resident of this state;
- (e) Assets in the nature of commercial loan and installment obligations which are unsecured or secured by intangible property, ~~shall be attributed to this state~~ if and ~~to the extent that~~ the borrower is a resident of this state;
- (f) Assets in the nature of funds deposited by one financial institution in another financial institution, ~~shall be attributed to this state~~ if the depositor is a resident of this state;
- (g) A participating financial institution's portion of a participation loan, ~~shall be attributed~~ under the rules set forth in subsections (b) through (e) above;
- (h) Financial institution credit card and travel and entertainment credit card receivables, ~~shall be attributed to this state~~ if such credit card charges and fees are regularly billed to a resident of this state;
- (i) Assets in the nature of securities of this State, its political subdivisions, agencies and instrumentalities ~~shall be attributed to this state;~~
- (j) Assets in the nature of securities and money market instruments, ~~shall be apportioned to this state~~ based upon the ratio that total deposits from this

State, its residents, its political subdivisions, agencies and instrumentalities bear to the total deposits from all States, their residents, their political subdivisions, agencies and instrumentalities. In the case of an unregulated financial institution subject to this regulation, such receipts shall be apportioned to this state based upon the ratio that its gross business income earned from sources within all states. For purposes of this subsection, deposits made by this State, its residents, its political subdivisions, agencies and instrumentalities shall be attributed to this state regardless of whether or not such deposits are accepted or maintained by the taxpayer at locations within this state.

(j)

(k)

All property located by this rule in a state without jurisdiction to tax shall be excluded from both the numerator and the denominator.

(4) Payroll Factor. In general. -- The payroll factor is a fraction the numerator of which is the total amount paid by the taxpayer for compensation during the year, and the denominator of which is the total amount of compensation paid in every state.

(a) Neither the numerator nor the denominator of the payroll factor shall include wages compensation paid to an employee in a state without which has no jurisdiction to tax.

(D) **Special Rules.** If the allocation and apportionment provisions of this regulation do not fairly represent the extent of the taxpayer's activity in this state, the taxpayer may petition for or the tax administrator may require, in respect to all or any part of the taxpayer's business activity, if reasonable:

(1) Separate accounting;

(2) The exclusion of any one or more of the factors;

(3) The inclusion of one or more additional factors which will fairly represent the taxpayer's business activity in this state; or

- (4) The employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

EXHIBIT B: 13

**March 1989 Draft Proposal
w/ strikeouts and underlining reflecting Philip Plant's recommendations
(March 1989) (prepared by MTC)**

Proposed Amendments (1/89)

Multistate Tax Commission
July, 1987

DRAFT

PROPOSED REGULATIONS FOR THE ATTRIBUTION OF THE INCOME OF
FINANCIAL INSTITUTIONS.

(A) Definitions. Except as specifically defined herein, all terms used in this regulations shall have the same meaning as such terms have under [here include your state cite to the Multistate Tax Compact or other applicable state law] and the rules and regulations promulgated thereunder.

- (1) "Receipts" for the purpose of the receipts factor, means gross income, including net taxable gain on disposition of assets (including securities, loans, personal and real property and money market transactions) when derived from transactions and activities in the regular course of the taxpayer's trade or business.
- (2) "Participation Loans" means a loan in which more than one lender is a creditor to a common borrower.
- (3) "Securities" means United States Treasury securities, obligations of United States Government agencies and corporations, obligations of State and political subdivisions, corporate stock and other corporate securities, participations in securities backed by mortgages held by United States or State government agencies, loan-backed securities and similar investments to the extent that such investments are reflected as assets under generally accepted accounting principles.
- (4) "Money Market Instruments" means Federal funds sold and securities purchased under agreements to resell, commercial paper, banker's acceptances, and purchased certificates of deposit and similar instruments to the extent that such instruments are reflected as assets under generally accepted accounting principles.
- (5) "Property Located in this State"
 - (a) Tangible Property: General Rule.-- Except as otherwise provided in this section, tangible and real property which is security for a loan or property subject to a lease, shall be considered to be located in the State in which such property is physically situated. It shall be presumed, subject to rebuttal, that the property is

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physically situated in the same state as the billing address of the borrower or lessee.

(b) Moveable tangible property.-- Tangible personal property which is characteristically moving property, such as motor vehicles, rolling stock, aircraft, vessels, mobile equipment, and the like shall be considered to be located in a State if:

(i) the operation of the property is entirely within the state; or

(ii) the operation of the property is in two or more states, but the principal base of operations from which the property is sent out is in the state. It shall be presumed, subject to rebuttal, that the location of operation of the property and the principal base of operations from which the property is sent out shall be that duly certified in writing by the lessee or borrower in the same state as the billing address of the borrower or lessee.

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(6) "Exercising a Corporate Franchise or Transacting Business in a State." A financial institution is exercising a corporate franchise or transacting business in this state if:

(a) it has a place of business in this state;

(b) it has employees, representatives or independent contractors conducting business activities in its behalf in this state; or,

(c) it engages in regular solicitation in this state (whether at a place of business, by travelling loan officers or other representatives, by mail, by telephone or other electronic means), and the solicitation results in the creation of a depository of direct debtor/creditor relationship with a resident of this state. For purposes of this regulation, mere processing or transfer through financial intermediaries of checks, credit card receivables, commercial paper and the like does not create a debtor/creditor relationship.

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A financial institution is presumed, subject to rebuttal to be engaged in regular solicitation within this state if it has entered into any of the relationships listed in subsection (c) above with at least 100 or more residents of this state during any tax period or if it has \$5,000,000 or more of assets attributable to sources within this state at any time during the tax period.

(7) "Taxpayer" means a financial institution which is subject to taxation in a state because it is exercising its corporate franchise, or is transacting business in a corporate or organized capacity in the state, and has gross income attributable under this regulation to sources within this state.

(8) "Subsidiary" means a corporation whose voting stock is more than 50% owned, directly or indirectly, by a financial institution.

(9) "Holding Company" means any corporation subject to [insert citation of the state law governing the creation of bank holding companies], or registered under the Federal Bank Holding Company Act of 1956, as amended, or registered as a savings and loan holding company under the Federal National Housing Act, as amended.

(10) "Regulated Financial Corporation" means an institution, the deposits or accounts of which are insured under the Federal Deposit Insurance Act or by the Federal Savings and Loan Insurance Corporation, any institution which is a member of a Federal Home Loan Bank, any other bank or thrift institution incorporated or organized under the laws of the United States, any State or any foreign country which is engaged in the business of receiving deposits or which holds a bank charter, any corporation organized under the provision of 12 U.S.C. sections 611 to 631 (Edge Act Corporations), and any agency of a foreign depository as defined in 12 U.S.C. section 3101.

(11) "Business of a Financial Institution" includes the following:

(a) the business that a regulated financial corporation may be authorized to do under state or federal law or the business that its subsidiary is authorized to do by the proper regulatory authorities.

(b) the business that any corporation organized under the authority of the United States or organized under the laws of this state or any other state or country does/or has authority to do which is substantially similar to the business which a corporation may be created to do under [insert citations of state's laws governing the creation of banks and trust companies, industrial banks, savings and loan association, etc.] or any business which a corporation or its subsidiary is authorized to do by said laws.

(c) the business that any corporation organized under the authority of the United States or organized under the laws of this state or any other state or country does/or has authority to do if such corporation derives more than fifty percent of its gross income from lending activities (including discounting obligations) in substantial competition with the businesses described in subsections (a) and (b) above. For purposes of this subsection, the computation of the gross income of a corporation shall not include income from nonrecurring, extraordinary items.

(12) "Financial Institution" includes the following:

(a) A holding company.

(b) Any regulated financial corporation.

(c) Any other corporation organized under the laws of the United States or organized under the laws of this state or any other state or country which is carrying on the business of a financial institution.

~~(13) "Place of consumption or use of services" means the state in which the benefits of the services are received. If such benefits are received in more than one state, the receipts from these benefits shall be apportioned to this state pro rata according to the portion of the benefits received in this state.~~

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~~(14)~~ (13) "Borrower" means the individual or entity who is primarily liable on a debt instrument. If more than one individual or entity is primarily liable on a debt instrument, each such individual or entity shall be considered the borrower to the extent of its interest in the debt instrument. For purposes of this regulation, a partnership shall be treated as a ~~group of individuals~~ separate entity.

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~~(15)~~ (14) "Deposit" means:

(a) the unpaid balance of money or its equivalent received or held by a financial institution in the usual course of business and for which it has given or is obligated to give credit, either conditionally or unconditionally, to a commercial, checking, savings, time, or thrift account whether or not advance notice is required to withdraw the credited funds, or which is evidenced by its certificate of deposit, thrift certificate, investment certificate, or certificate of indebtedness, or other similar name, or a certificate of

indebtedness, or other similar name, or a check or draft drawn against a deposit account and certified by the financial institution, or a letter of credit or a traveler's check on which the financial institution is primarily liable; provided, that, without limiting the generality of the term "money or its equivalent" any such account or instrument must be regarded as evidencing the receipt of the equivalent of money when credited or issued in exchange for checks or drafts or for a promissory note upon which the person obtaining any such credit or instrument is primarily or secondarily liable, or for a charge against a deposit account, or in settlement of checks, drafts, or other instruments forwarded to such bank for collection;

(b) trust funds received or held by such financial institution, whether held in the trust department or held or deposited in any other department of such financial institution;

(c) money received or held by a financial institution, or the credit given for money or its equivalent received or held by a financial institution, in the usual course of business for a special or specific purpose, regardless of the legal relationship thereby established, including without being limited to, escrow funds, funds held as security for an obligation due to the financial institution or others (including funds held as dealers reserves) or for securities loaned by the bank, funds deposited by a debtor to meet maturing obligations, funds deposited as advance payment on subscriptions to United States Government securities, funds held for distribution or purchase of securities, fund held to meet its acceptances or letters of credit, and withheld taxes; provided, that there shall not be included funds which are received by the financial institution for immediate application to the reduction of an indebtedness to the receiving financial institution, or under condition that the receipt thereof immediately reduces or extinguishes such as indebtedness;

(d) outstanding drafts (including advice or authorization to charge a financial institution's balance in another such institution), cashier's checks, money orders, or other officer's checks issued in the usual course of business for any purpose, but not including those issued in payment for services, dividends, or purchases or other costs or expenses of the financial institution itself.

(e) money or its equivalent held as a credit balance by a financial institution on behalf of its customer if such entity is engaged in soliciting and holding such balances in the regular course of its business.

~~(16)~~ (15) "State" means a state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, or any territory or possession of the United States or any foreign country.

~~(17)~~ (16) "Taxable in a State." For the purpose of the receipts factor, a taxpayer is taxable in another state if: (a) in that State, he is subject to a franchise tax measured by net income, a net income tax, a franchise tax for the privilege of doing business, or a corporate stock tax, or (b) that State has jurisdiction to subject the taxpayer to such a tax regardless of whether, in fact, the State does or does not.

~~(18)~~ (17) "Resides/Residence/Resident." A person shall be considered to reside or make his or her residence in or be a resident of a state if, in the case of an individual, he/she resides there for more than ~~180~~ 182 days in the relevant tax period. For purposes of this regulation, a partnership shall be treated as a ~~group of individuals, each of who is subject to the above residence rule~~ resident of the state of its commercial domicile. A corporation shall be considered a resident of the state ~~in which it has an~~ of the office out of which works the corporate officer making the deposit or applying for the loan, or other place of business during the relevant tax period. ~~For purposes of this regulation, a corporation may be a resident of more than one state.~~ An individual, partnership or a corporation shall be presumed, subject to rebuttal, to reside (be a resident of, make his residence at) at the address to which its statement of account is regularly mailed.

(18) "Loan Related Fees". For purposes of the receipts factor, loan related fees include all fees associated with the generation and administration of loans. Receipts from loan related fees which are either (a) "pooled" or aggregated for collective financial accounting treatment or (b) manually written as non-recurring extraordinary charges to be processed directly to the general ledger shall be attributed to a state based upon the ratio that total interest sourced to that state bears to total interest from all sources.

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(19) "Deposit Related Fees". For purposes of the receipts factor, deposit related fees include all fees associated with the administration of deposit accounts. Receipts from deposit related fees which are either (a) "pooled" or aggregated for collective financial accounting treatment or (b) manually written as non-recurring extraordinary changes to be processed directly to the general ledger shall be attributed to a state based upon the ratio that total deposits sourced to that state bears to total deposits from all sources.

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(20) "Third Party Check Processing Fees". For purposes of the receipts factor, third party check processing fees include fees charged by a loan originating financial institution to a third party financial institution buying the loan in instances where the loan originating financial institution continues to process loan payments.

(21) "Presumption". A presumption subject to rebuttal, as provided in this regulation, shall be rebuttable by clear and convincing proof established by either the financial institution or [here include title of your state taxing agency].

(B) Business Income. All income (taxable under the laws of this State) which arises from the business of a financial institution shall be deemed derived from transaction in the regular course of the taxpayer's business and subject to apportionment under this regulation. All such income which arises from activities of a financial institution which are not the business of a financial institution as defined in this rule shall be apportioned or allocated in accordance with the rules set forth in [here include your state cite to UDITPA or the Multistate Tax Compact].

(C) Apportionment of Business Income

(1) General Method.

(a) If a financial institution is carrying on the business of a financial institution both within and without this state, and if by reason of such business activity, it is taxable in another state, the portion of the net income (or net loss) arising from such business which is derived from sources within this state shall be determined by apportionment in accordance with this regulation.

(b) The tax applicable to financial institutions whose net income (or net loss) is apportionable according to the rules in this section shall be determined by multiplying the tax base by a fraction, the numerator of which is the sum of the receipts factor, the property factor, and the payroll factor as defined in this regulation and the denominator of which is three. If any factor(s) is missing, the remaining factors are added together and the sum is divided by the number of remaining factors. A factor is missing if both its numerator and denominator are zero, but it is not missing merely because its numerator is zero.

(2) Receipts Factor. In general. -- The receipts factor is a fraction, the numerator of which is the receipts of the taxpayer within this state during the tax period and the denominator of which is the total receipts of the taxpayer from all states in which the taxpayer is taxable during such tax period. The numerator of the receipts factor shall include, in addition to items otherwise assignable under [here include your state cite to the Multistate Tax Compact or other applicable state law], the following receipts attributable to this state:

(a) Receipts from the lease or rental of real or tangible personal property (including both finance leases and true leases) shall be attributed to this state if the property is located in this state.

(b) Interest income and other receipts from assets in the nature of loans which are secured primarily by real estate or tangible personal property shall be attributed to this state if such security property is located in this state. In the event such security property is located in two or more states, it shall be deemed to be located in the state having the greatest property values.

(c) Interest income and other receipts from consumer loans not secured by real or tangible personal property that are made to residents of this state (whether at a place of business, by travelling loan officer, by mail, by telephone or other electronic means) shall be attributed to this state.

(d) Interest income and other receipts from commercial loans and installment obligations not secured by real or tangible personal property shall be attributed to this state if ~~and to the extent that~~ the borrower is a resident of this state.

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(e) Interest income and other receipts from a participating financial institution's portion of participation loans shall be attributed under the rules set forth in subsections (a) through (d).

(f) Interest income and other receipts including service charges from financial institution credit card and travel and entertainment credit card receivables and credit card holders' fees shall be attributed to the state to which such card charges and fees are regularly billed.

(g) Merchant discount income derived from financial institution credit card holder transactions with a merchant shall be attributed to the state in which the merchant is located. In the case of merchants located within and without this state, only receipts from merchant discounts attributable to sales made from locations within the state shall be attributed to this State. It shall be presumed, subject to rebuttal, that the location of a merchant is the address shown on the invoice submitted by the merchant to the taxpayer.

(h) Receipts from the performance of ~~fiduciary and other~~ services are attributed to this state if ~~the services are consumed or used in this state~~ :

(i) the service receipts are loan related fees and the borrower resides in this state;

(ii) the service receipts are deposit related fees and the depositor resides in this state;

(iii) the service receipts are third party financial institution check processing fees and the third party financial institution resides in this state;

(iv) the service receipt is a brokerage fee and the brokerage account is maintained at an office of the financial institution located in this state;

(v) the service receipts are fees related to estate or trust services and the executor or trustee resides in this state or, if there are two or more executors or trustees, the executor or trustee primarily responsible for administering the estate or trust is located in this state; or

(vi) the service receipt is associated with the performance of any other service not identified above and the service is primarily performed in this state.

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(i) Receipts from the issuance of travelers checks and money orders shall be attributed to the state in which such checks and money orders are purchased.

(j) Receipts from investments of a financial institution in securities of this state, its political subdivisions, agencies and instrumentalities shall be attributed to this state.

(k) Receipts from investments of a financial institution in other securities and from money market instruments shall be apportioned to this state based upon the ratio that total deposits from this state, its residents, its political subdivisions, agencies and instrumentalities bear to the total deposits from all states, their residents, their political subdivisions, agencies and instrumentalities. ~~In the case of an unregulated financial institution subject to this regulation, such receipts shall be apportioned to this state based upon the ratio that its gross business income earned from sources within this state bears to gross business income earned from sources within all states. For purposes of this subsection, deposits made by this state, its residents, its political subdivisions, agencies and instrumentalities shall be attributed to this state, whether or not such deposits are accepted or maintained by the taxpayer at locations within this state.~~

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(1) All receipts located by this rule in a State without jurisdiction to tax shall be excluded from both the numerator and the denominator of the receipts factor.

(3) Property Factor. In general.-- The property factor is a fraction, the numerator of which is the average value of the taxpayer's real and tangible personal property owned or rented and used in and intangible property attributed to this State during the tax period and the denominator of which is the average value of all the taxpayer's real and tangible personal property owned or rented and used in and intangible property attributed to all states during the tax period. For purposes of this regulation, the value of property owned by the taxpayer shall be its federal income tax basis, without diminution for bad debt reserves; the value of property rented by the taxpayer shall be eight times its net annual rental rate. The net annual rental rate for any item of rented property is the annual rate paid by the taxpayer for such property, less the aggregate annual subrental rates paid by subtenants of the taxpayer. Intangible personal property shall be included at its tax basis for federal income tax purposes. Goodwill shall not be included in the property

factor. The numerator of the property factor shall include, in addition to items otherwise assignable under [here include your state cite to the Multistate Tax Compact or other applicable state law], the following:

(a) Coin and currency located in this state shall be attributed to this state.

(b) Lease financing receivables shall be attributed to this state if and to the extent that the property is located within this state.

(c) Assets in the nature of loans which are secured by real or tangible personal property shall be attributed to this state if ~~and to the extent that~~ the security property is located within this state. In the event such security property is located in two or more states, it shall be deemed to be located in the state having the greatest property values.

(d) Assets in the nature of consumer loans and installment obligations which are unsecured or secured by intangible property shall be attributed to this state if the loan was made to a resident of this state.

(e) Assets in the nature of commercial loan and installment obligations which are unsecured or secured by intangible property shall be attributed to this state if ~~and to the extent that~~ the borrower is a resident of this state.

(f) Assets in the nature of funds deposited by one financial institution in another financial institution shall be attributed to this state if the depositor is a resident of this state.

(g) A participating financial institution's portion of a participation loan shall be attributed under the rules set forth in subsections (b) through (e).

(h) Financial institution credit card and travel and entertainment credit card receivables shall be attributed to this state if such credit card charges and fees are regularly billed to a resident of this state.

(i) Assets in the nature of securities of this state, its political subdivisions, agencies and instrumentalities shall be attributed to this state.

(j) Assets in the nature of securities and money market instruments shall be apportioned to this state based upon

the ratio that total deposits from this state, its residents, its political subdivisions, agencies and instrumentalities bear to the total deposits from all states, their residents, their political subdivisions, agencies and instrumentalities. In the case of an unregulated financial institution subject to this regulation, such receipts shall be apportioned to this state based upon the ratio that its gross business income earned from sources within this state bears to gross business income earned from sources within all states. For purposes of this subsection, deposits made by this state, its residents, its political subdivisions, agencies and instrumentalities shall be attributed to this state, whether or not such deposits are accepted or maintained by the taxpayer at locations within this state.

(j) (k) All property located by this rule in a State without jurisdiction to tax shall be excluded from both the numerator and the denominator.

(4) Payroll Factor. In general. -- The payroll factor is a fraction the numerator of which is the total amount paid by the taxpayer for compensation during the year, and the denominator of which is the total amount of compensation paid in every state.

(a) Neither the numerator nor the denominator of the payroll factor shall include ~~wages~~ compensation paid to an employee in a State without jurisdiction to tax.

(D) Special Rules. If the allocation and apportionment provisions of this regulation do not fairly represent the extent of the taxpayer's activity in this state, the taxpayer may petition for or the tax administrator may require, in respect to all or any part of the taxpayer's business activity, if reasonable:

1. separate accounting;
2. the exclusion of any one or more of the factors;
3. ~~the~~ inclusion of one or more additional factors which will fairly represent the taxpayer's business activity in this state; or
4. the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

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Proposed Amendments (1/89)

Multistate Tax Commission
July, 1987

DRAFT

PROPOSED REGULATIONS FOR THE ATTRIBUTION OF THE INCOME OF
FINANCIAL INSTITUTIONS.

(A) Definitions. Except as specifically defined herein, all terms used in this regulations shall have the same meaning as such terms have under [here include your state cite to the Multistate Tax Compact or other applicable state law] and the rules and regulations promulgated thereunder.

- (1) "Receipts" for the purpose of the receipts factor, means gross income, including net taxable gain on disposition of assets (including securities, loans, personal and real property and money market transactions) when derived from transactions and activities in the regular course of the taxpayer's trade or business.
- (2) "Participation Loans" means a loan in which more than one lender is a creditor to a common borrower.
- (3) "Securities" means United States Treasury securities, obligations of United States Government agencies and corporations, obligations of State and political subdivisions, corporate stock and other corporate securities, participations in securities backed by mortgages held by United States or State government agencies, loan-backed securities and similar investments to the extent that such investments are reflected as assets under generally accepted accounting principles.
- (4) "Money Market Instruments" means Federal funds sold and securities purchased under agreements to resell, commercial paper, banker's acceptances, and purchased certificates of deposit and similar instruments to the extent that such instruments are reflected as assets under generally accepted accounting principles.
- (5) "Property Located in this State"
 - (a) Tangible Property: General Rule.-- Except as otherwise provided in this section, tangible and real property which is security for a loan or property subject to a lease, shall be considered to be located in the State in which such property is physically situated. It shall be presumed, subject to rebuttal, that the property is

physically situated in the same state as the billing address of the borrower or lessee.

(b) Moveable tangible property.-- Tangible personal property which is characteristically moving property, such as motor vehicles, rolling stock, aircraft, vessels, mobile equipment, and the like shall be considered to be located in a State if:

(i) the operation of the property is entirely within the state; or

(ii) the operation of the property is in two or more states, but the principal base of operations from which the property is sent out is in the state. It shall be presumed, subject to rebuttal, that the location of operation of the property and the principal base of operations from which the property is sent out shall be ~~that duly certified in writing by the lessee or borrower in the same state as the~~ billing address of the borrower or lessee.

(6) "Exercising a Corporate Franchise or Transacting Business in a State." A financial institution is exercising a corporate franchise or transacting business in this state if:

(a) it has a place of business in this state;

(b) it has employees, representatives or independent contractors conducting business activities in its behalf in this state; or,

(c) it engages in regular solicitation in this state (whether at a place of business, by travelling loan officers or other representatives, by mail, by telephone or other electronic means), and the solicitation results in the creation of a depository of direct debtor/creditor relationship with a resident of this state. For purposes of this regulation, mere processing or transfer through financial intermediaries of checks, credit card receivables, commercial paper and the like does not create a debtor/creditor relationship.

A financial institution is presumed, subject to rebuttal to be engaged in regular solicitation within this state if it has entered into any of the relationships listed in subsection (c) above with ~~20~~ 100 or more residents of this state during any tax period or if it has \$5,000,000 or more of assets attributable to sources within this state at any time during the tax period.

(7) "Taxpayer" means a financial institution which is subject to taxation in a state because it is exercising its corporate franchise, or is transacting business in a corporate or organized capacity in the state, and has gross income attributable under this regulation to sources within this state.

(8) "Subsidiary" means a corporation whose voting stock is more than 50% owned, directly or indirectly, by a financial institution.

(9) "Holding Company" means any corporation subject to [insert citation of the state law governing the creation of bank holding companies], or registered under the Federal Bank Holding Company Act of 1956, as amended, or registered as a savings and loan holding company under the Federal National Housing Act, as amended.

(10) "Regulated Financial Corporation" means an institution, the deposits or accounts of which are insured under the Federal Deposit Insurance Act or by the Federal Savings and Loan Insurance Corporation, any institution which is a member of a Federal Home Loan Bank, any other bank or thrift institution incorporated or organized under the laws of the United States, any State or any foreign country which is engaged in the business of receiving deposits or which holds a bank charter, any corporation organized under the provision of 12 U.S.C. sections 611 to 631 (Edge Act Corporations), and any agency of a foreign depository as defined in 12 U.S.C. section 3101.

(11) "Business of a Financial Institution" includes the following:

(a) the business that a regulated financial corporation may be authorized to do under state or federal law or the business that its subsidiary is authorized to do by the proper regulatory authorities.

(b) the business that any corporation organized under the authority of the United States or organized under the laws of this state or any other state or country does/or has authority to do which is substantially similar to the business which a corporation may be created to do under [insert citations of state's laws governing the creation of banks and trust companies, industrial banks, savings and loan association, etc.] or any business which a corporation or its subsidiary is authorized to do by said laws.

(c) the business that any corporation organized under the authority of the United States or organized under the laws of this state or any other state or country does/or has authority to do if such corporation derives more than fifty percent of its gross income from lending activities (including discounting obligations) in substantial competition with the businesses described in subsections (a) and (b) above. For purposes of this subsection, the computation of the gross income of a corporation shall not include income from nonrecurring, extraordinary items.

(12) "Financial Institution" includes the following:

(a) A holding company.

(b) Any regulated financial corporation.

(c) Any other corporation organized under the laws of the United States or organized under the laws of this state or any other state or country which is carrying on the business of a financial institution.

~~(13) "Place of consumption or use of services" means the state in which the benefits of the services are received. If such benefits are received in more than one state, the receipts from those benefits shall be apportioned to this state pro rata according to the portion of the benefits received in this state.~~

~~(14)~~ (13) "Borrower" means the individual or entity who is primarily liable on a debt instrument. If more than one individual or entity is primarily liable on a debt instrument, each such individual or entity shall be considered the borrower to the extent of its interest in the debt instrument. For purposes of this regulation, a partnership shall be treated as a ~~group of individuals~~ separate entity.

~~(15)~~ (14) "Deposit" means:

(a) the unpaid balance of money or its equivalent received or held by a financial institution in the usual course of business and for which it has given or is obligated to give credit, either conditionally or unconditionally, to a commercial, checking, savings, time, or thrift account whether or not advance notice is required to withdraw the credited funds, or which is evidenced by its certificate of deposit, thrift certificate, investment certificate, or certificate of indebtedness, or other similar name, or a certificate of

indebtedness, or other similar name, or a check or draft drawn against a deposit account and certified by the financial institution, or a letter of credit or a traveler's check on which the financial institution is primarily liable; provided, that, without limiting the generality of the term "money or its equivalent" any such account or instrument must be regarded as evidencing the receipt of the equivalent of money when credited or issued in exchange for checks or drafts or for a promissory note upon which the person obtaining any such credit or instrument is primarily or secondarily liable, or for a charge against a deposit account, or in settlement of checks, drafts, or other instruments forwarded to such bank for collection;

(b) trust funds received or held by such financial institution, whether held in the trust department or held or deposited in any other department of such financial institution;

(c) money received or held by a financial institution, or the credit given for money or its equivalent received or held by a financial institution, in the usual course of business for a special or specific purpose, regardless of the legal relationship thereby established, including without being limited to, escrow funds, funds held as security for an obligation due to the financial institution or others (including funds held as dealers reserves) or for securities loaned by the bank, funds deposited by a debtor to meet maturing obligations, funds deposited as advance payment on subscriptions to United States Government securities, funds held for distribution or purchase of securities, fund held to meet its acceptances or letters of credit, and withheld taxes; provided, that there shall not be included funds which are received by the financial institution for immediate application to the reduction of an indebtedness to the receiving financial institution, or under condition that the receipt thereof immediately reduces or extinguishes such as indebtedness;

(d) outstanding drafts (including advice or authorization to charge a financial institution's balance in another such institution), cashier's checks, money orders, or other officer's checks issued in the usual course of business for any purpose, but not including those issued in payment for services, dividends, or purchases or other costs or expenses of the financial institution itself.

(e) money or its equivalent held as a credit balance by a financial institution on behalf of its customer if such entity is engaged in soliciting and holding such balances in the regular course of its business.

(16) ~~(15)~~ "State" means a state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, or any territory or possession of the United States or any foreign country.

(17) ~~(16)~~ "Taxable in a State." For the purpose of the receipts factor, a taxpayer is taxable in another state if: (a) in that State, he is subject to a franchise tax measured by net income, a net income tax, a franchise tax for the privilege of doing business, or a corporate stock tax, or (b) that State has jurisdiction to subject the taxpayer to such a tax regardless of whether, in fact, the State does or does not.

(18) ~~(17)~~ "Resides/Residence/Resident." A person shall be considered to reside or make his or her residence in or be a resident of a state if, in the case of an individual, he/she resides there for more than ~~100~~ 182 days in the relevant tax period. For purposes of this regulation, a partnership shall be treated as a ~~group of individuals, each of who is subject to the above residence rule~~ resident of the state of its commercial domicile. A corporation shall be considered a resident of the state ~~in which it has an~~ of the office out of which works the corporate officer making the deposit or applying for the loan. or other place of business during the relevant tax period. ~~For purposes of this regulation, a corporation may be a resident of more than one state.~~ An individual, partnership or a corporation shall be presumed, subject to rebuttal, to reside (be a resident of, make his residence at) at the address to which its statement of account is regularly mailed.

(18) "Loan Related Fees". For purposes of the receipts factor, loan related fees include all fees associated with the generation and administration of loans. Receipts from loan related fees which are either (a) "pooled" or aggregated for collective financial accounting treatment or (b) manually written as non-recurring extraordinary charges to be processed directly to the general ledger shall be attributed to a state based upon the ratio that total interest sourced to that state bears to total interest from all sources.

(19) "Deposit Related Fees". For purposes of the receipts factor, deposit related fees include all fees associated with the administration of deposit accounts. Receipts from deposit related fees which are either (a) "pooled" or aggregated for collective financial accounting treatment or (b) manually written as non-recurring extraordinary changes to be processed directly to the general ledger shall be attributed to a state based upon the ratio that total deposits sourced to that state bears to total deposits from all sources.

(20) "Third Party Check Processing Fees". For purposes of the receipts factor, third party check processing fees include fees charged by a loan originating financial institution to a third party financial institution buying the loan in instances where the loan originating financial institution continues to process loan payments.

(21) "Presumption". A presumption subject to rebuttal, as provided in this regulation, shall be rebuttable by clear and convincing proof established by either the financial institution or [here include title of your state taxing agency].

(B) Business Income. All income (taxable under the laws of this State) which arises from the business of a financial institution shall be deemed derived from transaction in the regular course of the taxpayer's business and subject to apportionment under this regulation. All such income which arises from activities of a financial institution which are not the business of a financial institution as defined in this rule shall be apportioned or allocated in accordance with the rules set forth in [here include your state cite to UDITPA or the Multistate Tax Compact].

(C) Apportionment of Business Income

(1) General Method.

(a) If a financial institution is carrying on the business of a financial institution both within and without this state, and if by reason of such business activity, it is taxable in another state, the portion of the net income (or net loss) arising from such business which is derived from sources within this state shall be determined by apportionment in accordance with this regulation.

(b) The tax applicable to financial institutions whose net income (or net loss) is apportionable according to the rules in this section shall be determined by multiplying the tax base by a fraction, the numerator of which is the sum of the receipts factor, the property factor, and the payroll factor as defined in this regulation and the denominator of which is three. If any factor(s) is missing, the remaining factors are added together and the sum is divided by the number of remaining factors. A factor is missing if both its numerator and denominator are zero, but it is not missing merely because its numerator is zero.

(2) Receipts Factor. In general. -- The receipts factor is a fraction, the numerator of which is the receipts of the taxpayer within this state during the tax period and the denominator of which is the total receipts of the taxpayer from all states in which the taxpayer is taxable during such tax period. The numerator of the receipts factor shall include, in addition to items otherwise assignable under [here include your state cite to the Multistate Tax Compact or other applicable state law], the following receipts attributable to this state:

(a) Receipts from the lease or rental of real or tangible personal property (including both finance leases and true leases) shall be attributed to this state if the property is located in this state.

(b) Interest income and other receipts from assets in the nature of loans which are secured primarily by real estate or tangible personal property shall be attributed to this state if such security property is located in this state. In the event such security property is located in two or more states, it shall be deemed to be located in the state having the greatest property values.

(c) Interest income and other receipts from consumer loans not secured by real or tangible personal property that are made to residents of this state (whether at a place of business, by travelling loan officer, by mail, by telephone or other electronic means) shall be attributed to this state.

(d) Interest income and other receipts from commercial loans and installment obligations not secured by real or tangible personal property shall be attributed to this state if ~~and to the extent that~~ the borrower is a resident of this state.

(e) Interest income and other receipts from a participating financial institution's portion of participation loans shall be attributed under the rules set forth in subsections (a) through (d).

(f) Interest income and other receipts including service charges from financial institution credit card and travel and entertainment credit card receivables and credit card holders' fees shall be attributed to the state to which such card charges and fees are regularly billed.

(g) Merchant discount income derived from financial institution credit card holder transactions with a merchant shall be attributed to the state in which the merchant is located. In the case of merchants located within and without this state, only receipts from merchant discounts attributable to sales made from locations within the state shall be attributed to this State. It shall be presumed, subject to rebuttal, that the location of a merchant is the address shown on the invoice submitted by the merchant to the taxpayer.

(h) Receipts from the performance of ~~fiduciary and other~~ services are attributed to this state if ~~the services are consumed or used in this state~~ :

(i) the service receipts are loan related fees and the borrower resides in this state;

(ii) the service receipts are deposit related fees and the depositor resides in this state;

(iii) the service receipts are third party financial institution check processing fees and the third party financial institution resides in this state;

(iv) the service receipt is a brokerage fee and the brokerage account is maintained at an office of the financial institution located in this state;

(v) the service receipts are fees related to estate or trust services and the executor or trustee resides in this state or, if there are two or more executors or trustees, the executor or trustee primarily responsible for administering the estate or trust is located in this state; or

(vi) the service receipt is associated with the performance of any other service not identified above and the service is primarily performed in this state.

(i) Receipts from the issuance of travelers checks and money orders shall be attributed to the state in which such checks and money orders are purchased.

(j) Receipts from investments of a financial institution in securities of this state, its political subdivisions, agencies and instrumentalities shall be attributed to this state.

(k) Receipts from investments of a financial institution in other securities and from money market instruments shall be apportioned to this state based upon the ratio that total deposits from this state, its residents, its political subdivisions, agencies and instrumentalities bear to the total deposits from all states, their residents, their political subdivisions, agencies and instrumentalities. ~~In the case of an unregulated financial institution subject to this regulation, such receipts shall be apportioned to this state based upon the ratio that its gross business income earned from sources within this state bears to gross business income earned from sources within all states. For purposes of this subsection, deposits made by this state, its residents, its political subdivisions, agencies and instrumentalities shall be attributed to this state, whether or not such deposits are accepted or maintained by the taxpayer at locations within this state.~~

(1) All receipts located by this rule in a State without jurisdiction to tax shall be excluded from both the numerator and the denominator of the receipts factor.

(3) Property Factor. In general.-- The property factor is a fraction, the numerator of which is the average value of the taxpayer's real and tangible personal property owned or rented and used in and intangible property attributed to this State during the tax period and the denominator of which is the average value of all the taxpayer's real and tangible personal property owned or rented and used in and intangible property attributed to all states during the tax period. For purposes of this regulation, the value of property owned by the taxpayer shall be its federal income tax basis, without diminution for bad debt reserves; the value of property rented by the taxpayer shall be eight times its net annual rental rate. The net annual rental rate for any item of rented property is the annual rate paid by the taxpayer for such property, less the aggregate annual subrental rates paid by subtenants of the taxpayer. Intangible personal property shall be included at its tax basis for federal income tax purposes. Goodwill shall not be included in the property

factor. The numerator of the property factor shall include, in addition to items otherwise assignable under [here include your state cite to the Multistate Tax Compact or other applicable state law], the following:

(a) Coin and currency located in this state shall be attributed to this state.

(b) Lease financing receivables shall be attributed to this state if and to the extent that the property is located within this state.

(c) Assets in the nature of loans which are secured by real or tangible personal property shall be attributed to this state if ~~and to the extent that~~ the security property is located within this state. In the event such security property is located in two or more states, it shall be deemed to be located in the state having the greatest property values.

(d) Assets in the nature of consumer loans and installment obligations which are unsecured or secured by intangible property shall be attributed to this state if the loan was made to a resident of this state.

(e) Assets in the nature of commercial loan and installment obligations which are unsecured or secured by intangible property shall be attributed to this state if ~~and to the extent that~~ the borrower is a resident of this state.

(f) Assets in the nature of funds deposited by one financial institution in another financial institution shall be attributed to this state if the depositor is a resident of this state.

(g) A participating financial institution's portion of a participation loan shall be attributed under the rules set forth in subsections (b) through (e).

(h) Financial institution credit card and travel and entertainment credit card receivables shall be attributed to this state if such credit card charges and fees are regularly billed to a resident of this state.

(i) Assets in the nature of securities of this state, its political subdivisions, agencies and instrumentalities shall be attributed to this state.

(j) Assets in the nature of securities and money market instruments shall be apportioned to this state based upon

the ratio that total deposits from this state, its residents, its political subdivisions, agencies and instrumentalities bear to the total deposits from all states, their residents, their political subdivisions, agencies and instrumentalities. In the case of an unregulated financial institution subject to this regulation, such receipts shall be apportioned to this state based upon the ratio that its gross business income earned from sources within this state bears to gross business income earned from sources within all states. For purposes of this subsection, deposits made by this state, its residents, its political subdivisions, agencies and instrumentalities shall be attributed to this state, whether or not such deposits are accepted or maintained by the taxpayer at locations within this state.

(→) (k) All property located by this rule in a State without jurisdiction to tax shall be excluded from both the numerator and the denominator.

(4) Payroll Factor. In general. -- The payroll factor is a fraction the numerator of which is the total amount paid by the taxpayer for compensation during the year, and the denominator of which is the total amount of compensation paid in every state.

(a) Neither the numerator nor the denominator of the payroll factor shall include ~~wages~~ compensation paid to an employee in a State without jurisdiction to tax.

(D) Special Rules. If the allocation and apportionment provisions of this regulation do not fairly represent the extent of the taxpayer's activity in this state, the taxpayer may petition for or the tax administrator may require, in respect to all or any part of the taxpayer's business activity, if reasonable:

1. separate accounting;
2. the exclusion of any one or more of the factors;
3. the inclusion of one or more additional factors which will fairly represent the taxpayer's business activity in this state; or
4. the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

pmp1:098:cnc

EXHIBIT B: 14

Minutes of April 19, 1989 Meeting - Chicago, IL

Multistate Tax Commission

Multistate Tax Commission
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Los Altos, CA 94022
Phone (415) 941-0556
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ALAN H. FRIEDMAN, General Counsel

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MINUTES OF MEETING WITH REPRESENTATIVES OF FINANCIAL INSTITUTIONS, CHICAGO, ILLINOIS, MULTISTATE TAX COMMISSION

APRIL 19, 1989

The meeting was called to order by Alan Friedman, General Counsel of the Multistate Tax Commission, at 9:00 a.m. The following representatives of financial institutions, state revenue departments, and the Multistate Tax Commission attended:

Financial Institution Representatives:

Robert E. Allison	National Bank of Detroit P.O. Box 33287 Detroit, MI 48232-5287
Joanne Ames	American Bankers Association 1120 Connecticut Ave. Washington, D.C. 20036
Jim Blackman	Firststar Corp. 777 East Wisconsin Ave. Milwaukee, WI 53202
James J. Engel	Ameritrust Co., N.A. Tax Counsel Dept. T-14 Cleveland, OH 44101-0937
Kristin A. Hall	Harris Trust and Savings Bank 111 West Monroe P.O. Box 755 Chicago, IL 60690
Steven A. Hinshaw	Banc One Corporation 100 East Broad Street Columbus, OH 43271-0251
Bruce C. Janovsky	The Northern Trust Company 125 South Wacker Drive Chicago, IL 60675
Henry S. Landon & John b. Truskowski	Keck, Mahin & Cate (for First City Texas) 8300 Sears Tower 233 South Wacker Drive Chicago, IL 60606-6589

Gene Mason

First Bank System
Minneapolis, MN

Thomas B. Williams

Indiana bankers Association
One North Capitol, Suite 315
Indianapolis, IN 46204

State Revenue Department Representatives:

Phil Aldape

Idaho State Tax Commission
P.O. Box 36
Boise, ID 83722

Lynn Chenoweth

Montana Department of Revenue
Mitchell Building
Helena, MT 59620

Cindy Chinnock

Oregon Department of Revenue
955 Center St., N.E.
Salem, OR 97310

Eric J. Coffill

California Franchise Tax Bd.
P.O. box 2229
Sacramento, CA 95810-2229

Jack DeYoung

Wisconsin Department of Revenue
P.O. box 8933
Madison, WI 53708

James A. Fry

South Dakota Department of Revenue
700 Governors Drive
Pierre, SD 57501

Manuel F. Gallegos

New Mexico Tax. and Rev. Dept.
P.O. Box 1671
Santa Fe, NM 87504

Stephen Krenkel

Minnesota Department of Revenue
Centennial Office Building
St. Paul, MN 55145

Multistate Tax Commission Representatives:

Alan Friedman

386 University Avenue
Los Altos, CA 94022

Paull Mines

444 No. Capitol St., N.W. #500
Washington, D.C. 20001

Others in Attendance:

John Malach

Ernst & Whinney
150 S. Wacker Drive
Chicago, IL 60606

Alan Friedman introduced the subject of a "proposed draft" of the Regulation for the Attribution of the Income of Financial Institutions by briefly outlining the history of the development of these regulations. That draft had been developed, working from the July 1987 MTC draft, but making the proposed changes suggested through Phil Plant of the Bank of America, as a result of the MTC Seattle meeting with financial institution representatives.

Friedman also described the MTC procedure established for the adoption of MTC regulations and the current intention of the MTC to have the "proposed draft" regulation be the subject of a formal hearing authorized by the Executive Committee of the MTC in time for the regulations to be reported to the full Commission in July of 1990 for possible action.

Friedman also noted that the MTC necessarily acknowledges the existence of the nexus issue and therefore encouraged the participants to avoid concentrating their comments on that issue to the exclusion of commenting on how the regulation could best be drafted. Friedman further stated it was unlikely that all money center states would adopt MTC's proposed apportionment approach to the taxation of in-state financial institutions without the new nexus concept in the proposal having survived a court challenge. A money center state would likely require assurance that the taxes collected under traditional nexus, but which would be lost to the money center state through apportionment, would be significantly replaced by inbound taxes.

Having made these introductory comments, Friedman invited specific comments on the "proposed draft" regulation that appeared in the October 1988 issue of the Multistate Tax Commission Review. A summary of the comments received is set forth below by category. Some comments may appear under more than one category when that comment was not easily categorized.

STATE EXPERIMENTATION HAS BEGUN: One state and at least two others were identified as either having adopted apportionment taxation of financial institutions or having such form of taxation under active consideration of its legislature. (Minnesota, Indiana and Oregon). Gene Mason of First Bank System indicated that they were still adjusting to the new concept of taxation in Minnesota. One major concern of Minnesota financials is the potential increase in the cost of capital to their customers. Other problems with respect to situsing of participations and syndications were currently being addressed by amendatory language to the Minnesota statute. The complexity of administering and complying with this new system of taxation was noted.

Impact of the new system of taxation was noted, including possible adverse impact on the availability of credit in the taxing state because (i) the secondary loan market was reluctant to accept loans from a taxing state for fear of becoming subject to tax; (ii) increased complexity in complying with apportionment taxation made out of state lenders reluctant to enter a taxing state's jurisdiction; (iii) the costs of compliance were passed on to the borrower which made the loan more expensive and possibly infeasible; (iv) double taxation existed due to out of state financial institutions being subject to non-apportioned taxation in their home state or other states.

NEXUS CONTINUES TO DRAW COMMENTS: Several comments and questions were raised by the banking representatives with regard to the nexus concepts inherent in the proposal:

Will the states which adopt the apportionment approach unnecessarily suffer revenue losses if MTC's nexus theory is not upheld in the courts?

Once a financial institution establishes nexus is that nexus established for all time?

Should the mere holding of a portfolio of loan documents generated within a taxing state, without more, establish nexus regardless of how the financial institution acquired the loans through secondary market, walk-in business outside of the taxing state, syndication, etc.?

Financial institutions need a P.L. 86-272 law, because out of state loan production officers are comparable to drummers.

The residence of a cardholder in the taxing state should not be equated with nexus, because all the work by the financial institution is completed out of state.

Much of the concern over nexus would be alleviated by raising the nexus standards of the proposal: 100 residents or \$5,000,000 in assets is much too low.

Should a bank which develops cardholder accounts in a taxing state but who sells such accounts to an unrelated financial institution retaining only the servicing obligation of such accounts be subject to apportionment taxation?

Many banking circumstances include the presence of a bank within a large population center which is very close to a state line. These banking circumstances ensure that considerable banking will occur across state lines without the bank ever developing a presence within a border state which has adopted apportionment taxation of financial institutions.

Will a financial institution which only processes credit

card accounts within a taxing state for other financial institutions be subject to state apportionment taxation?

What constitutes regular solicitation of credit card holders which will subject a financial institution to nexus within a state imposing an apportionment tax?

ADMINISTRATIVE BURDENS ARE ALLEGED TO BE ENORMOUS: The burden of compliance required by the proposed regulation is suggested to be "nightmarish". The following comments were offered by the banking representatives as to the administrative requirements of the proposal:

Attempting to track the income of a financial institution with loan portfolios involving movables is too difficult, especially when you add complexities involving different states of incorporation, commercial domicile and administrative offices.

Too much work is involved for the amount of revenues anticipated to be received by the states. A major New York bank undertook a study to determine its tax liability under the Multistate Tax Commission "draft proposal" and found that its over all tax liability was increased negligibly. (The reporter of this tax study could not tell the assembled group whether the study disclosed major shifting in tax revenues from one state to another.)

A one-stop filing and payment system might remove considerable opposition to the proposal.

The proposal should specifically allow the use of averages and should ensure that the specific averages authorized will be uniform throughout the taxing states. Otherwise the real potential exists that states will adopt different averaging conventions, thereby increasing the complexity of an otherwise already complex regulation. One suggestion was to permit the use of daily general ledger balances for the denominator, at least with respect to the asset (property) side of the formula.

Financial institutions will find it easier to play audit lottery than to develop systems to comply, because the cost of a new system to comply will be much greater than the penalties and interest assessed in an audit.

In valuing the hard assets of a financial institution the regulation should require the use of original cost rather than adjusted basis under the federal tax laws, because of the difficulty in determining adjusted basis.

Banks do not pay taxes, but they collect taxes from their

customers. The costs of compliance will inevitably be passed on to the financial institution's customers.

The economic effect of the proposal should be studied before implementation, and the administrative burdens should be weighed in light of the economic gain to the states.

A credit or at least a deduction of taxes imposed by the other states should be built into the proposal.

SOME POLICY AND TECHNICAL ISSUES RAISED BY THE PROPOSAL: Several financial institution representatives in attendance offered the following comments and questions directed at the tax policy implications of the proposal, as well as to problems of a more technical nature:

Money center states will not adopt apportionment taxation of financial institutions for fear of a loss of revenues. This lack of uniformity will result in double taxation.

Varying tax rates will influence the possible opposition of financial institutions to the proposal.

The payroll factor of the proposal, as contrasted by the receipts and property factors, is not grossed up to reflect the margin built into the extension of credit to remunerate the financial institution for extending the credit. As a result, the proposal does not adjust enough for the fact that most of the activities and costs generating financial income occur outside of the non-domiciliary state which has adopted apportionment taxation.

The receipts factor in essence duplicates the property factor, because the sourcing rules for these two factors essentially operate in parallel.

To what extent has the "proposed draft" regulation considered income generated by the utilization of ATMs?

Will a bank which packages a loan within a taxing state and then sells 100% participation but still services the loan be subject to state apportionment taxation?

Is a financial institution "taxable in another state" within the meaning of the "proposed draft" regulation, if there is not the requisite nexus present? Thus, what effect will activities in such a state have on both the numerator and the denominator of the apportionment fractions?

In order to ensure as much uniformity as possible, should there be a triggering mechanism built into the regulation so that its effectiveness in a state will be conditioned upon the regulation being adopted in a certain number of states?

Is it fair apportionment practice to apportion out loan fees (estimated by one institution to represent 73% of non-interest income) when most of the services are being performed in the domiciliary state?

Should the relocation of a debtor after the issuance of a credit card or loan create nexus in the state to which the debtor has moved? (Could a determination of nexus be made as of a certain date, e.g., September 30th of the prior calendar year, to create more certainty?)

Is the definition of Section A(16)(b) surplusage?

How should money market funds be treated?

POSSIBLE FEDERAL LEGISLATION SOUGHT:

The American Bankers Association has explored the possibility of securing federal legislation to deal with the perceived difficulties of the proposal. The ABA has determined to seek federal legislation which would adopt the American Bar Association's 1981 legislative recommendation on nexus.

Federal legislation authorizing one-stop filing and payment to the states is another proposal on which the ABA may have some interest.

COOPERATION AMONG THE COMPETING INTERESTS POSSIBLE:

The American Bankers Association seeks to cooperate with the MTC to determine a workable solution to the state taxation of financial institutions.

The ABA indicated a willingness to investigate whether the major New York bank study referenced above under Administrative Burdens would be available to the MTC for examination.

Tax and operational managers of financial institutions should be allowed the opportunity to review the proposal and to make comments thereon, because these hands-on people will be able to give significant commentary.

STATE REVENUE DEPARTMENT REPRESENTATIVES' COMMENTS:

Jim Frey (South Dakota Department of Revenue):

South Dakota, a member state of the MTC, which has developed a considerable industry that processes credit card accounts. It opposes the concept of state apportionment taxation of

financial institutions.

South Dakota is concerned about the regulation's complexity and inherent difficulty in administration, because (i) developing an audit trail will be difficult and (ii) lower voluntary compliance may result where the cost of compliance (cost of developing systems) will likely exceed the anticipated costs of penalties and interest which would be assessed for non-compliance.

South Dakota believes full implementation of the regulation will not occur for some time, because it will be necessary to uphold the regulation in court challenges which will be extensive and expensive.

South Dakota desires to preserve as much as possible its control over the development of local conditions which are fostering its status as a major credit card processing center. Adoption of the regulation will potentially interfere with a state's ability to control its own economic policy.

South Dakota believes that the recent history of each state skewering its apportionment factors (e.g., Iowa's single factor, Minnesota's 70% sales factor, California's possible adoption of a double weighted sales factor) does not bode well for the proposed regulation. South Dakota anticipates each state will skewer the apportionment factors in its adoption of the proposed regulation for its own special benefit, thereby exacerbating non-uniformity in the taxation of financial institutions.

South Dakota's first choice is to adopt a nexus standard which requires minimal contacts in a physical sense within a taxing state before nexus attaches. Additionally, South Dakota would like to see the receipts and property factors in the proposal adjusted, because both factors point in the same direction. One approach would be to exclude some of the listed intangibles from the property factor.

South Dakota would favor a slower implementation of the proposal by taking various segments of the proposal and adopting them piecemeal over time. Gradual implementation of the proposal would allow credit card operations to be phased in at the last.

Cindy Chinnock (Oregon Department of Revenue):

Oregon noted that there were pressures within the state which were prompting its state legislature to undertake the possible adoption of apportionment taxation of financial institutions.

Oregon's treatment of apportionment taxation for financial

institutions was driven by the need for uniformity in the taxation of these multistate businesses and by the changing nature of the modern world economy. The need for uniformity and recognition of the changing world economy is strong enough to propel consideration of the issue, even though apportionment taxation of financial institutions is revenue neutral. The changing world economy requires Oregon to adopt a method of taxation which will be fair and equitable. Intangibles must now begin to be considered.

Oregon foresaw a reasonable lead time before apportionment taxation of financial institutions was adopted.

Lynn Chenoweth (Montana Department of Revenue):

Montana also believes that uniformity and equity requires that something be done to address the issue of taxation of financial institutions. Relief is now being granted to in-state financial-type institutions where traditional apportionment factors produce an unfair result. This relief builds pressure for dealing more effectively with out-of-state financial institutions which are operating within the state's economy.

Phil Aldape (Idaho State Tax Commission):

Idaho similarly indicated that the in-state pressures were building for some resolution of the issue of state taxation of financial institutions.

Ted Middle (Colorado Department of Revenue):

Colorado indicated that it was not actively considering the independent adoption of apportionment taxation of financial institutions; but that the MTC proposal would be considered after it was adopted, as long as it was not perceived as an anti-economic development proposal.

Eric Coffill (California Franchise Tax Board):

California is undertaking a study of its financial institutions which would likely be made available to the MTC, except for those parts which must be kept confidential under California law.

Stephen Krenkel (Minnesota Department of Revenue):

Minnesota has recently passed amendatory legislation to its banking statute to address some of the industry concerns.

CONCLUSION: Friedman concluded the meeting by thanking all present for their participation and input. He invited written comments that offered solutions to the problems raised by the

proposal. Friedman noted the MTC is sharing its proposal for the purpose of securing constructive comments; and he requested interested members of the financial community to be specific in its criticisms and, above all, propose alternative solutions. Friedman indicated that generalized criticisms of the complexity of the proposal were not that useful, if the critic did not suggest specific alternatives to avoid the complexity.

Friedman finally noted that while some of the comments today had been directed at economic and tax policy, those were not the direct concerns of the MTC staff at this time; but that such comments would nevertheless play an important part in the process. Friedman noted that economic and tax policy issues were the special province of the full Commission and the member states.

Comments for further consideration by the staff of the MTC at this stage can be forwarded as follows:

**Alan Friedman
General Counsel
Multistate Tax Commission
386 University Avenue
Los Altos, CA 94022**

EXHIBIT B: 15

**Letter from James A. Fry
(South Dakota Department of Revenue)
(May 5, 1989)**



May 5, 1989

Alan Friedman
General Counsel, Multistate Tax Comm.
444 North Capital Street, NW
Suite 500
Washington, DC 20001

RE: Bank Income Allocation Regulations

Dear Alan:

Thank you again for the opportunity to express our views on the proposed allocation of income for financial institutions purposes. We appreciate your openness and your sympathy with our rather difficult position. We also appreciate the willingness of the MTC to consider changes in the proposed regulation or the implementation thereof which might be beneficial to South Dakota.

Aside from the fiscal implications of the regulation, we would like to reiterate our concern regarding the problems which will be created for each state because of the administrative complexity of this regulation. As we stated earlier, we believe that voluntary taxpayer compliance will suffer dramatically. If this regulation is adopted in its present form, taxpayers will be confused or will be unwilling to expend the necessary monies to provide the accounting and record keeping necessary to track the dollars involved. They will adopt a catch-me-if-you-can mentality gambling that their particular firm will not be audited and if it is, the auditors will analyze what records are available, complete a return and bill the taxpayer. The penalty and interest may very well be less than the administrative costs incurred in proper record keeping and reporting. Properly auditing such taxpayers will also be quite difficult and time consuming in that the information available will often be insufficient to allow an auditor to reconstruct the necessary records upon which a sustainable assessment can be made.

This letter would also restate our concern that this regulation sets economic policy rather than tax policy for individual states and is a disincentive to economic development. This regulation would shift the benefits of economic development to states based upon the population size rather than upon any success a state may have in



EXHIBIT B: 16

**Letter from J. Daniel Vandermark
(Norwest Corporation) (May 10, 1989)**

J. Daniel Vandermark
Vice President
Tax

NORWEST CORPORATION

Norwest Corporation
Norwest Center
Sixth and Marquette
Minneapolis, Minnesota 55479-1013
612/667-0612

May 10, 1989

Mr. Eugene Corrigan
Multistate Tax Commission
1790 30th Street, Suite 314
Boulder, CO 80301-1024

RE: Proposed MTC Apportionment Regulations

Dear Mr. Corrigan:

Thank you for requesting our comments on the proposed MTC apportionment regulations. I apologize for the delay in answering.

I have enclosed a memorandum prepared by one of the tax attorneys on my staff. It represents our views and suggestions on implementing the proposed regulations. In short, we do not object to the market state approach of sourcing income. However, as pointed out in the attached memorandum, some of the provisions would be extremely difficult to implement in their present form.

If you have any questions or matters which you would like to discuss, please address them to the author of the memorandum. Again, thank you for considering our comments.

Very truly yours,



J. Daniel Vandermark
Vice President - Tax

JDV:cas

Enclosure

MEMORANDUM TO THE FILES

RE: Comments on MTC Financial Apportionment Regulations

Jurisdiction to Tax

The MTC draft regulations provide that a financial institution will be subject to tax if it is exercising a corporate franchise or transacting business in the MTC state. A financial institution is exercising a corporate franchise or transacting business if it engages in "regular solicitation" in the MTC state. Regular solicitation includes "by mail, by telephone or other electronic means" if the solicitation results in the creation of a depository or direct debtor/creditor relationship with a resident of the MTC state. It is presumed that a financial institution is engaged in regular solicitation in the MTC state if it: (1) has entered into depository or debtor/creditor relationships with 20 or more residents of the MTC state during any tax period; or (2) has \$5 million or more of assets attributable to sources within the MTC state at any time during the tax period.

This "jurisdiction to tax" provision of the MTC draft regulations falls short of the nexus requirements established under the Due Process Clause and the Commerce Clause of the U.S. Constitution. Extensive research reveals no U.S. Supreme Court case which has gone so far as to say that nexus exists and due process is satisfied by an out-of-state corporation merely obtaining business from residents of the taxing state without some sort of physical presence in the state. Physical presence can be established through either an actual physical presence, such as a brick and mortar presence in the state, or by an imputed physical presence such as a presence through employees, agents, independent contractors, or through the use of in-state services such as collection agencies, credit bureaus and state court systems. However, no case has established a state's jurisdiction to tax a business' income where an out-of-state company's only activity in the state is solicitation of residents by mail, telephone or other electronic means. Use of the mail and telephone has long been a constitutionally protected activity of interstate commerce. Therefore, the MTC regulations' "jurisdiction to tax" provision is unconstitutional because it does not satisfy either the Due Process Clause or the Commerce Clause of the U.S. Constitution. The fact that all of the MTC states may implement the regulations cannot overcome the due process requirements.

The presumption in the jurisdiction provision that a financial institution is subject to tax if it creates a depository or direct debtor/creditor relationship with 20 or more residents is absolutely without constitutional support. The presumption makes no attempt to examine the in-state activities of an interstate business; it only looks at a superficial number of customers. A financial institution could have a bank located in State A on the border of State B. This border bank may receive deposits or give loans to 20 residents of State B without having any physical presence or solicitation activities in State B. State B residents may have simply chosen, of their own free will, to deposit funds or obtain loans from the State A bank without the State A bank making any attempt to obtain that business. In such a case the MTC regulations would grant State B jurisdiction to tax the bank. However, such a tax would clearly violate the due process requirements.

The jurisdiction provision of the draft regulations would appear to subject an out-of-state financial institution to taxation even if the institution had merely purchased a security sourced to an MTC state on the secondary market. Such a secondary market purchase could produce a direct debtor/creditor relationship subjecting the institution to tax under the regulations. It is doubtful that such a tax would pass muster under a constitutional due process test, without any further activity on the part of the secondary market purchaser. A secondary market exception should be inserted in the draft regulations for both nexus and factor purposes.

The jurisdiction requirements should be written to reflect present due process requirements. They should not attempt to put taxpayers into a litigation position just so MTC states can attempt to overturn present case law.

Sourcing of Income

Receipts Factor – Assignment of Service Fees

The Committee appears to be taking the general view that "service" receipts should be assigned to the market state *if* the consumer of the services is an individual. Otherwise, the service receipts should be assigned to some other state. If the MTC and the Committee believe service receipts should be assigned to a state based on a customer's residence, such assignment should be uniform without regard to the customer entity involved.

The MTC and the Committee should bear in mind the administrative expense of implementing the apportionment regulations. Systems, software, personnel and procedure all must be implemented to examine where income should be sourced. Therefore, the apportionment regulations should encourage compliance with the least expense possible. For instance, banks should not have to look at what type of entity is involved in determining where a loan is sourced. Whether a borrower or depositor is a corporation, a partnership, a Trust, or an individual should not make a difference when sourcing receipts. The least expensive manner of sourcing would be to have the bank source the income based on the customer's address (information which the bank has available). It is doubtful that banks or customers (to whom sourcing is irrelevant) would attempt to circumvent such a system.

The regulations should attempt to assign receipts uniformly, without regard to entity. The proposed system, would cause banks to incur large expenses in order to comply. Also, the Committee should remember that sourcing in the manner provided by the draft regulations and the Committee notes would have to be implemented, for example, with the loan officer making the loan. The officer, in many cases, would lack the necessary information or knowledge or both to identify to the bank's tax department, where the fees should be sourced. For instance, an officer may not know where an account is maintained, or may not be able to determine corporate domicile if that were to determine sourcing.

Partnerships

The draft regulations contain provisions which source income to the market state; where the customer resides. For purposes of sourcing income the regulations state that a partnership is treated as a group of individuals. Thus, each partner's residence becomes important to properly source income. This imposes a hardship on financial institutions doing business with partnerships. The bank may not be able to obtain the residence of each partner. Also, it would be a substantial administrative burden to source income based on the residence of *each* partner rather than the location of the partnership. Finally, it seems much more relevant, as well as reasonable, to look at the location of the partnership instead of all the partners.

The partnership is really the recipient of the loan (for purposes of sourcing income). Surely, an analogy can be drawn between a partnership and a closely-held corporation where the shareholders personally guarantee loans. The MTC draft regulations would look to the corporation's commercial domicile for sourcing income yet in the partnership case the regulations would require a determination of each partner's residence. Consequently, a virtually identical transaction is treated differently under the draft regulations. Income from unsecured partnership loans should be sourced to the state where the partnership office obtaining the loan is located without reference to a partner's residence.

Corporate Unsecured Debt

The Committee's suggestion on sourcing corporate unsecured debt is not administratively feasible. First of all the committee says that the loan and its proceeds should be sourced for both the property and receipts factor to the state where the borrower's officer or employee is located who negotiated the loan. If that state doesn't have jurisdiction to tax then the loan and its proceeds are sourced to the state where the office of the loan officer who worked on the loan is located. Finally, if the officer doesn't work out of an office, the loan and its proceeds are sourced to the state of the officer's residence (ignoring the fact that such state, also, may not have jurisdiction to tax). The Committee also states that this information should be easy to obtain.

While the information may be easy to gather implementing this pyramid sourcing scheme would be a nightmare. Throwback rules and throwout rules, while being constitutionally questionable, are extremely hard to handle from an administrative viewpoint. The cost of systems to handle such a pyramid sourcing mechanism would be prohibitive, thereby encouraging noncompliance due to an inability to comply.

In addition, the Committee's suggestion that the "statement rule" is unacceptable because banks would manipulate sourcing by conspiring with large customers to send statements to a low tax or no tax jurisdiction is offensive. Most loan officers would not be familiar enough with state apportionment rules to ever think of such a scheme.

The Committee and the MTC should draft rules which can be inexpensively applied by the banks. The "statement rule" can be; the 3-layer approach presently being contemplated by the Committee cannot be.

Assignment of Receipts from Securities

If the MTC and the Committee have abandoned the deposits factor, deposits should not be used to measure other factors, such as receipts and property. The use of deposits to establish receipt and property factors will require banks to maintain information on deposits to the same extent they must maintain receipt, property and payroll information. As with other provisions, this causes an increased administrative burden to be placed on the banks.

Securities investment is for the most part, a low risk, low payroll, low cost activity. It really should not be used to measure the income attributable to a state. Receipts from securities should be discarded from the receipts factor. The nature of securities investment is not relative to a bank's in-state activity.

State Obligations

According to the draft regulations, state securities, like other securities, are sourced using a deposits formula. The arguments used in the discussion dealing with receipts from securities is also applicable here. In addition, the provision as it applies to state obligations is unconstitutional. An example of unconstitutional multiple taxation in violation of the U.S. Constitution's Commerce Clause can be found in the draft regulation provision dealing with the inclusion of State securities in the receipts and property factors. The draft regulations require that securities of the MTC State be attributed to that state. In addition, securities of another state are apportioned to the MTC state based on the ratio of deposits of the MTC state to deposits from all states. Thus, State A would base its receipts and property factor on 100% of its obligations as well as some percentage of State B's securities. The result being that more than 100% of State A & B securities and their income are included in the combined factors of states A and B.

Example:

Property Factor	
Total State A Deposits	\$ 9,000,000
Total State B Deposits	1,000,000
Total Deposits	<u>\$10,000,000</u>
State A Securities	\$ 100,000
State B Securities	100,000
Total State Securities	<u>\$ 200,000</u>

State A		
	100% State A Securities	\$100,000
	Apportioned % of State B Securities (State A Deposits ÷ Total Deposits) × State B Securities	<u>90,000</u>
	Total State Securities in State B Property Factor	<u>\$190,000</u>
State B		
	100% State B Securities	\$100,000
	Apportioned % of State A Securities (State B Deposits ÷ Total Deposits) × State A Securities	<u>10,000</u>
	Total State Securities in State B Property Factor	<u>\$110,000</u>
	Sum of State Securities Included in both State A and State B Property Factors	\$300,000
	Total State Securities	<u>200,000</u>
	Apportioned State Securities Causing Multiple Taxation	<u>\$100,000</u>

Thus, the present apportionment formula causes multiple taxation by including more than 100% of state securities in MTC states' combined receipts and property factors thereby increasing the factors and the apportionment percentage for all MTC states. Such a provision violates the Commerce Clause and should be dropped from the draft regulations. State securities should be treated like unsecured loans and be sourced to the state issuing the securities (without a throwout or throwback clause), in the alternative they should be dropped from all factors.

Purchased Obligations

Purchased obligations, obtained through secondary markets, should not be assigned to a state with which a bank has no other contact. Such purchased obligations do not reflect a bank's activity in that state, and, as stated above, such sourcing raises constitutional nexus problems. Purchased obligations should be removed from the factors.

Throwout Provisions

The draft regulations also contain "throwout" provisions which dictate that factors which are attributed to a state without jurisdiction to tax should be excluded from both the numerator and denominator of the appropriate factor. Of course, the items which are attributable to another state would not be included in the numerator of the MTC state factor anyway. Thus, the effect of the throwout provision is to decrease the denominator without decreasing the numerator causing an increase in the factor and apportioning a larger portion of income to the

MTC state. These throwout provisions can result in discrimination in violation of the Commerce Clause of the U.S. Constitution. A tax on interstate commerce must be fairly apportioned under the Commerce Clause of the U.S. Constitution. One of the requirements of fair apportionment is that the tax must be externally consistent. To be externally consistent, a tax must be structured so that the state has taxed only that portion of the interstate revenues from the interstate activity which reasonably reflects the in-state component of the activity being taxed. *Goldberg v. Sweet*, U.S. Sup. Ct. No. 87-826 (January 10, 1989). "That one state through which interstate commerce flows may not constitutionally tax such commerce does not mean that another state may make up for the gap, as it were, by taxing its share as well as the first state's share." *Id.* n. 3 (Stevens, J., concurring).

The MTC draft regulations throwout provisions cause a decrease in the multistate business' denominator thereby increasing the factor allowing the MTC state to increase the tax it can collect. In effect, the MTC state has taxed its share as well as a portion of the other state's share that cannot constitutionally tax the business. Thus, the throwout provisions in the draft regulations lack external consistency and are a violation of the Commerce Clause of the U.S. Constitution. The throwout provisions of the draft regulations should be removed so that a state can tax only its share of the interstate activity, regardless of other states' jurisdictional rights.

For further information regarding this memorandum, please contact John Kalligher, Assistant Tax Counsel, at (612) 667-8054.

EXHIBIT B: 17

Minutes of June 22, 1989 Meeting - Atlanta, GA

Multistate Tax Commission



MINUTES OF MEETING WITH REPRESENTATIVES OF FINANCIAL
INSTITUTIONS, ATLANTA, GEORGIA, MULTISTATE TAX COMMISSION

JUNE 22, 1989

The meeting was called to order by Alan Friedman, General Counsel of the Multistate Tax Commission, at 10:05 a.m. The following representatives of financial institutions, state revenue departments and the Multistate Tax Commission were in attendance:

Financial Institution Representatives:

Johnathan W. Allen	First Wachovia Corp. P.O. Box 3099 Winston-Salem, NC 27150
Joanne Ames	American Bankers Association 1120 Connecticut Avenue, N.W. Washington, D.C. 20036
Terry J. Baker	SunTrust Banks, Inc. P.O. Box 4418 Atlanta, GA 30302
Stephen Cameron	First Nat'l Bank of Louisville P.O. Box 36000 Louisville, KY 40233
John Coalson	Alston & Bird Attorneys at Law One Atlantic Center 1201 W. Peachtree Street Atlanta, GA 30309-3424
Lynda A. Kern	AmSouth Bancorp. P.O. Box 11007 Birmingham, AL 35288
David M. Schwartz	Crestar Bank 919 E. Main Street Richmond, VA
David Smith	Barnett Banks, Inc. P.O. Box 40789 Jacksonville, FL 32203-0789

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Multistate Tax Commission Representatives:

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Washington, D.C. 20001

Alan Friedman introduced the subject of the "proposed draft" of the Regulation for the Attribution of the Income of Financial Institutions by briefly outlining the history of the development of the regulation. Friedman noted that the development of new regulations in the financial institutions area is only a part of the Commission's efforts to deal with tax issues involving industries which were not the focus of UDITPA when it was first proposed. Financial institutions, for example, were specifically excluded from the basic three factor formula apportionment first developed in UDITPA. Changes in the nature of the American economy have also compelled the states to become sensitive to the need to change their methods of taxation to match current business conditions, including the significant movement toward a service, remote control and intangible property based economy.

Friedman noted that both the states of Minnesota and Indiana had recently amended their existing methods for taxing financial institutions. While both states have taken a market approach to taxing financial institutions, the approaches of the two states

are somewhat different. This emerging diversity therefore emphasizes the need for developing an acceptable, uniform recommendation for the other states to consider before the opportunity for uniformity in the state taxation of financial institutions is lost.

The Multistate Tax Commission believes taxation of financial institutions based upon principles evident in the current proposal are an inevitable evolution of today's and tomorrow's economic conditions. The product will be a better one, if the parties affected by these concerns cooperatively develop the applicable principles of law which will regulate the taxation of financial institutions. Friedman urged that the meeting be conducted in the spirit of these observations. Cooperation will avoid piecemeal, ad hoc legislation adopted by each state and will hopefully promote uniformity.

In addition, Friedman referenced the study on state taxation of financial institutions which the Advisory Commission on Intergovernmental Relations (ACIR) was in the process of preparing. This study concerns the Monitoring and Working Group on State Taxation and Regulation of Banks which is being sponsored by ACIR and which was scheduled to hold its first organizational meeting on July 7, 1989.

Friedman also described the MTC procedure established for the adoption of MTC regulations. The current intention of the MTC is to submit the "proposed draft" regulation, as it may be further revised, to a formal hearing authorized by the Executive Committee of the MTC in time for the regulation to be reported to the full Commission in July 1990. Upon receipt of this report, the full Commission can adopt the proposed regulation, as it may have been amended in the process. Adoption of a regulation or rule by the full commission is a recommendation to the member states that the rule be adopted by them in furtherance of the Commission's purpose to promote uniformity. Each state remains free to act in accordance with its own sovereign desires in possibly adopting the regulation once it has been approved by the full Commission.

Friedman also noted that the MTC necessarily acknowledges the existence of the nexus issue in the proposed regulations. Friedman contrasted the Pub. Law 86-272 threshold for the existence of nexus in the circumstance of state income taxation involving the sales of goods to the threshold which exist under the Due Process Clause of the U.S. Constitution for state income taxation in general. Neither side to the nexus issue was going to convince the other of the rightness of their position, so Friedman noted it would be best if each party in the context of these proceedings agreed to disagree and focused more on the actual mechanics of the proposal.

Friedman also invited comment on some of the basic concepts

present in the proposal and hoped that the discussion would permit the parties to gain an understanding, for example, as to why the proposal has adopted a throw-out approach rather than a throw-back approach. In addition, Friedman requested some comment on the possible application of water's edge principles to the proposal.

Having made these introductory comments, Friedman invited specific comments on the "proposed draft" regulation. A summary of the comments received is set forth below by category. These categories are not inviolate but serve as a useful reference to locating a specific comment some time after the fact. (Some comments may appear under more than one category when that comment is not easily categorized. Duplications are kept to a minimum, however.) The compiler of these minutes has inserted a few editorial observations when thought appropriate.

Additional Comments on Nexus Received:

One attendee reads the proposed regulation as requiring that a financial institution do something affirmative to develop a market in a state before nexus can develop. This observer questioned whether nexus should develop from out-of-state walk-ins coming into a bank situated on or near a state border.

Another representative noted that virtually all banks hold tax exempt securities which have been issued by political subdivisions which are representative of all the states. Holding these securities, without more, should not afford a basis for nexus.

The 3M hypothetical¹ continued to draw comments, including the

¹The 3M hypothetical situation is so labeled from a hypothetical circumstance described in a prior meeting with representatives of financial institutions. Representatives of the financial institutions used the assumed fact pattern to secure a better understanding as to how the proposed regulation was intended to operate. The hypothetical case assumed a hostile take-over attempt on 3M Corporation which is located in Minnesota, the first state to take a decidedly market approach to the apportionment taxation of the income of financial institutions. The assumption describes 3M Corporation as responding to the attempted take over by borrowing a sum of money in excess of the normal lending limits of the Minnesota banks to raise its defense fund. The hypothetical further assumes (and perhaps unrealistically) that 3M Corporation's use of the borrowed funds can be traced to a point out-of-state. The basic issue raised by this assumed hypothetical situation is the degree to which the money center bank submits itself to the taxing jurisdiction of Minnesota through its lending activities with 3M Corporation under various factual scenarios. The hypothetical has been utilized enough in discussions with representatives of financial institutions to have become known by

inquiry as to how a money center bank which has been called into to package a loan can show that it has not transacted business in, and thereby has not become subject to the taxing laws of, the borrower's state. One participant responded to this inquiry by noting that the direct solicitation presumption of ¶(A)(6) of the proposal is only a presumption which aids in determining whether direct soliciatation has in fact occurred. This participant believed that the money center bank had the ability to demonstrate under the MTC proposal that its in-state lending activities were not as a result of regular solicitation. Another participant countered this observation by arguing that the money center bank may already have sufficiently engaged itself in the taxing state to fall afoul of the nexus rules, because of the proposal's exceedingly low nexus threshold.

The proposal's low threshold will create continuous disputes over the presumption rules, because financial institutions will wish to demonstrate that they are not in fact regularly engaging in solicitation.

Does placement of a national advertisement create nexus in all the states?

The proposal's low nexus threshold of activity within a taxing state is unrealistic, because without more activity within the taxing state it is unlikely that the state has afforded any substantial benefit to the financial institution.

Financial institutions do not care about state taxes at their current levels; what concerns the banks is the cost of compliance.

Paragraph 6(b) of the proposal raises several problems: the activities should be regularly conducted before they give rise to nexus; if independent contractors are going to cause the existence of nexus, they should be independent contractors who are somehow tied into income producing activities--the hiring of outsider experts upon whom financial institutions are increasingly relying should not create nexus; the isolated presence of bank employees in a state not involving regular and systematic market development should not create nexus.

What is the rule on whether a financial institution with nexus once developed will always have nexus? Does a post loan move from a taxing state by a financial institution's borrower destroy nexus in the state from which he moves and create nexus in the state to which he moves?

Coordinate the first time establishment of nexus with a state's rules for making estimated tax payments. Banks should not be penalized for failure to have made estimated tax payments until

the shorthand name of the 3M hypothetical.

it is clear to the bank that nexus does in fact exist. The obligation to make estimated tax payments should depend on circumstances existing in the prior year.

Create an irrebutable presumption against the existence of nexus regardless of whatever threshold nexus standard is established for presuming nexus under ¶(A)(6)(c). Thus, if a financial institution does not meet the thresholds set forth in ¶(A)(6)(c), however they may be revised, it should be irrebutably presumed that no nexus in fact exists. An irrebutable presumption in favor of no nexus will afford the banks a safe harbor for avoiding the necessity of having to engage in sophisticated compliance analysis each year.

Make the presumption of ¶(A)(6)(c) conjunctive and not disjunctive, so that it would require both 100 or more bank customer relationships and \$5,000,000 in assets attributable to the taxing state.

Utilize a different level of nexus, depending upon the size of the bank. A lower threshold can be justified for a large bank.

Is the MTC proposal focusing its threshold on the level of in-state activity (which is relevant) or revenue potential (which is practical but not so relevant)--should these two standards be confused?

Complexity:

We do not think that the proposal will increase the overall tax bills of banks, but it will increase complexity and compliance costs. It would be better if representative revenues were used to apportion the income of banks, because complexity could thereby be reduced. Representative revenues would be revenues which are more easily traced but which are fairly representative of a financial institution's overall income. Also if true uniformity were achieved, there would be less objection to the proposal, because administrative costs would be reduced.

If you simplify the proposal by using representative revenues and by achieving uniformity, the low threshold would not be objectionable.

Simplify the receipts factor found in ¶(C)(2). Sourcing for the items found in ¶(C)(2)(a)-(f) should all be done on the basis of the borrower's residence. The items of income listed in ¶(C)(2)(h) which deals with services are relatively unimportant sources of bank revenues. Use the rule that these items are sourced where the services are performed.

We want more simplification--less precision.

Provide a cut off date (bright line) for determining addresses each tax year.

Current threshold rule would require significant work to determine if a bank is taxable any one year. Find a more easily administrable threshold, such as a threshold based in part on federal taxable income before state tax deductions, gross receipts, or even bank financial reporting income adjusted for major differences from taxable income--munies, large loan charge-offs.

We would have too many returns to file--35 affiliated entities doing business in 50 states creates 1750 returns.

Complexity necessarily affects the states also, because they have to audit. States have an equal interest in developing a simpler proposal.

If compliance is too costly, like what would result from the current proposal, we simply won't comply. We will take our chances.

We cannot do the required calculations, because we do not have the necessary data on system. One of the banks represented at the meeting by reputation has one of the most sophisticated information systems available. Yet this bank does not have its accrued taxable income calculated on a monthly basis state by state.

Ideally, the Multistate Tax Commission does not wish to force the banks to develop an entirely new information system in order to comply with the different state tax systems. The Multistate Tax Commission needs the help of the banks to devise a fair, common sense approach to measuring income where the banks must rely on existing, available data.

Avoid some of the complexity of the proposal by grandfathering earlier loans and making them exempt from the proposal. We cannot get the initial data for these earlier loans, because this data has been dumped.

Do not try to source trust and other miscellaneous fees. These items are too administratively difficult. As a general rule, fee income is too insignificant to be accounted for separately. Trust companies may be an exception to this observation.

If the MTC proposal occurs or something like it, I hope that I am out of the business of having to deal with bank taxes. I hate to think about being forced by circumstances to be even more noncompliant.

The GRS information data system is not that useful to extract data from the banks' typical loan systems.

Double Taxation:

We want standard sourcing; standard nexus. We do not want to be whipsawed by different state rules. We detect a definite movement away from allowing only the state of commercial domicile to tax financial institution income.

Even money center states are moving away from the commercial domicile concept. Witness New York's treatment of Loan Production Offices located in New York. [ed. note: New York's tax treatment of credit card receipts reflects the fact that as to credit cards, New York is apparently a market state.]

The MTC should study the extent to which states are currently taxing so-called out-of-state income of financial institutions through market state sourcing rules.

The Factors:

The proposal employs inconsistent definitions when you compare definitions used for the property factor with definitions used for the receipts factor.

The MTC should not feel compelled to use the same sourcing rules on the receipts side and the property side if both factors will include intangibles. The receipts factor measures the market state's contribution. [Ed. note: The logic of this comment presupposes that intangible assets, if included in the property factor, should reflect the assets of the financial institution which created the income, not the income itself, which is already sourced under the receipts factor. This suggests deposits, even though not a balance sheet asset, should be considered in the property factor.]

Using more than one factor (receipts) potentially creates more of an external consistency issue, because of the various methods states would adopt to source the specific items of the other factors.

There should be no difficulty in sourcing assets; the difficulty arises on the income side.

One way to simplify the reporting factors would be to use figures derived from the financial reporting balance sheet of financial institutions. This would avoid references to many off balance sheet items, such as letters of credit.

The receipts factor is in effect double weighted, because of the sourcing rules for intangibles included in the property factor.

Financial accounting standards require some fees generated on loan transactions to adjust interest. This observation suggests that financial accounting should be used to apportion income.

Would the banks look favorably upon including deposits, but not intangibles, in the property factor? [Ed. note: Although deposits are not an asset, they can be analogized to rental property which under traditional UDIPTA concepts is included in the property factor. There would be no need to capitalize the interest (analogous to rent) paid on deposits, because the actual value of the deposits can be determined in most cases as a sum certain.]

Are states constitutionally required to include intangibles in the property factor?

Throw out the property factor, because it is too complicated. Use two factors (receipts and payroll) or 1 factor (receipts).

Make taxpayer use of the property factor to apportion income optional with the taxpayer.

MTC's proposed sourcing rules for intangibles in the property factor are not consistent with established law which relies on commercial domicile or business situs to source intangibles. This divergence affords a basis for a legal challenge.

Possibly the property factor could be limited to tangible property but this factor itself would be proportionately adjusted to account for what percentage of the property is represented by intangibles which are being excluded. Thus, if only 10% of all property held by a taxpayer bank is tangible, the overall weight of a tangible property factor of 33-1/3% (as one of three equally weighted factors) would be reduced 90% and the weight of the two other factors would be proportionately increased equally.

The address presumption of ¶(A)(17) for determining residence is subject to manipulation, especially in large, sophisticated transactions.

Credit card fees should be easy to source; merchant discounts are much more difficult to source.

Policy Concerns:

The MTC proposal potentially undoes the banking tax policy of the Bank's commercial domicile. North Carolina for example has fostered the growth of its banks through the enlightened taxation of banks. By attributing income of a North Carolina bank on a market basis to another state, the other state is lessening the policies of North Carolina. This effect is especially disconcerting, because states which tax out of state banks have not completely opened up their markets to these out of state banks which they are taxing.

[Ed. note: A comment somewhat similar to the above was made in

the New York meeting in the context of Indiana's new bank tax: By taxing 100% of the income of its domiciliary banks (with a credit for other state taxes), Indiana would negate any tax holiday enjoyed in another state, because that means there will be no credit available to lower Indiana's tax burden. Indiana will have subverted the tax policy of the other state by requiring the domiciliary bank on its out of state income to pay the higher of Indiana's or the other state's tax.]

Is the proposal a water's edge or non-combination reporting rule? [Ed. note: Not necessarily; the proposed rule only deals with apportioning the tax base and does not directly deal with the identity of the filing entity.]

It would be preferable to impose an apportioned capital franchise tax rather than an income or franchise tax, which are simply too difficult to administer.

Cross state line banking relationships pose special problems. Consider a North Carolina bank which lends money to its Florida affiliate which in turn lends money to one of its retail customers. All the Florida activity is traceable to the North Carolina deposits. Does the MTC proposal ensure that North Carolina will get a full measure of income which the North Carolina deposits have generated?

Would a transaction tax be easier to apply?

Observations on the Nature of Banking Today:

Third parties are servicing mortgage loans and banks are less likely to do so today.

Specialized activities are being accomplished by specialized entities rather than within the banks' corporate shells themselves. A good example of this phenomenon is bank leasing which is typically conducted through a subsidiary.

The banking industry has a long tradition of limiting the offering of certain bank products to in-state (not to out-of-state) customers.

Technical Nits:

¶(C)(4)--insert the words "in the state" after the word "year" in the third line and delete the hyphen.

¶(C)(3)(b)--lease financing receivables have already been considered; this reference is unnecessary.

¶(C)(2)(b)--define "value" specifically so all states will have a consistent rule and will be more likely to reach a uniform

conclusion as to which state has the greatest property value.

¶(C)(2)(b)--UDITPA's normal definition of value, original cost, will not work here, because that information will not be known.

¶(C)(2)(g)--banks will not know how to source merchant discount income without the assistance of the merchant.

¶(A)(17)--banks will not be able to calculate the number of days its customers resided within a particular state; the presumption of the address will govern.

¶(A)(11) and (12)--The definitions ensure that bank affiliates will be considered financial institutions. Subsidiaries will also be treated as financial institutions under ¶(A)(11)(a), because they will be engaged in a business authorized by proper regulatory authorities.

Written Comments:

Attached to these minutes is a copy of a written comment submitted by Wachovia Bank & Trust Company, N.A. (per Johnathan W. Allen).

EXHIBIT B: 18

**Letter from Sheila J. Slaughter
(California League of Savings Institutions)
(July 11, 1989)**



**CALIFORNIA LEAGUE OF
SAVINGS INSTITUTIONS**

July 11, 1989

Mr. Alan Friedman
General Counsel
Multistate Tax Commission
386 University Avenue
Los Altos, California 94022

**Re: Proposed Regulations for the Attribution
of the Income of Financial Institutions**

Dear Mr. Friedman:

The California League of Savings Institutions (the "League") appreciates the opportunity to comment on the January 1989 draft of the MTC's Proposed Regulations for the Attribution of Income of Financial Institutions (hereinafter the "Regulations"). The League believes that the Regulations are an improvement over the July 1987 draft regulations, and is pleased to see that they address many of the issues raised in our letter of November 11, 1988. This comment is therefore directed at those residual problems in the Regulations which we feel still need to be addressed, and will generally not deal with issues covered by the League's prior letters.

1. Definition of "Business of a Financial Institution." Section (A) (11) of the Regulations contains a definition of what constitutes conducting the "business of a financial institution." Subsection (a) defines this phrase as including both the business that a regulated financial corporation is authorized to conduct under state or federal law or "the business that its subsidiary is authorized to do by the proper regulatory authorities." The League feels that it is inappropriate to automatically classify any permitted subsidiary activities as constituting the conduct of the business of a financial institution merely because the parent is a financial institution. In view of the fairly broad range of activities permitted for subsidiaries of regulated financial institutions, the League believes that the Regulations should include within the definition only the financial activities of such subsidiaries. One way of accomplishing this result would be to make such subsidiaries subject to the test of Subsection (11) (c), which could be done by replacing the above quoted language with the following:

"any business conducted by a subsidiary thereof meeting
the requirements of subsection (c) below."

2. Definition of "Loan Related Fees." While the League generally agrees with the allocation approach contained in Section (A)(18) of the Regulations for handling pooled loan fees, it believes that the ratio should be based upon the interest from loans on which loan fees are normally charged, rather than basing the ratio on all of the interest received by the taxpayer. Furthermore, the League believes that taxpayers should be permitted to allocate fees to different categories of loans if they maintain adequate records to support such an allocation.

9600 S. Sepulveda Boulevard
Suite 500
Los Angeles, CA 90045-0054
Telephone 213 670 6300

3. Definition of "Deposit Related Fees." For the reasons discussed in item 2 above, the League favors giving taxpayers the flexibility to use different categories of deposits as the basis for making the required allocation where adequate records are available to substantiate such allocations.

4. Definition of "Third Party Check Processing Fees." The League feels that the current definition of third party check processing fees set forth in Section (A)(20) needs to be revised to address a number of issues. As a preliminary matter, if this category is to include fees paid to third parties that have nothing to do with check processing, the League feels that the existing heading should be changed to "Third Party Fees" or a similarly generic heading. The League also favors adding a preamble to the text of the section that sets forth a generic description of the types of fees covered by the definition similar to that contained in the definitions of "Loan Related Fees" and "Deposit Related Fees" (e.g., "third party fees include all fees paid to third parties other than Loan Related Fees and Deposit Related Fees"), as well as language specifically including fees charged for ATM transactions. The League also believes that the definition should be expanded to cover fees charged to any third party, regardless of whether it is a financial institution, and that it should also cover loan servicing fees received by a financial institution that has purchased the related loan servicing rights but did not originate the underlying loans. It would also be helpful to make it clear that a party purchasing a pool of loans without the related servicing rights is to be treated as a "third party" with respect to the servicer for purposes of this definition.

5. Loan Guarantee Fees. As currently drafted, none of the three definitions relating to fees appear to cover loan guarantee fees, which presumably would result in such fees being sourced to the state where the services are performed under the rule set forth in Section (C)(2)(h)(vi). While we doubt that this type of fee is a material item to any of our members, as suggested in its letter of November 11, 1988, the League believes that it would be more consistent with the destination sourcing approach generally adopted by the Regulations to source these fees to the state of residence of the borrower whose note is being guaranteed, rather than to the state of residence of the guarantor.

6. Apportionment of Income From the Performance of Services.

(a) Brokerage Fees. Section (C)(2)(h)(iv) of the Regulations apportions brokerage fees to the state in which the brokerage account is "maintained", which term suggests the type of continuing relationship typically involved in the retail securities brokerage business. In many cases, however, brokerage fees are received in connection with one-time transactions (e.g., real estate transactions) in which no account is established or maintained by the customer. The League therefore feels that language in the Regulations should be broadened to more clearly address such situations, by replacing the language "and the brokerage account is maintained at . . ." with "paid in connection with transactions handled through . . ." an office of a financial institution located in the state. The League also believes it important to note that notwithstanding its clear preference for a rule that sources fee income to the state where the services are performed, we question the wisdom of allocating brokerage fees in this manner when the Regulations allocate other types of fee income using a destination sourcing approach.

(b) Fees for Estate and Trust Services. The League's primary concern with the approach taken in the Regulations for apportioning fees relating to estate or trust services relates to the allocation of fees when there are two or more executors or trustees. Our members have indicated that where there are multiple executors or trustees, they are rarely in a position of knowing which executor or trustee has "primary responsibility for administration." The League therefore favors a more mechanical approach, such as allocating such fees on a per capita basis among the executors or trustees, or allocating all of the fees to the first named party on the books and records of the financial institution.

7. Apportionment Of Income From Securities. As noted in its November 11, 1988 letter, the League remains opposed to resurrecting a deposits factor solely for the purpose of sourcing income from securities, and is disappointed that the Regulations have not abandoned this approach. Besides the additional administrative burdens created by use of a deposit factor, there is no sound policy justification for utilizing such approach to apportion the income of financial institutions in today's marketplace. While many of the League's smaller members still primarily rely upon deposits to fund their acquisition of assets, an increasingly large percentage of the debt reflected on our members' financial statements relates to non-deposit liabilities, such as Federal Home Loan Bank advances, unsecured debt obligations and secured financing, many of which involve securing the borrowing with the asset acquired with the borrowed funds. For this reason, there is frequently little relationship between an institution's level of deposits and the funding of any particular asset it acquires. The League also remains concerned that the California Franchise Tax Board will not abandon the commercial domicile rule for sourcing the income from securities, therefore, strongly urges the MTC to follow the widely accepted practice of allocating securities income to the taxpayer's commercial domicile.

On a related matter, in our letter of November 11, 1988, the League suggested that a distinction be made between public and private mortgage-backed securities, with the former being treated as securities and the latter as real estate loans. On further reflection, the League now feels that an easier and more appropriate way to classify mortgage-backed securities is to treat those in which the underlying loans were originated by the taxpayer as loans, and the balance as securities. With regard to the apportionment of income from securities issued by state and local governments, the League believes that the approach taken in the Regulations of sourcing such income to the state of the issuer is theoretically unjustifiable. Where a financial institution makes a real estate or consumer loan to a resident of a particular state, it engages in a business activity that is competitive with institutions in that state, receives income directly related to such activities, and often obtains the benefit of being able to enforce its contract in the courts of such state. The purchase of a municipal bond, on the other hand, can in no realistic sense be viewed as the conduct of business by the purchaser in the state of the issuer, and the purchaser receives no benefits from such state. The League therefore feels that state and local government securities should be treated in the same manner as securities, generally, and should either be apportioned to the taxpayer's commercial domicile or thrown out.

8. Prospective Application of Regulations. The League wishes to reiterate the comment contained in our letter of November 11, 1988, requesting that the Regulations, when adopted in final form, be made prospective.

Alan Friedman
July 11, 1989
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The foregoing comments were prepared by the members of the Tax Issues Committee of the League. If the League can be of any further assistance in connection with the development of the Regulations, please feel free to contact the undersigned or Michael J. Palko of Great Western Bank, (213/852-2349).

Very truly yours,



Sheila J. Slaughter
General Counsel and
Senior Vice President

SJS:jer

EXHIBIT B: 19

**Letter from Jonathan W. Allen
(Wachovia Bank & Trust Company)
(July 11, 1989)**

Wachovia

Wachovia Bank & Trust Company, N.A.
P.O. Box 3099
Winston-Salem, NC 27150-3099

July 11, 1989

Mr. Alan H. Friedman
386 University Avenue
Los Altos, California 94022

Dear Mr. Friedman:

Re: MTC Proposed Regulation for the Attribution of the
Income of Financial Institutions

I enjoyed the opportunity to participate in the June 22 meeting in Atlanta on the above proposed regulation. It is my personal view that it is better to participate constructively in the shaping of these regulations as they seek to balance taxpayer burdens with the need for state revenues.

It is my perception of the meeting that the primary areas of concern were the untested low nexus threshold in Section (A) (6) of the proposal and the concerns of taxpayer administrative burden arising from apportionment complexity. The complexity issue concern is the receipts tracing of all income and use of intangibles in the property factor. There were numerous other smaller concerns such as whether independent contractors should be defined, however all points seemed to revert back to the basic nexus and complexity issues. This letter will attempt to expand on the major concerns raised at the June 22 meeting and offer comments to alleviate areas of concern.

Nexus

The greatest nexus issue is having nexus without the presence of traditional nexus features (tangible property located within a state and employees residing in a state). Section (A) (6) (c) basically would establish nexus (under a rebuttable presumption) that any financial institution would have nexus if it had a loan or deposit relationship with 100 or more residents of a state during any tax period or five million dollars of tangible or intangible assets attributable to sources within the state. While this regulation obviously has yet to be tested it appears to be an unreasonably low threshold even in the event it was upheld by judicial review. An asset or number of customers threshold "during any tax period" presents problems in monitoring.

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July 11, 1989

If the 100 customer base threshold was crossed solely from having 100 credit cards issued to residents of a state, there appears little justification for having this situation trigger taxability even if the rebuttable presumption provision would negate taxation in that situation. Therefore, to base nexus solely on a specified number of customers would not seem to serve the best interests of a state or a financial institution when viewed with the attendant administrative monitoring burdens.

The alternative test for assumed nexus is a five million dollars of assets at any time during the tax period. Due to the ebb and flow of business relationships, it appears unreasonable to request a financial institution to monitor this five million dollar threshold at all times during a tax year even with the rebuttable presumption. Additionally, a five million dollar loan portfolio to customers in a particular state is not likely to generate that much revenue under apportionment given the narrow interest rate spread between a financial institution's interest bearing assets and interest bearing liabilities.

Assume five million dollars of assets are in a state during the entire taxable year and the financial institution has a 4% spread on the loans of five million dollars. If administrative costs of managing the five million dollars of loans is ignored, the state would reap \$1,000 or less of tax revenue if that state's base was \$200,000 with an apportionment factor of 7% and a state tax rate of 7%.

One should also visualize the situation where a financial institution had loans of five million dollars to residents of the state for 30 days or less during a tax period. Again, the rebuttable presumption would seem to probably deny nexus, however financial institutions need a more clear and definitive rule that will not require constant arguments to be advanced to support the rebuttable presumption or complex systems to monitor crossing the asset or number of customers tests during a tax period. In order to accomplish this, the threshold should be increased to a higher level and targeted more at cumulative gross income rather than the number of customers or assets. I would suggest something in the range of \$750,000 to one million dollars of the receipts used for the receipts factor. A threshold for nexus at this level still might not generate any sizable state tax revenue, however, this higher amount would give stronger support to a state's position that the state is rendering or providing valuable services to the out-of-state financial institution and therefore has jurisdiction to tax.

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This higher threshold would also remove many of the smaller depository financial institutions from the burdensome requirements to file numerous state income tax returns where their business volume in a particular state is relatively low. Even where this threshold was crossed for establishing nexus there still may be little tax revenue due to either the size of the tax base or a very low apportionment percentage. Thus a de minimis rule is also needed for those instances where a financial institution has a nominal base under a particular state's rules and/or has an exceedingly small apportionment percentage. During our meeting in Atlanta, Ben Miller expressed \$1,000 as a de minimis tax liability. It seems reasonable that a financial institution crossing the nexus threshold of receipts discussed above would then have to take the additional steps to determine tax base, the apportionment percentage and the resultant tax in order to test whether the de minimis rule applied. Since any de minimis rule should override nexus rules, it might be better to place any de minimis rule somewhere other than in the nexus section of the regulation.

There was also concern on whether the traditional nexus test of property or employees residing in a state would override any presumption of nexus based on business volume. For example, should a financial institution be required to file a return showing nominal tax because they had a storefront in a state but had minimal business volume from that storefront or other activities? If a de minimis rule based on actual tax liability is adopted, then a financial institution having nexus under the traditional test would still not be required to file a return even though nexus had clearly been established if the tax was less than the amount established by a de minimis test.

An alternative would be to have nexus based solely on business volume. A business volume nexus test standing alone, would have short comings in situations where there was a substantial processing location in a particular state but no receipts of any material amount from that particular state.

Because of this, I believe the traditional nexus tests are needed and if the traditional nexus tests are not met, one then looks to the business volume test to establish nexus. If either the traditional nexus tests or the business volume test are met, then a financial institution still may not be required to file a return provided there was a de minimis tax test. This would allow a financial institution to quickly determine whether or not any of the traditional nexus tests or the business volume test had been met. For any state in which the financial institution met any of the nexus thresholds it would have to go further in its calculations to determine whether it met any de minimis tax liability test.

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Tax Administration

Another concern expressed at the Atlanta meeting was the difficulty for a financial institution to know during the taxable year when it might be required to file estimate tax payments obtain return filing extensions or perform other interim tax administrative acts. In view of this concern, it appears appropriate to establish rules to prohibit any type of penalty for failure to perform administrative acts prior to filing a tax return but only for the initial year a company is taxable under the nexus rules and the de minimis tests recommended above. It may also be desirable to have the penalty exemption repeat itself if a financial institution previously taxable in a particular state is not required to file a return for three consecutive tax periods.

Receipts Factor and Sourcing

Another major concern expressed at the Atlanta meeting was the complexity of the receipt sourcing rules and having to identify a source for each and every type of receipt. The banks concerns stem mostly from the administrative burden. For example, Arla Taylor of C&S Bank mentioned that they have approximately eight loan application systems that would require extensive programming under the proposal and operational overhead. Many bank application systems are monthly systems rather than annual systems. Our institution has over 200 categories of interest income and 400 categories of non-interest income on its General Ledger. These numerous categories of interest and non-interest income are necessary for various regulatory, shareholder and management reporting analysis but are not geared to a state sourcing concept. The numerous application systems coupled with the huge volume of categories of book income and monthly cycles of application systems create extreme high burdens of compliance if each transaction in these numerous accounts must be identified and accumulated by state under whatever rules are applicable with the attendant programming costs for each system and new systems to assimilate and aggregate the tax data for all the accounts.

Interest income and gains or losses on taxable investment portfolio securities do not in any way relate to standards of nexus and should not be included in the receipts factor. The banks opposition to including any income or gains on securities in the receipts factor based on the state issuing the securities was due to the fact that these securities are often acquired in

Allen to Friedman
Page Five
July 11, 1989

Receipts Factor and Sourcing (Continued)

the open market rather than directly from an issuing state. There connection to activities in a state seems remote. It might appear reasonable to include those securities acquired directly from an issuing state or if the financial institution is the first holder, however, this presents unreasonable complexities from a record keeping base. One should also keep in mind that whether non-taxable receipts from federal or municipal securities should be included in the receipts factor as a number of states do not tax either their own obligations or federal obligations where the tax is an income tax.

The problem of having to trace all items of income can be substantially reduced by limiting the receipts factor for a depository to the major items of interest income. Under this suggestion, non-interest income would be totally excluded from both the numerator and the denominator of the receipts factor of a depository. Attached to this letter is a summary of the consolidated income of seven bank holding companies which show that the interest on loans, interest bearing bank balances, fed funds sold and securities sold under resale agreements constitute 68-75% of all gross income of the seven financial institutions. The financial institutions represented on the attachment consist of a money center bank, several super regionals and other regionals and range in asset size from 3 billion to 75 billion. It should be noted that credit card income usually represents 2% or less of all income of a bank. Trust fees represent 5% or less and all other operating income represents 7% or less of the total income. Given that the primary source of income is from interest on loans, interest bearing bank balances, fed funds sold, and securities sold under resale agreements, it seems reasonable to use only these items for determining the receipts factor (and for the receipts nexus test discussed above) as the effect of all the other items would be expected to be nominal. These items would still cause considerable administrative burden, however that burden would be substantially less than under the current MTC proposal which requires sourcing all non-interest income as well as some other small items of interest.

Therefore, I would propose the receipts factor and any receipts nexus test for a depository be limited to interest on loans, interest bearing bank balances, fed funds sold and securities sold under resale agreements. Interest on investment securities would be excluded from both the numerator and denominator of the receipts factor. The calculation would be to first take the total book income of these items of interest income as the receipts denominator. The numerator would consist of each state's portion of these items based on the destination or mailing address used for billing or state of payment source in the event payments are made automatically. The depository's

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Receipts Factor and Sourcing (Continued)

receipts factor numerators would contain the interest income from tax exempt loans (but not investment securities) which may be exempt from state taxation depending upon the scheme of taxation utilized by a state. This proposal would not remove any such exempt loan interest from the receipts factor, however, any exempt income would be removed from the state defined base if the state provided an exemption. Using book income for the receipts factor facilitates reconciling the denominator and numerators used for apportionment.

Property Factor

The MTC proposal for the property factor would include intangibles. Use of intangibles in a property factor has somewhat the same administrative burdens as attempting to source all receipts. Most multi-state taxpayers are familiar with the rules and sourcing for tangible property. Intangible sourcing would produce factors somewhat similar to a receipts factor under the MTC proposal. The MTC proposed rule appears inconsistent with existing statutory and judicial interpretations of situs for intangibles and could be in conflict with existing state laws for taxation of intangibles.

I would therefore propose that no intangibles be used in the property factor and that the property factor be determined solely from tangible real and personal property.

Summary

In summary, only a dollar receipts volume test should be added to the traditional nexus standard and that dollar volume should be sufficiently high enough to prevent the filing of de minimis returns. Second, a de minimis tax liability test of \$1,000 is needed in the event the minimal gross receipts threshold for nexus has been reached or nexus has been established through other traditional means. Third, the receipts factor for a depository should be based solely on major selected items of interest income as it is believed they would fairly represent the volume of business done for the balance of gross income. Fourth, the property factor should be based solely on tangible real and personal property. Fifth, the receipts factor denominator should be book income of selected items before any adjustment for income that may not be taxed by a particular state.

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July 11, 1989

I look forward to working with you on regulations that will result in fair and equitable apportionment when viewed both by state and corporate tax administrators. Please let me know if you would like further elaboration on any of the suggestions contained in this letter or I may be of any assistance to you and MTC.

Sincerely,



Jonathan W. Allen
Senior Vice President

JH/JWA

Attachement

CC: Ms. Joanne Ames
American Bankers Association

PER 1988 ANNUAL REPORTS

	BANK A		BANK B		BANK C		BANK D		BANK E		BANK F		BANK G	
	ITEM	CUMULATIVE												
INTEREST INCOME														
INTEREST ON LOANS (1)	60.53%	60.59%	66.99%	66.99%	70.77%	70.77%	70.77%	70.77%	61.82%	61.82%	74.56%	74.56%	66.15%	66.15%
INTEREST BEARING BANK BALANCES	4.17%	64.76%	1.09%	68.09%	2.87%	73.64%	7.50%	73.64%	11.98%	73.80%	0.77%	75.33%	2.53%	68.68%
FED FUNDS SOLD AND SECURITIES														
SOLD UNDER REVERSE AGREEMENTS	5.27%	70.03%	0.15%	68.24%	0.48%	74.12%	2.25%	68.59%	0.12%	73.92%	0.00%	75.33%	1.54%	70.22%
INVESTMENT PORTFOLIO (2)	9.62%	79.65%	15.56%	83.80%	13.27%	87.38%	13.43%	81.52%	14.23%	88.14%	10.44%	85.76%	13.80%	84.02%
ALL OTHER INTEREST	1.72%	81.37%	0.24%	84.04%	0.04%	87.42%	0.13%	81.65%	0.00%	88.14%	0.78%	86.53%	1.05%	85.06%
NON-INTEREST INCOME														
CREDIT CARD INCOME	9.74%	91.10%	1.63%	85.67%	1.35%	88.77%	5.75%	87.42%	1.44%	89.58%	2.17%	88.77%	1.97%	87.54%
SERVICE CHARGES ON DEPOSITS														
TRUST FEES	2.39%	93.50%	2.58%	93.23%	3.29%	95.40%	4.77%	97.70%	3.74%	96.97%	3.74%	95.56%	3.61%	95.65%
ALL OTHER OPERATING INCOME	6.14%	99.63%	6.54%	99.77%	4.55%	99.94%	2.31%	100.01%	3.23%	100.19%	4.63%	100.19%	4.12%	99.77%
SECURITY GAINS (LOSSES)	0.37%	100.00%	0.23%	100.00%	0.06%	100.00%	-0.01%	100.00%	-0.19%	100.00%	-0.19%	100.00%	0.23%	100.00%
GROSS INCOME	100.00%	100.00%	100.00%	100.00%	100.00%	100.50%	100.00%	100.00%	100.00%	100.00%	100.00%	100.50%	100.00%	100.00%

(1) LOAN INTEREST SHOULD INCLUDE "TAX-FREE" GAINS AND INDUSTRIAL REVENUE BONDS

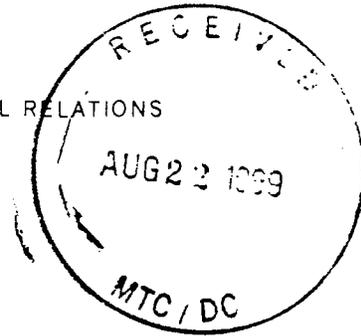
(2) INVESTMENT PORTFOLIO INTEREST USUALLY IS FROM FEDERAL, STATE AND MUNICIPAL OBLIGATIONS

EXHIBIT B: 20

**Letter from Luc Noiset (ACIR)
(August 19, 1989)**



ADVISORY
COMMISSION ON INTERGOVERNMENTAL RELATIONS
WASHINGTON DC 20575



Mr. Dan Bucks
MTC
Suite 409
Hall of the States
444 N. Capitol St.
Washington, D.C. 20001

August 19, 1989

Dear Dan:

I am sending you a short note explaining a revelation of mine about the "dual approach" to taxing multistate banks, which is discussed in Sandy McCray's bank tax paper. I hope that it clarifies a number of issues. If you get a chance I would welcome hearing what you think about it.

Thanks,

A handwritten signature in cursive script that reads "Luc Noiset".

Luc Noiset

The Dual Approach is Formulary Apportionment with a Throw-back Provision

Pure source-based taxation with formulary apportionment is used by nearly all States to tax general business multistate corporations. A State uses an apportionment formula to determine the fraction of a corporation's income to attribute to itself. The typical formula is a weighted average of three terms (1) the corporation's in-state property divided by its total property (2) its in-state payroll divided by its total payroll (3) its in-state receipts divided by total receipts. The state chooses whatever weights it sees fit and defines in-state property, in-state payroll and in-state receipts according to situs rules, which it also chooses. Because each state chooses its own situs rules and weights, there are a wide variety of apportionment formulas in use.

Critics claim that this nonuniformity imposes an unnecessary compliance burden on business and a high administrative burden on some states. In addition, nonuniformity may lead to tax avoidance behavior on the part of the business taxpayer. Assume, for example, that one State places a disproportionate weight on property and payroll in its apportionment formula, while another state disproportionately weights receipts. A business could minimize paying state taxes if the bulk of its sales are made in the former state and it locates all its property and employees in the latter state. Moreover, the result is economically inefficient since the firm's production and distribution decisions are tax

rather than market determined.

It is claimed that, because of the highly mobile nature of bank assets, tax avoidance and distortionary decision-making would be even more likely to occur in the banking industry if formulary apportionment were used to tax bank income. The dual approach has been suggested as an alternative to formulary apportionment for the taxation of bank income. Under the dual approach a state levies its tax on the entire net income of its domestic banks, and allows those banks a credit for taxes paid to other states. The amount of the credit is limited to the amount that would have been paid under the home state's tax. The state uses an apportionment formula to define the fraction of the income of an out-of-state bank that is earned within its borders.

The dual approach has been recommended on grounds that it will help bring more uniformity to the system. It is argued that all states will have an incentive to use similar (market-state) apportionment formulas and situs rules because apportionment formulas will be applied only to the income of out-of-state banks. Such formulas and rules would, typically, heavily weight the receipts factor, and define the location of loan receipts as in the State where the property securing the loan is located or where the borrower resides. If a more uniform system could be achieved under the dual approach, then the compliance and administrative burdens of State taxes would be reduced, and economically inefficient tax avoidance behavior would diminish.

We show below, however, that the dual approach will not bring

about a more uniform system, and, consequently, will not ease administrative and compliance costs, nor will it eliminate distortionary behavior. If States are allowed to freely choose their situs rules and formulas, then the dual approach is identical to formulary apportionment with an appropriately defined "throw-back" provision. Such a system ensures that no income will escape taxation (the minimum tax bill of a bank under such a system will equal what its tax bill would be if all of its income was earned in its home state), but it will not affect a States choice of apportionment formula. If, on the other hand, particular situs rules and formula weights are dictated to the States for the apportionment of out-of-state income, then this is equivalent to requiring States to use a uniform set of rules and weights for the apportionment of all income. Thus, apportionment formulas under the dual approach will remain as different as they are under pure formulary apportionment. Uniformity can only be achieved by a compact among States, or in the unlikely event of a federal mandate.

All this can be made clear with some very simple algebra. Assume there are three States, each with one home bank doing business in all three States. We need only focus on State one, recognizing that States two and three will behave similarly. Under formulary apportionment with a throw-back provision, State one applies its formula to define the in-state income of each bank. Then levies its tax, t_1 , on that income. In addition, the throw-back provision says that bank one, the home bank, must also pay the

difference between the tax it would have paid on its out-of-state income (defined by State one), if that income had been earned in-state, and its actual tax bill on that income, if the difference is positive. The throw-back amount, P, can be written as,

$$(1) \quad P = t_1(I_{12}^1 + I_{13}^1) - t_2I_{12}^2 - t_3I_{13}^3 \quad (\text{if positive})$$
$$P = 0 \quad (\text{otherwise})$$

Where t_i is State i 's tax rate and I_{ij}^k is the income of bank i generated in State j according to State k 's situs rules.

The tax revenue that State one collects from bank i , R_i , is,

$$(2) \quad R_1 = t_1I_{11}^1 + P$$

$$(3) \quad R_2 = t_1I_{21}^1$$

$$(4) \quad R_3 = t_1I_{31}^1$$

There are two things to recognize here. First, the apportionment formula chosen by State one will presumably be, from State one's perspective, the optimal formula for achieving whatever goals it may have. This formula may be quite different for each State. For example, for money-center States with large home banks, a formula that heavily weights property and payroll will tend to generate the most revenue from those banks. If receipts are weighted at all, they will be defined with a money-center-state bias (e.g. located in the State where the bank initiating the loan is located). This may not maximize the revenue from the out-of-state banks, but it will maximize total revenue.

In market-states, on the other hand, home banks tend to be

small community banks that do little or no out-of-state business. In addition, large out-of-state banks may be generating business there through the mail or through electronic banking machines. These States will maximize their tax revenues by heavily weighting the receipts factor, and using market-state situs rules to define the location of receipts. Thus, a variety of formulas and situs rules is likely under this approach. Each state will choose the formula and rules which best fits its needs.

The second thing to recognize is that equations (2)-(4) exactly describe the dual approach. To see this more directly, substitute equation (1) into equation (2) to get,

$$(5) \quad R_1 = t_1 I_T - t_2 I_{12}^2 - t_3 I_{13}^3 \quad (\text{when } P > 0)$$

$$R_1 = t_1 I_{11}^1 \quad (\text{when } P = 0)$$

Where I_T is total income of bank one, $I_T = I_{11} + I_{12} + I_{13}$.

This is the exact definition of the revenue collected from bank one under the dual approach, and equations (3) and (4) exactly define the revenue collected from banks two and three respectively. Therefore, the apportionment formula that was optimal under formulary apportionment with a throw-back will continue to be optimal under the dual approach. If the apportionment formulas chosen by States differ under formulary apportionment with a throw-back, they will differ under the dual approach.

The argument that all States will always want to use market-state formulas and situs rules under the dual approach is clearly wrong. If a State uses such a system, it will be as if it is

apportioning its home-banks' incomes (as well as out-of-state banks' incomes) according to market-state rules under formulary apportionment with a throw-back. If this is not the optimal formula and set of rules for the State, it will not use them under formulary apportionment with a throw-back or under the dual approach. Each State will continue to use whatever specific formula and set of situs rules that it deems optimal, and the problems associated with nonuniformity will continue.

Therefore, since they are equivalent, it matters little whether we use the name "dual approach" or "formulary apportionment with a throw-back." The throw-back provision explicit in the latter name is implicit in the former. This provision ensures that no income can escape taxation. A bank's minimum tax bill will equal what it would pay if all its income was apportioned to its home state, but its bill could easily exceed this amount.

Uniformity, can only be imposed on the system by federal statute dictating the apportionment formula and situs rules that all States must use, or by voluntary agreement among the States. In such a scenario the only difference between the States would be in their tax rates. The amounts of a particular bank's income apportioned to each State would sum to one hundred percent of the bank's total income. Thus, one hundred percent of the bank's income would be taxed, albeit at different rates.

A high-tax State could still increase its collections from its home banks by requiring them to pay the difference between their tax bill on out-of-state income and the amount that they

would have paid on that income if it had been generated in-state. But if a high-tax state did this it could become a less desirable place for a bank to locate its home base. The bank's total tax bill would be as if it had earned all its income in the high-tax state. It could carry out the same level of business in every State and lower its tax bill, by locating its home base in a low-tax State.

Finally, if uniformity is imposed on the system by, say, federal statute, there are likely to be some winners and some losers among the States. For example, if the federal government dictates that all States must use an apportionment formula that heavily weights receipts, and dictates situs rules that define receipts with a market-state bias (eg. located in the State of the borrower), then money-center states will experience a sudden reduction of their tax base. In such a scenario, money-center states might be expected to increase their tax rates in order to maintain revenues.

Luc Noiset
ACIR
Washington, DC 20575
8/18/89

EXHIBIT B: 21

**Memorandum from Alan H. Friedman and Paul Mines (MTC)
(September 11, 1989)**

TO: MEMBERS OF THE UNIFORMITY COMMITTEE

FROM: ALAN H. FRIEDMAN, GENERAL COUNSEL
PAULL MINES, COUNSEL

SUBJECT: STATUS PAPER ON MTC REGULATION GOVERNING INCOME
APPORTIONMENT FOR FINANCIAL INSTITUTIONS

DATE: SEPTEMBER 11, 1989

The following memorandum outlines the major issues and industry comments to be considered by the Committee at its September 27th meeting in Rapid City, SD. On December 13, 1989 a public conference on the issues of state taxation and regulation of banking will be held in Washington, DC. The conference will be co-sponsored by the Advisory Commission on Intergovernmental Relations, the National Conference of State Legislatures, the National Center for Policy Alternatives and the MTC. It would be most helpful for the Committee to now grapple with the issues raised below and provide MTC staff with as clear guidance as possible so that the Committee's direction can be best represented.

This memorandum begins with a general discussion of where the MTC is currently in the development of its regulation and asks the Committee to focus on the question of when and under what circumstances should the MTC bring the matter to the public hearing stage. We describe the recent enactment of the Indiana financial institutions tax which presents a market approach that substantially differs from the approach under the MTC's current proposals. Additionally, we have listed preliminarily the perceived advantages and disadvantages of the approach taken in the MTC's drafts (formula apportionment) and the approach taken by the state of Indiana (dual-residence and source based--approach). Finally, you will find a catalog listing of the several major issues for your consideration regarding the current MTC financial institution regulation proposals.

For the convenience of your reference, we have attached (as Exhibit A) a copy of the two MTC proposals--Sandy McCray's original draft of July 1987 and the mark-up of that draft proposed by Phil Plant of the Bank of America. We have also appended (as Exhibit B) to this paper a copy of Indiana's new tax statute which governs the taxation of financial institutions.

I.

SHOULD THE COMMITTEE A RECOMMENDED APPROACH TO
THE TAXATION OF FINANCIAL INSTITUTIONS IN THE FACE OF CERTAIN
PHILOSOPHICAL ISSUES THAT REQUIRE DECISION?

This question is most important because the financial institution regulation project is approaching its cross roads. Significant unfinished work remains, yet there are unresolved issues inherent in the proposal which make the desirability of currently completing the project over the short term an appropriate subject for inquiry. At the same time we are all aware that pressure is mounting in certain states to effect a reform of the method of taxation of financial institutions. Three states have recently overhauled their system of financial institutions taxation (IN, MN, NY). Other states have reform under active consideration (AZ, MA). The opportunity to maximize the development of uniform solutions to state taxation in this area may well be lost without the active leadership of the Commission.

What follows under this Section I. is a general discussion of four basic issues which are inherent in the proposal and which directly impact the ability of the MTC to complete the financial institutions regulation at this point in time. These issues are also dove-tailed into several subsidiary issues that will be addressed in Sections IV. and V.

A. **NEXUS** (the economic presence issue): The market state orientation of any proposal likely to be recommended by the MTC inherently raises the issue as to whether the jurisdictional concept of "economic presence" will survive a court challenge. The yet to be determined validity of the market nexus rule necessarily would place states adopting an MTC recommended regulation at some risk. The risk arises because the adopting state will be apportioning income both in and out of the taxing state, but the state is only likely to face a court challenge to the extent the rules apportion income in. Thus, if the apportionment in of income is successfully challenged, a state will have given up potential revenues through the apportionment out of income

which will not necessarily be replaced. Any MTC recommendation in this area therefore must contain a direct warning of the risks inherent in adoption. The Committee may wish to consider whether it is realistic to be recommending state adoption of a market apportionment method prior to the nexus standard having been finally judicially approved. It will take several years before the results of any ultimate judicial test are in.

1. Step-by-Step Approach. If these concerns are valid, it is appropriate to inquire whether there are any suitable compromises which could enable development of innovative methods of state taxation of financial institutions without unreasonably jeopardizing state revenues. The ideal compromise would allow taxpayers the opportunity to challenge the economic presence, nexus standard without unreasonably jeopardizing state revenues. One compromise approach to consider would be for MTC to recommend that the financial institutions regulation be adopted in phases. For example, the regulation might first apply market apportionment principles to a limited, but discrete, area of business of financial institutions, such as lease financing, credit cards, real estate mortgages, commercial loans, or some other activity which can be reasonably isolated.

Unfortunately, a review of the Alabama credit card case reflects that the decision therein may well depend upon a construction of state law that is unrelated to the nexus issues involved. Limiting adoption of market nexus principles to less than all of the financial institutions industry would permit the theory of the nexus rule to be challenged without risking substantial state revenues if the entire financial industry were placed under the regulation at the inception.

2. Concurrent Tax Schemes Approach. Another approach might be to employ a concurrent tax system for financial institutions until the validity of the nexus rule was established. This approach might maintain preexisting taxes in force, or alternatively adopt a back-up tax based upon traditional taxing principles, such as a franchise tax based on capital. These additional taxes would provide that anyone paying taxes based upon the unchallenged

nexus principle would be entitled to a full (or partial) credit against the liability of the other tax, so long as the nexus principle was not held invalid.

3. Statutory Condition Approach. A third approach might be to secure a statutory agreement as a condition to allowing the apportionment out of income under the market nexus rule. The statutory agreement could require any taxpayer apportioning out income under the market nexus rule to agree, as a condition of such apportionment, that such income would be nevertheless subject to tax if apportioning in were subsequently held invalid and refunds were made.

There may well better compromises which occur to you than what is suggested above to accomplish the same objective--that is, establishing a framework which will permit the states to continue new development of tax systems appropriate to modern economic conditions (in this case financial institutions) without placing state revenues unduly at risk. Indeed, it should be noted that the U.S. Supreme court decision in McKesson and ATA may well afford some relief from these concerns, if the Court should grant discretion to the states to make or deny refunds of taxes paid which are subsequently determined to be unconstitutional.

B. **ADMINISTRABILITY:** A market oriented, apportioned income tax is a significant departure from what limited state income taxation financial institutions have had to face. Given the little exposure which banks have had to state income taxation in general, banks will not be particularly enthusiastic about any proposal which seeks to establish a sophisticated method of state income taxation. Indeed, industry reaction to the MTC proposal suggests that banks do not have developed data processing systems which would be useful to the banks to comply with sophisticated apportionment rules of a state income tax system.

In addition to this industry inertia to state taxation, financial institutions have been under immense pressure to adapt to the rapidly changing economy. Changes in methods of state taxation in this kind of environment are probably

viewed as another threat to survival of the financial institutions which are subject to the tax.

These observations suggest that one way to sell a sophisticated system of state apportioned income taxation is to simplify the immediate administrative burden of compliance. Should the MTC proposal therefore be more sensitive to establishing rules which are something the banks and other financials can handle without having to gear up a major, expensive effort? As one commentator of the MTC proposal suggested, the banks want less precision and more practicality.

Several compromises to creating a less burdensome tax in administration suggest themselves:

1. Should the MTC proposal attempt to source every dime of receipts? The MTC proposal might better permit reporting taxpayers on an elective¹ basis to source their income on the basis of sampling profiles (either as to time periods, types of income or both) in lieu of tracking each independent source of income for the entire tax year.
2. Could the MTC proposal apply the apportionment rules prospectively—that is, allow taxpayers to elect to apportion their income based solely upon the application of the sourcing rules to new transactions which occur after the effective date of the regulation? Such an election would allow banks to develop the data needed to comply with the apportionment rules of the MTC proposal as each new transactions was

¹This section of the narrative suggests possible solutions to making the proposed MTC regulation less complex. These possible provisions are phrased in terms of an election, because they could be subject to possible legal attack unless the taxpayer voluntarily decides that he/she desires to be bound by the rule elected. Hopefully, any elections permitted will be attractive enough that few taxpayers will not avail themselves of the simplification afforded by the election. The elections may accomplish therefore what otherwise might not be obtainable if the MTC proposed regulation were to mandate taxpayer compliance with the subject matter of the elections on a non-voluntary basis.

concluded.

3. Should the MTC proposal do more to promote uniformity, because the banks are not prepared to comply with all of the differing tax laws of the states in which they will have nexus unDer market oriented rules? The proposal could set forth more uniform definitions and rules and leave less to the possible local interpretation. A single reporting form and a one stop filing system should also be considered.

C. **DOUBLE/OVERLAPPING TAXATION**: Financial institutions, like most multi-jurisdictional businesses, are concerned over being whipsawed by the states. Financial institutions resist having to be taxed under market rules in many of the states and then being subjected to a tax under domicile rules in the few remaining money center states. Is it realistic for the MTC to be proposing a model regulation where the dichotomy between the market states and the money center states has not been better resolved? Is this circumstance really any different from what was faced with regard to heavy industry when the MTC was first implemented or does the concentration of money in California, New York and perhaps one or two other states makes this problem more difficult?

Should the MTC investigate methods for ameliorating the effects of double/overlapping taxation before pushing its proposal forward? This investigation may be no more than educating the money center states that the globalization of the world's financial markets has in effect made the entire country a market for financial institutions as opposed to a domicile for financial institutions. New York recognizes the validity in certain contests of a market rule approach, i.e., income derived from credit card business. California, with the participation of Pacific Rim money in its markets may well benefit from the development of market oriented rules of apportionment in the financial industry.

D. **SECONDARY LOAN MARKET AND SECURITIZATION**: Any market state approach to the income taxation of financial institutions based

upon formulary apportionment raises the inherent question of how to tax loans which are properly attributable to a taxing state, but which are resold sometime after they have been funded. Such resales can occur through various investment mediums ranging from the sale of direct participation interests to the sale of interests in a trust which holds a diversified loan portfolio.

The major issue faced by a market state imposing a formulary apportioned income tax is whether continued taxation of the loan obligations after they have been sold will discourage the extension of credit in the taxing state. The argument against continued taxation of loan obligations which have been sold into the secondary market is that there will be no one to purchase the obligations if to do so will result in the purchaser becoming subject to taxation in the state in which the loan was originated.

The solution to the secondary loan market issue thus far has been to exempt most of such loans from taxation entirely. The solution of affording an exemption does not seem entirely appropriate for a number of reasons. In the first place, such loans are still properly attributable to the originating state. Such state is after all the one which is most likely to be affording the creditor the advantages of a civilized society, including a system for filing security interests and for effecting collections of defaulted amounts. Secondly, significant lending is occurring through this mechanism. Mortgage loans, auto loans, credit card receivables, major loan syndications, among others, are now significantly packaged for resale into secondary markets. Thirdly, the centralization and globalization of the financial markets makes this trend more likely to occur in the future. Indeed, it would seem preferable that the states solve the issue of how to deal with the issue of the secondary loan market now before such markets become dominated by foreign financial institutions whose taxation by the states might well raise an additional level of concern. Finally, the secondary loan market issue must be resolved, if for no other reason than to avoid the manipulation potential which would exist for large, sophisticated transactions under the exemptions which have been adopted to deal with the problem to date.

The question of how to deal with the secondary loan market is perhaps an issue which needs to be resolved before the MTC can appropriately recommend the adoption of a market state approach. Development of a solution to this issue will require considerable study as to how the secondary loan markets currently operate. Possible solutions suggest themselves.

1. Tax the Transferee. One solution may well be to require out of state holders of interests in loans properly attributable to a taxing state to pay taxes on their loan income if their tax obligation reaches a certain minimum level. The problem with this solution is that it may be politically impractical to get a state legislature to adopt such a solution in the face of the doomsayers who will predict the demise of the taxing state's available credit.

2. Transaction Tax. Another solution may be to extract a transaction tax on the outbound sale of such loans, thereby imposing in effect a tax on the revenue which is being moved out of state by the sale. A transaction tax likewise would not be very popular politically, because the incidence of that kind of tax is more easily directly transferable to the debtor.

3. Assignment of Income. A third solution may be to develop a legal rule which will support the imputation of the loan income to the transferor/seller as such income is realized by the out of state transferee/purchaser. This solution offers the prospect of avoiding claims that to tax the secondary loan market is to kill the taxing state's available credit. Such a tax would not be easily transferable to the debtor either, because the tax, like any income tax, would be folded into the return the financial institution would have to receive on its lendable funds. The transactions which exist in some of secondary loan markets may well afford a rational basis for imposing such a tax.

II.

INDIANA'S FINANCIAL INSTITUTIONS TAX STATUTE.

The Uniformity Committee requested that staff provide it with a brief description of the new Indiana statute providing for taxation of financial institutions. Indiana House Enrolled Act No. 1625 creates what is described as a dual system approach, *i.e.*, one that incorporates both a residence-based and a source based measure of tax. Indiana, the domiciliary state, imposes a franchise tax upon its resident financial institutions' adjusted gross income (defined by IRC Section 63) and adjusted by subtracting, among other items, foreign source income; and then provides them with a credit for income or franchise taxes paid to other states. The tax credit allowed to a resident taxpayer is the lesser of either (1) the amount of creditable tax actually paid to other U.S. state taxing jurisdictions; or (2) the amount of creditable tax that would be due using Indiana's tax rate on the lesser of: (a) the taxpayer's adjusted gross income that is subject to taxation by the other taxing jurisdictions; or (b) the taxpayer's adjusted gross income attributable to the other taxing jurisdictions under the Indiana attribution rules.² (See Ch.2, Sec. 5.).

For non-resident financial institutions transacting business in Indiana, Indiana imposes an apportioned franchise tax. A financial institution is "transacting business" in Indiana, if it maintains an office in Indiana; has an employee, representative or independent contractor conducting business in Indiana; regularly sells products or services to Indiana customers; regularly solicits business from potential customers in Indiana; regularly performs services outside of Indiana that are consumed within Indiana; regularly engages in transactions with Indian customers that involve intangible property, including loans; owns or leases personal or real property located in Indiana; and regularly solicits and receives deposits from customers in Indiana.

The method for apportionment of income of non-resident financial

²It should be noted that this provision ensures that sourcing rules will be required for both domestic and out-of-state financial institutions.

institutions is based upon a single-factor: total receipts attributable to transacting business in Indiana divided by total receipts from transacting business in all state taxing jurisdictions. The non-resident financial institution is entitled to a tax credit:

"(a) for the amount of net income tax due to the nonresident taxpayer's domiciliary state for a taxable year if:

(1) the receipt of interest or other income from a loan or loan transaction is attributed both to the taxpayer's domiciliary state under that state's laws and also to Indiana under IC6-5.5-4; and

(2) the principal amount of the loan is at least two million dollars (\$2,000,000).

(b) The amount of the credit for each taxable year is the lesser of:

(1) the portion of the net income tax actually paid by the nonresident taxpayer to its domiciliary state that is attributable to the loan or loan transaction; or

(2) the portion of the net income tax due to Indiana under this article that is attributable to the loan or loan transaction."

The credit provision for non-domiciliary financial institutions is curious, especially when Indiana is also granting a general credit to its domiciliary banks. Whether there is such a significant difference in credit mechanisms to amount to discrimination against the nonresident taxpayer will need to be addressed.

III.

COMPARISON OF MINNESOTA FORMULARY APPORTIONMENT AND INDIANA DUAL (RESIDENCE AND SOURCED BASED) TAX SYSTEMS.

Thus far, we are aware of two states which have adopted a market state approach to apportioning income of a financial institution engaged in a multi-jurisdictional business. Minnesota has adopted a straight formula apportionment approach which is represented by the two draft regulations which the MTC has developed to date. Under formula apportionment, domiciliary and non-domiciliary financial institutions are taxed by the same procedure: by applying sourcing rules to the financial institution's receipts, property and payroll an apportionment fraction is calculated which is then applied to the taxpayer's overall income to determine how much of that income is taxable in the taxing state. Indiana adopted the dual (residence and source based) approach which has been described immediately above. The ideologies of the two approaches are already competing.

To assist the Committee members to begin to evaluate the perceived advantages and disadvantages of these two approaches to market state taxation of financial institutions, a preliminary list of such advantages and disadvantages follows. The list is preliminary because it is neither exhaustive nor the product of wide enough discussion and debate. Committee members are therefore invited and encouraged to evaluate the list critically and to suggest additional observations. In evaluating the list of perceived disadvantages, please keep in mind that technical deficiencies of either approach are not noted to the extent that these deficiencies can be corrected through revision without affecting the basic intended structure of the approach being revised.

MINNESOTA (formulary apportionment approach)

Advantages:

1. Promotion of market state perspective in sourcing income of multi-jurisdictional financial institutions.
2. Utilization of proposed apportionment structure similar to what the U.S. Supreme Court has called the standard by which all other formulary apportionments are measured.
3. Consistency with the wide spread acceptance of formulary apportionment in state taxation of multi-jurisdictional businesses among the states themselves.
4. Avoidance of special problems for states which employ combined reporting for unitary businesses. [Ed. Chapter 5. of the Indiana statute describes the use of combined reporting for members of the unitary group of which the financial is a party and appears to follow the Finnegan, as opposed to the Joyce approach as to factor inclusion of all members of the unitary group.
5. No attempt to tax income properly attributable to another state, thereby avoiding the necessity for a credit mechanism which raises a whole set of independent issues.
6. No potential exportation of the tax policy of the taxing state beyond its own borders. [Ed. Indiana's dual approach does potentially export the taxing state's tax policy to other states, because it taxes the entire income of its domiciliary financial institutions, regardless of where earned and its tax credit may not exceed the taxes paid to the other states.]
7. Political opposition likely to be less, especially due to item #6.
8. Internal consistency to the extent that the same principles are applicable to domiciliary and non-domiciliary financial institutions. [Ed. Indiana's dual approach mixes the business situs principle which justifies 100% taxation of domiciliaries and formula apportionment which eschews 100% taxation of non-

domiciliaries.]

9. Equalization of relative tax burdens between domiciliary and non-domiciliary financial institutions. [Ed. This is probably true only to the extent non-domiciliary financial institutions have a physical presence in the taxing state.]

10. Equalization of relative tax burdens between financial institutions and other segments of business which are engaged in multi-jurisdictional commerce. [Ed. This is probably true, because most segments of industry would be taxed under essentially the same basic tax structure.]

Disadvantages:

A. Generation of relatively lower tax revenues from branchless financial institutions whose physical presence is located out of state. [Ed. This really is a comment on three factor apportionment (receipts, property and payroll) versus a single factor (receipts) apportionment.]

B. Generation of relatively higher tax revenues from domiciliary financial institutions whose physical presence is located within the state as contrasted to out-of-state institutions. [Ed. The comment made immediately above is equally apt here.]

C. Administrative difficulty in sourcing the components of the receipts and property factors. [Ed. The comment pertains to both taxpayers and tax administrators.]

D. Potential for significant lack of uniformity leading to double/overlapping taxation due to diversity of sourcing rules which must be applied.

E. Confusion over the rules applicable to sourcing intangible property and the income generated by intangible property.

F. Potential for taxpayer manipulation of the sourcing rules in large, sophisticated transactions.

G. Promotion of conflict between the market states and the money center states.

H. Uncertainty as to how to handle the taxation of loans sold in the secondary markets or which are securitized.

INDIANA
(dual approach)

Advantages:

1. Promotion of market state perspective in sourcing income of multi-jurisdictional financial institutions.
2. Easier administration for both taxpayers and tax administrators because of the single factor (receipts).
3. Generation of relatively higher tax revenues from branchless financial institutions whose physical presence is located out of state. [Ed. This really is a comment on three factor apportionment (receipts, property and payroll) versus a single factor (receipts) apportionment.]
4. Generation of relatively lower tax revenues from domiciliary financial institutions whose physical presence is located within the state. [Ed. The comment made immediately above is equally apt here.]
5. Resolution of uncertainty as to how to handle the taxation of loans sold in the secondary markets or which are securitized. [Ed. This would appear to be true insofar as the loans are generated by domiciliary financial institutions but would not appear to be true for non-domiciliary institutions which may create

just as big a problem.]

6. Avoidance of a substantial double/overlapping taxation due to the credit mechanism.

7. Equalization of relative tax burdens between domiciliary and non-domiciliary financial institutions.

Disadvantages:

A. Potential exportation of tax policy of domiciliary state on the transaction of business in another state by a domiciliary financial institution. [Ed. This potential arises because of the credit mechanism.]

B. Failure to reflect all items which contribute to the production of income by financial institutions due to utilizing only a single factor (receipts).

C. Politically more difficult to sell, especially because of item A.

D. Confusion over the application of the dual approach to combined reporting for unitary businesses.

E. Mixture of different principles applicable to the taxation of financial institutions by applying both the business situs principle and formula apportionment to a single segment of industry.

F. Taxation of income attributable to another state in the case of domiciliary financial institutions necessitating a credit mechanism which raises issues of per state or aggregate credit, creditable taxes, limitations on the credit given, etc.

G. Significant departure from traditional principles which govern the taxation of multi-jurisdictional businesses.

H. *Creation of the same issues involving formulary apportionment due to the credit mechanism. [Ed. These issues necessarily arise if the credit cannot exceed the tax which Indiana would have imposed under its sourcing rules. In effect, it appears the Indiana approach through its credit mechanism requires application of formulary apportionment not only in the case of non-domiciliaries but also domiciliaries.]

I. Administrative difficulty in sourcing the components of the receipts property factor. [Ed. The comment pertains to both taxpayers and tax administrators.]

J. *Failure to resolve totally how to tax loans which are sold in the secondary market or are securitized. [Ed. This failure arises from the fact than any such loans generated by a non-domiciliary financial institution will be taxed if at all under formulary apportionment.]

K. Creation of disparity in the taxation of financial institutions and other businesses due to the different tax structures which will apply.

IV.

SELECTED POLICY ISSUES THAT NEED TO BE ADDRESSED

A. Will the money-centered states abandon their bias for a residence-based system of taxation, if the other states adopt a source based system? If not, a serious potential for double-taxation will exist. Will this lack of uniformity lead to a serious threat of Congressional intervention? How will increasing globalization of the financial industry affect these trends?

B. Given the yet unanswered issue regarding what amount of contacts between a taxing state and an out-of-state bank will support taxing nexus, can the money-centered states afford to abandon their residence-based approach? Can money-center states give up revenues which will be apportioned out of state under source based apportionment taxation when there is no assurance under the U.S. Constitution that they can pick up income which will be

sourced in state under sourced based apportionment?

C. Assuming the market states have nexus over the out-of-state financials under an economic presence theory, should the money-center states adopt a taxing scheme that apportions out if an insufficient number of states adopt an apportionment approach that would pick up this income?

D. What, if any, role should the MTC play if it desires to recommend a type of apportionment which conflicts with the current approaches taken by money-center and other states that are members of the Commission?

E. Given that Indiana has adopted its dual-based approach and Massachusetts is possibly considering a similar approach, should the Committee now review that approach for possible adoption?

F. Should the MTC and/or its member states be more willing to sell uniformity in the taxation of financial institutions by making appearances before state legislative bodies and tax study committees which are considering these issues? In this regard, should the MTC develop a speakers' bureau which will maintain the names of individuals who are well prepared to testify on specific issues affecting the taxation of financial institutions?

V.

LIST OF THE MAJOR TECHNICAL ISSUES THAT NEED TO BE ADDRESSED

The Uniformity Committee also requested that staff present the Committee with a list of issues for it to decide which, if any, should be addressed by new language. We have broken down the various issue areas for consideration as follows: Nexus, Coverage, Receipts Factor, Property Factor, Throw-Out, Credit Mechanism, Administrative Feasibility, and Implementation Timing. The entries that follow each category heading are various comments thus far received from industry representatives both in writing and orally at our informal regional meetings. We are still in the process of soliciting

comments from industry. Specifically, we have solicited comments from the non-traditional bank segment of the financial community, including savings and loans, thrifts, brokers, foreign banks, credit unions, finance companies, captive financials and the credit card industry. Any comments offered by staff are noted in brackets as "Ed." comments.

In the interest of not overly complicating an already tough subject area, we have exercised some discretion in not bringing to the Committee a multitude of the more mundane drafting and policy issues. Any proposed changes with regard to the "smaller stuff" will be highlighted for you in the next draft of the regulation.

A. NEXUS ISSUES (Section (A)(6)(C)).

1. Is the nexus threshold too low when it rebuttably presumes nexus if 20 or even 100 requisite relationships with its residents have been established or if have \$5,000,000 or more of assets attributable to in-state sources are present?

a. One suggestion: 100 requisite relationships or \$50,000,000 in assets.

b. Another suggestion: use the traditional nexus test; if no traditional nexus, use a sourced "receipts" test between \$750,000 and \$1,000,000. If nexus established under either one or both tests, apply a de minimis tax due threshold of \$1,000 under which no filing would be required.

c. Use a more easily administered nexus threshold.

2. Once nexus is established, is the taxpayer obligated forever, even though its future activities fall below the nexus standard?

3. Does nexus exist if the financial sells its credit card or loan

portfolio, but continues to service those accounts and earn fees from the servicing?

4. What effect should relocation of the debtor or credit-card holder have on the nexus analysis?

5. Should a bank suffer a penalty for failure to make estimated tax payments until it has notice of its having satisfied the requisite nexus standard within the taxing state?

6. Should the financial institution's purchase or holding of a state's security, whether acquired directly or on the open market, create nexus?

B. COVERAGE/EXEMPTION ISSUES.

1. Do we intend to apply the proposed regulation to credit unions, which enjoy substantial exemption from federal and state income taxation? Indiana picks up state credit unions which are insured by the National Credit Union Administration. (See Indiana law at Ch.1, Sec. 17).

2. Should "diversified savings and loan holding" companies be covered by the proposed regulation? Indiana excludes "diversified savings and loan holding" companies.(See Indiana law at Ch. 1, Sec. 17(b).).

3. What is the appropriate definition of coverage? Compare Indiana's definition which is more detailed with the MTC proposal. (See Indiana law at Ch. 1, Sec. 17. and MTC Draft Reg. § (A)(10), (11) and (12)).

4. Indiana's statute Ch. 1, Sec. 17 (D)(2)(B) includes under the "business of a financial institution" definition leasing activities regarding real and personal property in Sec. 18 that is the "economic equivalent" of the extension of credit as defined by the Federal Reserve Board under 12 C.F.R. 225.25(b)(5). Should we also include that activity?

5. Should MTC's proposed regulation define a unitary business engaged in the business of a financial institution? (See Indiana law at Ch. 1, Sec. 18, which defines "unitary business" for the purpose of combined reporting requirements, elimination of inter-company transactions.)

6. Indiana's statute specifically exempts certain activities from its definition of "transacting business". Should we also exempt such activities as:

- a. Maintaining or defending an action or suit?
- b. Filing, extending, transferring, etc. a mortgage, deed of trust, or other security interest?
- c. Acquiring, foreclosing, etc. in-state property as a result of a default under an in-state mortgage, etc.?
- d. Selling tangible personal property in the state if such sales are immune under P.L. 86-272?
- e. Owning an interest in the following types of in-state property and related activities thereto?:

(1) An interest in a real estate mortgage investment conduit, real estate investment trust, or regulated investment company.

(2) An interest in a loan backed security representing ownership or participation in a pool of promissory notes or certificates of interest that provide for payments in relation to payments or reasonable projections of payments on the notes or certificates.

(3) An interest in loan or other assets from which the

interest income is attributed to the taxing state because it arises from loans or installment sales that are either secured by in-state property; or, if unsecured, are made to in-state residents; or arises from unsecured commercial loans if the proceeds of the loan are to be applied in-state.

(4) Fiduciary activities.

(See Indiana law at Ch. 3, Sec. 8.(5) and Ch. 4, Secs. 4, 5, & 6.)

[Ed.: Items 6.a. - 6.c. appear to be derivative of typical state exemptions from having to register as a foreign corporation under a state's business corporation law. These exemptions should not necessarily be used to provide an exemption against a state's income tax. Indeed, many of the activities listed in the first three items are precisely the advantages afforded by a state to an out of state financial institution which justifies a charge for enjoying the fruits of an organized society. Item e raises the whole issue of "securitized loans." Although not all of the transactions described are actually securitized loans, that shorthand is aptly applied to raise the general issue. It would be preferable to state the issue in general terms, rather than to state it in all of its particulars, because focusing on the particulars may understate the issue. In this regard, the Uniformity Committee should decide to what extent the MTC proposal should accommodate the sale of, and investment in, loans generated within a taxing state to or by third parties residing outside of the taxing state.

f. Should MTC's proposal respond to the secondary loan market by not restricting the ability of the taxing state's financial institutions to resell in-state loans to out-of-state investors without regard to the investment medium through which resales

are accomplished? How can a taxing state preserve its right to tax income which is properly sourced to it and which as a policy matter should be taxed by it without unnecessarily damaging the secondary loan market?

One banking representative's suggestion was to avoid damaging the secondary loan market of a state by clearly exempting "participation" loans, i.e., those loans which a lender makes directly but then assigns or otherwise transfers all or a part of it to a purchasing financial institution. "Syndicated" loans would not be exempt, i.e., those multi-bank loan transactions in which all lenders are named parties to the original loan documentation and are known to and are in privity of contract with the borrower. Under this kind of rule, could a syndicated loan be converted into a participation loan by a syndicated lender selling his interest to a participation lender? [Ed.: If a state exempts out-of-state banks whose only connection to the taxing state is the purchase of loans or securitized instruments attributable to the taxing state, should the states nevertheless continue to tax the in-state bank transferor of those instruments in order to preserve the tax that would otherwise be lost on the future receipt of interest income?

(For additional suggestions for exempted activities from nexus consideration, see "Proposed Revisions to MTC's Draft Regulations" submitted by Eugene Mason, First Bank Systems, Minneapolis, MN of April 19, 1989 included here as Exhibit C.)

C. RECEIPTS FACTOR ISSUES.

1. One major concern with respect to the receipts factor is its attempt to source too many types of receipts, thereby increasing a financial institution's administrative and computer system development effort. For example,

Wachovia Bank and Trust of North Carolina reported that it has "over 200 categories of interest income and 400 categories of non-interest income on its General Ledger", but their computer system is not geared to a state sourcing concept. One suggestion is to throw-out all non-interest income from the receipts factor. (See letter of July 11, 1989 from Jonathan Allen of Wachovia appended as Exhibit D. Allen summarizes in his letter a study of the distribution of types of gross income generated by surveyed bank holding companies. Allen presented these figures to support his suggestion to limit the receipts factor to interest bearing items only.)

a. One recommendation suggested that all items of receipts described in the MTC proposal at § (C)(2)(a) through (f) be sourced to the borrower's residence. Additionally, the items of receipts described in § (C)(2)(h) were described as a relatively small percentage of a bank's income which could justify sourcing them to the place of performance. [Ed. Give the bank the option to source non-interest receipts either in the same proportion that the aggregated receipts are allocated to the state under (C)(2)(a) through (h) or to the state of performance as set forth in (C)(2)(h).

If the MTC proposal would permit this option, we may have to exempt specific types of institutions from these rules.

2. It is suggested that the receipts numerator and denominator, as well as any receipts test for nexus purposes, be derived from book figures, with the reason given that such would facilitate reconciling the numerator and denominator figures used as cost figures are not readily available.

3. Receipts are double-weighted in the MTC proposal, because the same sourcing rules for intangibles and income from intangibles are used in the property and receipts factors.

4. One suggestion to avoid the complexity is to use only a two-factor (receipts and payroll) or a one-factor (receipts).

5. The address presumption under (A)(17) is subject to manipulation with respect to large transactions.

D. PROPERTY FACTOR ISSUES.

1. Exclude intangibles from the property factor, as the inclusion is inconsistent with the concept of sourcing intangibles to the commercial domicile of the taxpayer. [Ed. It may not be inconsistent with sourcing intangibles to their business situs.]

2. The property factor should include deposits, because they are significant to the production of income. [ed. Although deposits are not a balance sheet asset, neither is rental property which is considered under UDITPA property factor at a multiple of 8 of the rent paid. Banks rent deposits by paying interest. It would not be necessary to adjust interest paid by a multiple, because the actual value of deposits generating the interest can in most cases be calculated as a sum certain.]

3. Make use of the property factor optional to the taxpayer.

4. Original cost, as opposed to current federal tax basis, should be used for valuing property. See (C)(3). [Ed. What problems exist with using original cost, as opposed to federal income tax basis, and how could intangible property be valued? Do financial institutions actually maintain their records consistent with the comment being made?]

5. One suggestion was to limit the property factor to real and tangible personal property, but to proportionately adjust this factor to take into consideration the amount of intangible property being excluded. For example, if only 10% of the total property is represented by tangible/real property, then the overall weight of the property factor (33 1/3%) would be reduced by 90% with the remaining two factors being proportionately increased. [Ed. ?]

E. CREDIT CARD INCOME ISSUES.

1. One participant observed that income received from fees and interest arising from the issuance of credit cards is relatively small. See attachment to Attachment D. New York without a large credit operation within the state takes a market state approach and apportions credit card interest income to the domicile of the credit card holder. South Dakota with a very large credit card operation takes a money center approach and imposes its bank tax on 100% of its domiciliary financials' credit card income, regardless of the location of the card holder. Is there a sound policy reason why credit card income should not be treated the same as other types of interest and fee income for allocation or apportionment purposes?

2. Should the MTC proposed regulation be phased in with the treatment of credit card income being one of the last items of income to be sourced under market state rules?

F. THROW-OUT ISSUE.

If the financial institution is not "taxable in a state" under the definition of § (A)(17), how are the factor numerators and denominators affected? [Ed. Sections (C)(2)(l), (C)(3)(j) and (C)(4)(a) provide for a throw-out from the numerator and denominator of receipts, property or payroll, respectively, of the factors in a state that lacks jurisdiction to tax. Is this the desired approach? A state is defined to include a foreign country for the purpose of this provision.]

G. CREDIT MECHANISM ISSUES.

[Ed.: Based on language contained in recent U.S. Supreme Court cases, a credit for taxes paid to other states is an important factor to defend a taxing statute from a Commerce Clause challenge. See, the D.H. Holmes and Goldberg v. Sweet cases. This is especially true for unapportioned taxing schemes.

Indiana's bank tax scheme, which imposes a franchise tax on 100% of the resident bank's income, provides a credit for taxes paid to other states is thought necessary to comply with the Commerce Clause. See the Court's reference to the effect of the existence of a credit in the Holmes and Goldberg cases. Under the current proposals being considered by the Committee, no credit mechanism should be required to save them from a Commerce Clause challenge, because we are dealing with an apportioned tax scheme whose design premise is not to result in an excess of 100% of the net income being subject to tax, assuming all states have adopted substantially the same taxing methodology. This basic assumption, however, clearly disregards the current approach of the money-center states; and, in fairness to the financial industry, this circumstance should be considered by the Committee when it suggests the tax policy that the member states should follow. A limited credit might be proposed therefore for financial institutions domiciled in a money center state for a limited transition period.]

The credit mechanism with respect to a nonresident under the Indiana statute is limited solely to the domiciliary state's tax that has been applied to the interest income attributable to loans in excess of \$2,000,000 which have been sourced to both the Indiana pre-apportionment tax base and the domiciliary state's pre-apportionment tax base. One issue to look further into is whether this credit is broad enough to meet Commerce Clause scrutiny.

H. **ADMINISTRATIVE FEASIBILITY ISSUES.**

1. Compliance costs caused by the regulation will enormous in relation to the revenue result. A more simple method, without the necessity of tracking all types of receipts, is necessary to get achieve compliance. An institution with 35 affiliated entities possibly would have to file 1750 returns. The data sought for the regulations is not available on current data bases used by the institutions for business purposes. Use of existing data should be the goal of any apportionment system. [Ed. We have seen some statements that suggested computer system development to capture income-source information would cost one institution in excess of \$700,000.]

2. The concept of a one-stop, filing and payment point merits some thought.

I. **IMPLEMENTATION TIMING ISSUE.**

Should the Committee explore developing a trigger mechanism to implement the proposal which would require satisfaction of a condition precedent before the Commission would commit to recommending to the states any given bank tax system? For example, in order to promote the uniformity we all seek, a Commission recommendation might include the requirement that a certain minimum number of states first commit to adopt the recommended approach before it became an MTC proposal. In this manner, the Commission's attempt to achieve uniformity among tax systems will be promoted and, at the same time, the substance of the Commission's preferred approach, whatever the approach, will still be made publicly available for consideration by the states.

SCHEDULE OF EXHIBITS:

"A"--The two MTC draft proposals: 07/87 (S. McCray) and 01/89 (per revision of Bank of America's Phil Plant).

"B"--Indiana Financial Institutions Tax Statute.

"C"--Comments of First Bank Systems, Minneapolis, MN, of 04/89 (per Eugene Mason).

"D"--Comments of Wachovia Bank and Trust, Winston-Salem, NC (per Jonathan Allen).

EXHIBIT B: 22

**Letter from Marvin C. Umholtz
(Credit Union National Association, Inc.)
(November 20, 1989)**

Credit Union National Association, Inc.

805 15th Street, NW, Suite 300, Washington, DC 20005-2207, 202-682-4200



November 20, 1989

Mr. Paull Mines, Counsel
Multistate Tax Commission
944 North Capitol Street, N.W.
Washington, D.C. 20001

Re: MTC "Proposed Regulation for the Attribution of the Income of
Financial Institutions"

Dear Mr. Mines:

I would like to express our association's continuing interest in the Multistate Tax Commission's project to develop a proposed model financial institution tax regulation. The "market approach" to taxing financial institution income envisioned by the proposal is revolutionary and could dramatically affect business decisions made by for-profit financial institutions such as banks and savings and loan associations. The Multistate Tax Commission is to be commended for its recognition of the significant public policy consequences of the proposal and for developing procedures for public comment and discussion.

Credit unions are an entirely unique sector of the financial services community. Organized under the Federal Credit Union Act (12 U.S.C. 1751 *et seq.*), forty-seven state acts or the Puerto Rican credit union law, credit unions are the non-profit alternative to the for-profit financial services sector. Credit unions are member (consumer) owned and democratically controlled cooperatives that provide consumer-oriented personal financial services. Credit unions are organized without capital stock and operated for mutual purposes and without profit. The combined assets of all credit unions are less than the nation's largest bank. Nearly eighty percent of all credit unions are \$10 million or less in assets.

Federal credit unions are exempt from federal and state income or franchise taxation (12 U.S.C. 1768). As of June 1989, our research reveals that only two states require domestically-chartered credit unions to pay a corporate income tax; five impose a franchise tax. The vast majority of states and the federal government do not impose these taxes on state-chartered credit unions. (26 U.S.C. 501(c)(14).)



In contrast to traditional for-profit corporate income taxation, the Multistate Tax Commission model proposes a "market approach," essentially linking the tax with a service and the location at which that service is delivered. Historically, tax exemptions are based on a "purpose test" and have no linkage to specific services or products. We are concerned that the MTC proposal does not accommodate the purpose-tested tax exempt treatment of credit unions.

While there is no indication that it is the proposal's intent, the broadly written language defining "Exercising a Corporate Franchise or Transacting Business in a State," "Business of a Financial Institution," and "Financial Institution" could inadvertently lead a state revenue department to attempt to administer the proposed tax regulation's provisions on non-profit, tax exempt credit unions.

CUNA would favor inclusion of a statement that the tax regulation does not apply to credit unions. The imposition of income taxation on credit unions, whether inadvertent or by design, is no ordinary issue for our association, our fifty-two state leagues and the nation's 15,000 state and federal credit unions. Now more than ever, this country and its citizens need a non-profit alternative like credit unions. Protecting the special role of credit unions is our association's number one public policy priority.

Thank you for providing this opportunity to participate in the Multistate Tax Commission's proposed tax regulation model development process. Please consider our interest in this project to be continuous throughout its development. I will be participating in the "State Taxation and Regulation of Banking: Time to Reform?" workshop on December 13th cosponsored by the MTC, National Conference of State Legislatures, National Center for Policy Alternatives, and Advisory Commission on Intergovernmental Relations and would welcome the opportunity to discuss this matter in more detail at that time.

If you have any questions or desire additional information, please do not hesitate to contact me.

Sincerely,



Marvin C. Umholtz, Vice President
State Governmental Affairs

EXHIBIT B: 23

**Letter to Various Financial Institutions Organizations
(November 22, 1989)**

Multistate Tax Commission



November 22, 1989

Re: Multistate Tax Commission: Financial Institution
Regulation

Informal Discussion--December 12, 1989 at 1:30 p.m.
Conference Room 211, Hall of the States
444 No. Capitol Street, N.W.
Washington, D.C. 20001

Dear ***

The Multistate Tax Commission has now arranged to sponsor an informal discussion of the proposed financial institution regulation which it has developed thus far. We have scheduled a participatory discussion meeting beginning at 1:30 p.m. on Tuesday, December 12, 1989, in Conference Room 211 of the Hall of the States, 444 No. Capitol Street, N.W., Washington, D.C. 20001.

We selected December 12, 1989, as the date of our discussion meeting, because that date precedes by one day the NCSL, ACIR, MTC and NCPA jointly sponsored conference in Washington, D.C., "State Taxation and Regulation of Banking: Time for Reform?" Our scheduling will permit one inclusive trip for those who wish both to attend this important conference and also to participate in MTC's formulation of an apportionment regulation to govern the financial industry. (A brochure describing the Conference is enclosed for your ready use.)

The Conference and the MTC's financial institution regulation project reflect the increased interest which the states now have to develop a specialized industry regulation to govern the state taxation of the financial industry. We, therefore, also expect representatives of state tax administrators who are attending the NCSL, ACIR, MTC and NCPA sponsored Conference also to attend our informal discussion meeting.

If your group or company continues to have interest in impacting the MTC's regulation development, now is the time to do so. While domestic, commercial banks have participated in several similar discussion meetings, this is the first time a discussion meeting has been held to solicit comments from the

Headquarters Office:
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Washington, D.C. 20001
(202) 624-8699

New York Audit Office:
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New York, NY 10036
Telephone (212) 575-1820

Chicago Audit Office
30 W. Washington, Suite 1000
Chicago, Illinois 60602
Telephone (312) 263-3232

Houston Audit Office
One Park 10 Place, Suite 128
Houston, Texas 77084
Telephone (713) 492-2260

re: MTC Financial Reg
November 22, 1989
Page 2

other important segments of the financial industry, including credit cards, savings institutions, finance companies (captive and non-captive), the securities industry and foreign banks.

The purpose of the informal discussions will be to solicit your group's or company's comments or concerns about the MTC financial institution regulation project and otherwise to exchange views on the issues raised by state taxation of the financial industry. The MTC believes it can learn from your comments. The MTC also believes it will be able to clarify its preliminary proposal so that you will have a better understanding of it.

In order that we may make appropriate arrangements for seating and refreshments, would you please advise Ms. Sylvia White at (202) 624-8699 during normal working hours, Eastern Time Zone, as to who will attend the MTC informal discussion on December 12, 1989, beginning at 1:30 p.m. Feel free to contact me also if you have any questions or comments about this informal discussion.

The MTC eagerly anticipates your possible participation in the informal discussion.

Very truly yours,
Multistate Tax Commission

By _____
Paul Mines, Counsel

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11/89

List of addressees to which the foregoing was sent:

1. Ms. Sheila J. Slaughter
General Counsel and Sr. V. President
California League of Savings Institutions
9800 S. Sepulveda Blvd.
Suite 500
Los Angeles, CA 90045-0054

re: MTC Financial Reg
November 22, 1989
Page 3

2. Mr. Brent Frost
Glendale Federal Bank
210 W. Lexington
Glendale, CA 91209
3. Ms. Colleen Kelly
Credit Union National
Association
805 15th Street, N.W.,
#300
Washington, D.C.
20005-2207
4. Mr. Michael Palko
Sr. V. President
Great Western
Financial
Corporation
8484 Wilshire Blvd.
Beverly Hills, CA
90211
5. Mr. Tim Jones
VISA USA, Inc.
P.O. Box 8999
San Francisco, CA
94128
6. Mr. Robert Williams
Mastercard
International
888 Seventh Avenue
New York, NY 10106
7. Mr. David Danovitch
National Council of
Savings
Institutions
1101 15th street,
N.W., #400
Washington, D.C. 20005
8. Ms. Diane Casey
Independent Bankers
Association
of America
One Thomas Circle,
N.W., #950
Washington, D.C. 20005
9. Ms. Mary Pfaff
Mortgage Bankers
Association
of America
1125 15th Street,
N.W., #700
Washington, D.C.
20005
10. Mr. William Larsen
Securities Industry
Association
1850 M Street, N.W.,
#550
Washington, D.C.
20036
11. Mr. Robert McKew
American Financial
Services
Association
1101 14th Street,
N.W., #400
Washington, D.C.
20005
12. Institute of
International
Bankers
c/o Mr. John L. Carr,
Jr.
Shaw, Pittman, Potts
& Trowbridge
2300 N Street, N.W.
Washington, D.C.
20037
13. Mr. Don Weeks
U.S. League of
Savings
Institutions
111 East Wacker Drive
Chicago, IL 60601
14. Mr. Coley O'Brien
U.S. League of
Savings
Institutions
1709 New York Avenue,
N.W., #801
Washington, D.C.
20006

re: MTC Financial Reg
November 22, 1989
Page 4

Additional addressee
(added 11/28/89)
Mr. Phil Plant
Vice President & Assistant
General Tax Counsel
Bank of America
Tax Department 3245
P.O. Box 37000
San Francisco, CA 94137

Multistate Tax Commission



NOTICE

A PARTICIPATORY DISCUSSION MEETING ON THE MTC DRAFT FINANCIAL INSTITUTE REGULATION IS SCHEDULED TO BE HELD ON TUESDAY, DECEMBER 12, 1989. YOU ARE INVITED TO ATTEND THIS IMPORTANT MEETING WHICH WILL OCCUR ONE DAY PRIOR TO THE NCSL, ACIR, MTC AND NCPA JOINTLY SPONSORED CONFERENCE, "STATE TAXATION AND REGULATION OF BANKING: TIME FOR REFORM?" THE SPECIFIC DETAILS OF THIS PARTICIPATORY DISCUSSION MEETING FOLLOW:

TOPIC: MTC DRAFT FINANCIAL INSTITUTE REGULATION

DATE: TUESDAY, DECEMBER 12, 1989

PLACE: CONFERENCE ROOM 211, HALL OF THE STATES, 444 NO. CAPITOL, N.W., WASHINGTON, D.C.

TIME: 1:30 p.m.

MORE INFORMATION: PAULL MINES, COUNSEL, MULTISTATE TAX COMMISSION, 444 NO. CAPITOL, N.W., #409, WASHINGTON, D.C. 20001, TELEPHONE (202) 624-8699.

uc\finregnb.not

11/89

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Houston Audit Office:
15835 Park Ten Place, Suite 104
Houston, TX 77084
Telephone (713) 492-2260

Multistate Tax Commission



MEMORANDUM

TO: Members, Uniformity Committee

FROM: Paul Mines, Counsel

SUBJECT: Informal Discussion Meeting on the MTC Draft Financial Institutions Regulation

DATE: November 22, 1989

Attached is a copy of a letter we have mailed this date to various persons in the non-commercial banking side of the financial industry. The letter invites these representatives, primarily industry tax lobbyists, to attend a participatory discussion meeting on the MTC financial institution regulation project one day prior to the NCSL, ACIR, MTC and NCPA jointly sponsored conference, "State Taxation and Regulation of Banking: Time for Reform?" The MTC discussion meeting is specifically scheduled for Tuesday, December 12, 1989, beginning at 1:30 p.m. in conference room 211 of the Hall of the States, 444 No. Capitol Street, N.W., Washington, D.C. 20001. The discussion meeting will solicit comments from some of the segments of the financial industry which have not yet reacted to the MTC proposal.

We wish to advise you of this scheduling so that should you or any of your colleagues be planning to attend the December 13, 1989, Conference, you could give consideration to attending the discussion meeting also on December 12, 1989. We hope that some of you will be able to participate in this important discussion meeting with financial institutions representatives on the non-commercial banking side.

Please do not hesitate to call if you have any questions or comments.

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15835 Park Ten Place, Suite 104
Houston, TX 77084
Telephone (713) 492-2260

EXHIBIT B: 24

**Letter from Donald Kinley
(First Commerce Bankshares, Inc.)
(December 20, 1989)**

FIRST COMMERCE

December 20, 1989

Mr. Paul Miles
Multistate Tax Commission
444 North Capital Street N.W.
Suite 409
Washington, DC 20001

Dear Sir:

I am writing in response to your proposed regulations for the Attribution of the Income of Financial Institutions. First Commerce Bancshares, Inc. is a multi-bank holding company located in Lincoln, Nebraska with approximately \$1 billion in assets. Our largest bank subsidiary, the National Bank of Commerce, currently has approximately 100,000 credit cards outstanding with \$53.5 million in receivables on those cards. Any credit card operation of this size is going to have a small number of cards in all 50 states just due to people moving around the country. Over 70% of our cards though are located within just three states. Your current proposal would require us to file tax returns in 41 different states.

It would cost First Commerce \$350-500 in accountant fees alone to file a state tax return. This does not include employee costs and computer costs to generate the information required to file the return.

On a separate attachment I have made several assumptions and tried to estimate what kind of state income taxes could be generated to a state with 100 of our cards in their state. I computed that maybe the taxes generated could range between \$220-300. As I just said, it would cost First Commerce \$350-500 of expense to our accountants to generate that income.

In my calculations on the attachment, I ignored the fact that most states allow corporations to exclude interest on U.S. Government obligations from state taxable income. This creates a taxable loss for First Commerce, yet we would still be required to file a tax return in 41 different states and pay our accountants \$350-500 per return or approximately \$20,000 in total). I have enclosed as support to my comments Page 1 from our 1988 Federal Tax return and the front page from three states we already file in. As you can see, even though we file the returns as required, there are no income taxes generated to any of the states.

DEC 27 1989

Mr. Paul Miles
Page Two
December 20, 1989

In closing, I sincerely hope you reconsider your proposals. I do not believe your proposals would generate substantial amounts of income taxes, yet they would be a financial hardship on the financial institutions affected.

Sincerely,
FIRST COMMERCE BANCSHARES, INC.


Donald Kinley
Vice President

ESTIMATED STATE INCOME TAXES GENERATED
ON 100 CREDIT CARDS

RECEIPT FACTOR:

100 cards @ \$543 average balance/card	\$54,300 avg. balance
Interest rate on receivables	<u>x18%</u>
Gross interest income/year	\$9,774
100 cards @ \$12 annual fee	<u>1,200</u>
TOTAL GROSS INCOME on 100 cards	\$10,974
 Estimated First Commerce Gross Receipts	 120,000,000
Apportionment Factor	.0091%

PROPERTY FACTOR:

100 cards @ \$543/card	\$54,300
Estimated total receivables of FCB	\$53,491,417
Other Property	<u>58,000,000</u>
TOTAL PROPERTY	\$111,491,417
 Apportionment Factor	 <u>.0487%</u>
Average of two apportionment factors	.0289%
State Taxable Income based on projected federal taxable income of \$15,000,000	\$4,350
 Average tax @ a rate of 5%	 \$220
Average tax @ a rate of 7%	\$300

Check if a— A Consolidated return <input checked="" type="checkbox"/> Personal holding co. <input type="checkbox"/> Personal service corp (as defined in Temp. Regs. sec. 1.441-4T—see instructions) <input type="checkbox"/>	Use IRS label. Otherwise, please print or type.	Name First Commerce Bancshares Inc. c Subs	B Employer identification number 47-0683029
		Number and street (or P.O. box number if mail is not delivered to street address) P.O. Box 82408	E Date incorporated 1985
		City or town, state, and ZIP code Lincoln Ne 68501	F Total assets (See Specific Instructions.) Dollars \$ 954,827,613

6 Check applicable boxes: (1) Initial return (2) Final return (3) Change in address

Income	1a Gross receipts or sales	b Less returns and allowances	c Bal ▶	1c
	2 Cost of goods sold and/or operations (Schedule A)			2 Schedule 1
	3 Gross profit (line 1c less line 2)			3
	4 Dividends (Schedule C, line 19)			4
	5 Interest			5
	6 Gross rents			6
	7 Gross royalties			7
	8 Capital gain net income (attach separate Schedule D)			8
	9 Net gain or (loss) from Form 4797, Part II, line 18 (attach Form 4797)			9
	10 Other income (see instructions—attach schedule)			10
	11 Total income—Add lines 3 through 10 and enter here ▶			11 114,586,894

Deductions (See instructions for limitations on deductions.)	12 Compensation of officers (Schedule E)			12 Schedule 1
	13a Salaries and wages	b Less jobs credit	c Balance ▶	13c
	14 Repairs			14
	15 Bad debts			15
	16 Rents			16
	17 Taxes			17
	18 Interest			18
	19 Contributions (see instructions for 10% limitation)			19
	20 Depreciation (attach Form 4562)	20		
	21 Less depreciation claimed in Schedule A and elsewhere on return	21a		21b
	22 Depletion			22
	23 Advertising			23
	24 Pension, profit-sharing, etc., plans			24
	25 Employee benefit programs			25
	26 Other deductions (attach schedule)			26
	27 Total deductions—Add lines 12 through 26 and enter here ▶			27 99,383,535
	28 Taxable income before net operating loss deduction and special deductions (line 11 less line 27)			28 15,203,559
29 Less: a Net operating loss deduction (see instructions)	29a 762,614			
b Special deductions (Schedule C, line 20)	29b 83,330		29c 845,946	

Tax and Payments	30 Taxable income (line 28 less line 29c)			30 14,357,613
	31 Total tax (Schedule J)			31 4,225,519
	32 Payments: a 1987 overpayment credited to 1988	32a 842,813		
	b 1988 estimated tax payments	32b 5,150,000		
	c Less 1988 refund applied for on Form 4466	32c (800,000)	d Bal ▶	32d 5,192,813
	e Tax deposited with Form 7004	32e —		
	f Credit from regulated investment companies (attach Form 2439)	32f —		
	g Credit for Federal tax on fuels (attach Form 4136)	32g —		32h 5,192,813
	33 Enter any penalty for underpayment of estimated tax—check <input type="checkbox"/> if Form 2220 is attached			33 —
	34 Tax due—If the total of lines 31 and 33 is larger than line 32h, enter amount owed			34 —
35 Overpayment—If line 32h is larger than the total of lines 31 and 33, enter amount overpaid			35 317,294	
36 Enter amount of line 35 you want: Credited to 1989 estimated tax ▶ 317,294 Refunded ▶			36	

Please Sign Here

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Signature of officer: Donald D. Finkley Date: 9/15/89 Title: Vice President

Preparer's signature: [Signature] Date: 9/14/89 Check if self-employed Preparer's social security number: 506 60 9813

Preparer's Use Only: Firm's name (or yours if self-employed) and address: Boüche Ross & Co. E.I. No.: 13 1939741 ZIP code: 68508-1469

1988 Form 112 - Colorado State Corporation Income Tax Return

for other tax year beginning _____, 1988, ending _____, 19 _____.

ACE LABEL HERE	Name <i>First Commerce Bancshares, Inc.</i>		Account number (Colo. I.D. No.) <i>21-62580</i>
	Number and Street <i>P.O. Box 82408</i>		Federal employer I.D. Number <i>47-0643029</i>
	City, State <i>Lincoln Ne</i>	ZIP Code <i>68501</i>	

- A. This return is being filed for:
- (42) A corporation not apportioning income;
 - (43) A corporation doing an interstate business apportioning income under the Colorado Income Tax Act (Schedule A, Page 2);
 - (44) A corporation doing an interstate business apportioning income under the multistate compact (Schedule AS-4);
 - (45) A corporation electing to pay a tax on its gross Colorado sales under the multistate compact;
 - (46) An S corporation (attach Schedule S);
 - (47) A foreign sales corporation.

COMPLETE QUESTIONNAIRE AT TOP OF PAGE 2 OF THIS FORM

Business code number per federal return <i>7389</i>	1. Federal taxable income from Form 1120 or 1120A or ordinary income from Form 1120S 1	<i>14,352,613</i>
Give year corporation began doing business in Colorado <i>1986</i>	2. Federal net operating loss deduction 2	<i>762,616</i>
	3. Colorado income tax deduction 3	<i>-</i>
Check this box if this return is filed under extension. <input checked="" type="checkbox"/>	4. Other additions, attach explanation <i>Tax-exempt interest</i> 4	<i>2,321,274</i>
	5. Total line of 2, 3, and 4 5	<i>3,083,890</i>
Give extended due date. <i>-15-89</i>	6. Total lines 1 and 5 6	<i>17,441,503</i>
	7. Exempt federal interest, explain <i>U.S. Gov't interest</i> 7	<i>21,073,624</i>
TAX RATES For years beginning before July 1, 1988: Taxable Income Rate 1st \$50,000 5.5% Balance 8%	8. Colorado income tax refund 8	<i>-</i>
	9. Other subtractions, attach explanation 9	<i>-</i>
For years beginning on or after July 1, 1988: Taxable Income Rate 1st \$50,000 5% Balance 5.5%	10. Total of lines 7, 8 and 9 10	<i>21,073,624</i>
	11. Modified federal taxable income, line 6 minus line 10 11	<i>(3,632,421)</i>
Make checks payable to and mail return to the Colorado Department of Revenue 1375 Sherman Street Denver, CO 80261	12. Colorado taxable income before net operating loss deduction 12	<i>(2,652)</i>
	13. Colorado net operating loss deduction 13	<i>(10,313)</i>
	14. Colorado taxable income, line 12 minus line 13 14	<i>(22,965)</i>
	15. Tax (rates at left). Check <input type="checkbox"/> if from Schedule 112-TC 15	
	16. New business facility credit from Form 112 NFC 16	
	17. Old investment tax credit from Form 112-CR 17	
	18. New investment tax credit Form 112-CR 18	
	19. Enterprise zone investment credit from Form 112-CR 19	
	20. Enterprise zone employee credit from Form 112-CR 20	
	21. Other credits, explain 21	
	22. Total credits, lines 16 through 21 22	
	23. Net tax, line 15 minus line 22 23	
	24. Investment credit recapture 24	
	25. Total of lines 23 and 24 25	
	26. Payments and credits on estimated tax 26	
	27. Payments on extension of time for filing 27	
	28. Total of lines 26 and 27 28	
	29. Balance due, line 25 minus line 28. Include penalty (96) • \$ _____ and interest (97) • \$ _____, if applicable 29	
	30. Overpayment, line 28 minus line 25 30	
	31. Overpayment to be credited to estimated tax 31	
	32. Overpayment to be refunded 32	

Under penalties of perjury in the second degree, I declare that I have examined this return and to the best of my knowledge it is true, correct and complete.

Donald D. Fisher 9/15/89
(Signature) (Date)
Vice President
(Title)

Touche Ross & Co.
1040 NBC Center
Lincoln, Nebraska 68508-1469

SSN: 506-60-9813 EIN: 13-1939741

Robert J. Submitt 9/14/89
(Name of person or firm preparing return)

TAXPAYER'S COPY

STATE OF IOWA
IOWA CORPORATION INCOME TAX RETURN
To Be Used for Calendar Year 1988 or

IA 11220

Fiscal Year Beginning _____, 19____, Ending _____, 19____

1988

Corporation Name and Address <i>First Commerce Bancshares, Inc.</i>		A. Fed. Emp. I.D. No. <i>47-0683029</i>	Do Not Use This Space
<i>P.O. Box 82408</i>		B. County No. / C. Business Code	
<i>Lincoln Nebraska 68501</i>		D. Basis of Return: Cash <input type="checkbox"/> Accrual <input checked="" type="checkbox"/>	

Type of Return: (Check one) REGULAR COOPERATIVE (IRC §6072d) UBIT
 Was the federal net income or tax for any prior period adjusted during the current period? YES NO
 Indicate years _____ . Submit copies of federal audits under separate cover.

IMPORTANT: Attach a complete copy of your Federal Return filed with the Internal Revenue Service.
 All applicable lines on pages 1 and 2 must be completed for the Department to accept the return.

NET INCOME	1. NET INCOME from federal return	1.	<i>15,120,229</i> ▲
	2. FEDERAL TAX (enter 50% of federal tax)	2.	<i>2,437,760</i> ▲
	3. EBALANCE (subtract line 2 from line 1)	3.	<i>12,682,469</i>
	4. FEDERAL SECURITIES (interest and dividends)	4.	<i>21,073,624</i>
	5. OTHER REDUCTIONS (list)	5.	<i>-</i>
	6. TOTAL REDUCTIONS (add lines 4 and 5)	6.	<i>21,073,624</i> ▲
	7. EBALANCE (subtract line 6 from line 3)	7.	<i>(8,391,155)</i>
	8. IOWA INCOME TAX taken as a deduction on federal return	8.	<i>-</i>
	9. INTEREST AND DIVIDENDS exempt from federal income tax	9.	<i>2,321,274</i>
	10. OTHER ADDITIONS (list)	10.	
	11. TOTAL increase to federal income (add lines 8, 9 and 10)	11.	<i>2,321,274</i> ▲
	12. NET INCOME (add lines 7 and 11)	12.	<i>(6,069,881)</i>
ADJUSTABLE INCOME	13. NONBUSINESS INCOME (net allocable nonbusiness income)	13.	<i>-</i> ▲
	14. INCOME SUBJECT TO APPORTIONMENT (subtract line 13 from line 12)	14.	<i>(6,069,881)</i>
	5. EBUSINESS ACTIVITY RATIO a. Gross within Iowa	15a.	<i>103,907</i> ▲
	b. Gross within and without Iowa	15b.	<i>116,908,168</i> ▲
	Divide line 15a by line 15b and enter the percentage carried to 6 decimal places	15.	<i>0.89</i> %
	16. APPORTIONED INCOME (multiply line 14 by line 15)	16.	<i>(5,395)</i>
	17. NET NONBUSINESS INCOME allocable to Iowa (attach Schedule AD-1)	17.	<i>-</i> ▲
	18. TOTAL (add lines 16 and 17)	18.	<i>(5,395)</i>
	19. NET OPERATING LOSS DEDUCTION	19.	<i>(8398)</i> ▲
	20. IOWA TAXABLE INCOME (subtract line 19 from line 18)	20.	<i>(13,793)</i>
21. TAX (PART III, page 2)	21.		
22. MINIMUM TAX (Attach IA 4626)	22.		
23. TOTAL TAX (add lines 21 and 22)	23.		
24. ESTIMATED TAX PAYMENTS	24.		
25. TAX PAID WITH EXTENSION (attach IA 7004)	25.		
26. MOTOR FUEL TAX CREDIT (attach IA 4136)	26.		
27. IOWA RESEARCH ACTIVITIES/NEW JOBS CREDIT (attach IA 128)	27.		
28. TOTAL CREDITS (add lines 24, 25, 26 and 27)	28.		
29. TAX DUE (if line 28 is less than line 23)	29.		
30. PENALTY (if underpayment penalty, check here <input type="checkbox"/> and attach IA 2220)	30.		
31. INTEREST	31.		
32. TOTAL DUE (add lines 29, 30 and 31) INCLUDE CHECK PAYABLE TO TREASURER, STATE OF IOWA	32.		
33. OVERPAYMENT (if line 28 is greater than line 23)	33.		
34. REFUND (amount on line 33 to be refunded)	34.		
35. CREDIT TO ESTIMATED TAX (amount on line 33 to be credited)	35.		

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief it is a true, correct, and complete statement of the taxpayer's income, deductions, and credits for the year shown on the return.

1/5/89
Date
2/17/89
Date

Donald D. Kelly
Signature of Officer
John J. Dubois
Signature of individual or firm preparing the return
Touche Ross

Vice President
Title
Touche Ross
1046 NBC Center
Lincoln, NE 68508
Preparer's Address
SSN: 506-60-9813
EIN: 13-1939741
F.E.I. or Soc. Sec. No.

TAXPAYER'S COPY

For the taxable year beginning 1988, ending 19

Do not write in this space except to write your file number if known.

C- File Number

First Commerce Bankshares, Inc.
1 Street of Principal Office
2. Box 8248
Lincoln Ne 68501

B. Federal Identification Numbers
(Enter both if applicable)
1. Single entity
2. Consolidated parent
47-0683029
C. State and Date of Incorporation
Nebraska - 1985
D. State of Commercial Domicile
Nebraska
E. Type of Federal Return Filed
1. () Separate
2. (X) Consolidated

Validation Number
F. Business Code Number
7389
G. Date Business Began in Kansas
1987
H. Check if:
1. () Initial Kansas return
2. () Prior Kansas return

A. Method Used to Determine Income of Corporation in Kansas
1. () Activity wholly within Kansas
2. (X) Single entity three factor formula apportionment (Part II)
3. () Consolidated income accounting three factor formula apportionment (Part II)
4. () Combined income accounting three factor formula apportionment (Attach Schedule 121)
5. () Qualified elective two factor formula (Part II) Year qualified
6. () Common carrier mileage (Attach schedule)
7. () Alternative or separate accounting (Attach letter of authorization & schedule)

1. Federal taxable income	1	14352613
2. Total state and municipal interest	2	2413
3. Taxes on or measured by income or fees or payments in lieu of income taxes (Schedule required)	3	
4. Federal net operating loss deduction	4	262616
5. Other additions to federal taxable income (Schedule required)	5	
6. Total additions to federal taxable income (Add lines 2, 3, 4, & 5)	6	765029
7. Interest on obligations of the United States (Schedule required) <u>U.S. Gov't</u>	7	121644
8. Other subtractions from federal taxable income (Schedule required) <u>Bank Subs</u>	8	16338192
9. Total subtractions from federal taxable income (Add lines 7 & 8)	9	16459836
10. Net income before apportionment (Line 1 plus line 6 minus line 9)	10	1332194
11. Nonbusiness income—Total company (Schedule required) <u>Amort. of Change in Acct.</u>	11	195563
12. Apportionable business income (Subtract line 11 from line 10)	12	1532757
13. Average Percent to Kansas (From Part II)	13	4.00 %
14. Amount to Kansas (Line 13 times line 12)	14	(61310)
15. Nonbusiness income—Kansas (Schedule required)	15	-
16. Kansas net income (Add lines 14 & 15) (Or separate schedule, see instructions)	16	(61310)
17. Adjustments (Schedule required)	17	-
18. Kansas net income before net operating loss deduction (Subtract line 17 from line 16)	18	(61310)
19. Kansas net operating loss deduction (Schedule required) <u>1987 NOL</u>	19	(45696)
20. Kansas Taxable Income (Subtract line 19 from line 18)	20	(107006)
21. Normal tax (4 1/4% of line 20)	21	
22. Surtax (2 1/4% of amount of line 20 in excess of \$25,000)	22	
23. Total tax (Add lines 21 & 22)	23	
24. Economic development credits (Attach schedule K-34, K-53, and K-55)	24	
25. Interest reduction credit (Attach K-51's and K-52)	25	
26. Handicapped accessibility credit (Attach schedule K-37)	26	
27. Total nonrefundable credits (Add lines 24, 25, & 26)	27	
28. Balance (Subtract line 27 from line 23)	28	
29. Estimated tax paid and credits (Attach schedule)	29	
30. Other tax payments (Attach schedule)	30	
31. Total prepaid credits (Add lines 29 & 30)	31	
32. Balance due (If line 28 exceeds line 31)	32	
33. Interest (If applicable)	33	
34. Penalty (If applicable)	34	
35. Underpayment penalty (If applicable) (Attach schedule 220)	35	
36. Total tax, interest, & penalty due (Add lines 32, 33, 34, & 35)	36	
37. Overpayment (If line 28 is less than line 31)	37	
38. Amount of line 37 you wish to be refunded	38	
39. Amount of line 37 you wish to be credited to 1989 estimated tax	39	

I declare under the penalties of perjury that to the best of my knowledge and belief this is a true, correct, and complete return.

Donald R. Kinley Vice President 9/15/89
Lincoln, Nebraska
1040 NBC Center Lincoln, Nebraska 68508-1469
SSN: 506-60-9813 EIN: 13-1939741

MAIL THIS RETURN AND PAYMENT TO: KANSAS INCOME TAX, TOPEKA, KANSAS 66699-0001
ATTACH A COPY OF YOUR FEDERAL RETURN AND SUPPORTING SCHEDULES TO THIS RETURN

TAXPAYER'S COPY

EXHIBIT B: 25

**Letter from Robert F. McCammon Jr.
(CoreStates Financial Corp.)
(December 21, 1989)**

CoreStates Financial Corp
FC 1-23-1
PO Box 7618
Philadelphia PA 19101-7618
215 973 3508

Robert F McCammon Jr
Vice President



CoreStates

December 21, 1989

Mr. Paull Mines
Multistate Tax Commission
444 North Capital Street
N.W. Suite 409
Washington, DC 20001

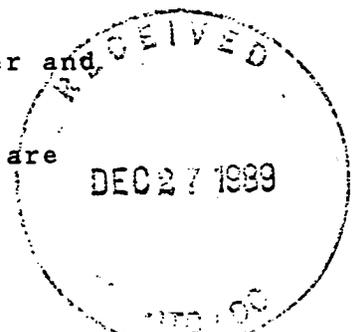
Re: Multistate Tax Commission Proposed
Regulation for Attribution of the
Income of Financial Institutions

Dear Mr. Mines,

CoreStates Financial welcomes the opportunity to respond to the MTC's proposed regulation for the attribution of the income of financial institutions. CoreStates is the 39th ranked, by assets, bank holding company and is incorporated under the laws of Pennsylvania with its principal office in Philadelphia.

We believe the Commission has gone too far in determining what is nexus for financial institutions and is breaking new constitutional grounds. Low nexus standards prescribed by the proposed regulations based on a specified amount of dollars or number of customers within the nondomiciliary state are unreasonable - especially where the financial institution does not otherwise have a physical presence within the state. It has long been the premise under Public 86-272 and judicial interpretations that the mere solicitation of business in a state without having either property or employees permanently located in a state does not constitute "doing business" and consequently nexus is not established. Many financial institutions have borrowers who are located outside the state where their main offices are located and those borrowers are developed in many different ways. Those avenues can be:

- a) Mail solicitation
- b) Telephone solicitation
- c) Borrowers moving from state where loan originated to another state
- d) Participation in syndicated loans
- e) Original loan developed in home state of lender and merger or acquisition activity changing the location of guarantor of the loan.
- f) Brokers, located in customers home state, who are



- not employees of financial institutions, developing loans
- g) Lender sending calling officers to a neighboring state to solicit business but the lender does not establish a permanent office in that state.

In each of the above situations the presence in the state is merely that of the borrowers business domicile.

If the MTC was to adopt the proposed regulations they should likewise consider what type of tax credit should be given in the home state or in the foreign state. When that same income is taxed in more than one jurisdiction, without such tax credit there would be double taxation. We would also suggest that if the home state of the financial institutions does not tax loans from out of state financial institutions that industry group would pressure its legislature to tax out of state bank loans in a similar manner as a retaliatory measure so that they are not at competitive disadvantage. The net result of this is that no one gains and the borrowers will have to incur higher rates in order for the financial institutions to keep their necessary interest margins.

No bank should be subject to tax in a state where it has no physical presence--i.e., brick and mortar and/or employees. Nexus should not be based on unsecured loans--e.g., credit card customers or depositors. In the latter circumstances, merely having one hundred depositors move from your state to a contiguous state which adopted the MTC standard would trigger nexus, yet there would be no tax liability as there would be no numerators under the three-factor formula. A deposit, though valuable to the bank, does not, by itself, earn the bank income. Therefore, states should not measure the nexus to tax a bank when it involves a non-income producing activity. The thresholds are equally unfair when applied to the credit card activity. The proposed threshold of over 100 accounts would produce nexus when on average the total loans outstanding would be less than \$130,000 (100 x \$1300). A more reasonable basis would be to eliminate any criteria on the number of accounts and use loan volume in excess of \$10,000,000 only.

The apportionment method requiring that receipts include income from secured loans if the collateral is in the state should be removed since the financial institution does not either hold title or own any property unless the borrower defaults and the collateral located in the state is taken over. In addition, the borrower being located in one state and the collateral in another should not give rise to receipt allocation in the state where collateral is located.

We would also suggest that by including receipts from securities of the taxing state would force financial institutions outside the state from purchasing those securities and consequently because of lesser competition the rate on those securities would rise in the issuing state.

Finally the cost of administration for both the financial institutions and the taxing jurisdictions to comply and audit these tax returns would in most cases greatly exceed the tax being generated.

We appreciate the opportunity to respond to those regulations and would support a more reasonable and pragmatic approach to nexus and nexus thresholds.

Sincerely,

Robert F. McCammon J

EXHIBIT B: 26

**Letter from Daniel N. Leiter
(Chase Manhattan Bank, N.A.)
(December 21, 1989)**



CHASE

December 21, 1989

Mr. Paul Mines
Multi-State Tax Commission
444 North Capital St. N.W.
Suite 4021
Washington, D.C. 20001

Dear Mr. Mines:

As a member of VISA U.S.A. Inc., I appreciate the opportunity to comment on the proposed MTC regulations on the attribution of the income of financial institutions. Visa member financial institutions play a vital role in making reasonably priced credit and financial services available to consumers across the country. The rules proposed by the MTC will impact the cost and availability of credit nationwide.

The substantial recordkeeping and compliance costs associated with the proposed minimal level of market state activity for subjecting a financial institution to taxation will increase the cost of business. Card issuers' home state will not be willing to reduce tax revenues as the market states impose new and increased tax costs, i.e., resulting from the adoption of these rules. Over-taxation is certain in this situation. Such increased costs, whether passed on to the customer or absorbed by the financial institution, will increase the cost and reduce the availability of credit.

The primary technical problem with the proposed regulation is the minimal economic contact with the market state necessary to subject the out-of-state financial institution to taxation, i.e., 100 resident debtors/creditors or \$5 million in assets. Mercantile and manufacturing companies are not presently subject to taxation based on mere market presence. Accordingly, financial institutions will be unfairly discriminated against versus their mercantile competitors until P.L. 86-272 is repealed or amended.

The proposed minimum nexus requirements are contrary to existing MTC regulation which leave the individual states to determine the level of activity necessary for jurisdiction to tax.

The sourcing rules do not adequately address the economic source of bank earnings or profitability, but are oriented to maximize tax revenues of the market states. No distinction is made in attribution of income between loans directly made or acquired from originating institutions in secondary markets. This failure will affect the free flow of credit.

The factors for attributing income to the market state are duplicative and overly weighted in favor of the market state. Including intangible property in the property factor dilutes the effect of maintaining a physical banking office. Sourcing intangibles the same way as the interest derived therefrom, is essentially duplicative and distorts the receipt factor in favor of the market state.

The technical rules for sourcing receipts from lending transactions essentially distill down to two--the location of the security for loans secured by tangible property and the address to which the statement of account is regularly mailed (presumptively the state of residence) for all other loans. The billing location rule eases the compliance and recordkeeping burden of taxpayers. However, it is totally arbitrary subjecting apportionment of taxable income to the whims of customers, e.g., a customer can choose to have his credit card billed to his home state or office in another state.

The adoption of regulations with such an arbitrary rule of convenience undermines any economic policy of taxation based upon the contribution of the market state versus the home state.

Member states are free to amend the proposed rules by adding, eliminating or increasing the weight accorded the factors, (as was done in Minnesota and Indiana). Thus, over-apportionment and double taxation will certainly result. The proposed regulations do not address the concerns of the states in which financial institutions elect to locate their businesses. Favorable business environment in the home state which encourages the availability of efficient national credit should not be undone by the Multistate Tax Commission and the adoption of arbitrary regulations favoring the market states.

jtvms/p10-12

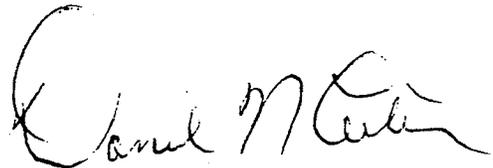


EXHIBIT B: 27

**Letter from Marie Cutillo
(First Financial Savings Bank)
(December 28, 1989)**

FIRST FINANCIAL SAVINGS BANK, S.L.A.
10 WOODBRIDGE CENTER DRIVE
WOODBIDGE, NEW JERSEY 07095
(201) 855-3040

B
H 29



December 28, 1989

Mr. Paull Mines
Multistate Tax Commission
444 North Capitol Street, N.W., Suite 409
Washington, D.C. 20001

Dear Mr. Mines:

We welcome the opportunity to comment on the Proposed Regulation for the Attribution of the Income of Financial Institutions.

First Financial Savings Bank, S.L.A. is a New Jersey savings and loan association with \$80 million in assets. We maintain a physical presence in and remit state taxes to only New Jersey. Our credit card portfolio consists of 31,000 cardholders located throughout the nation.

First Financial has 100 or more cardholders in 32 states, and pursuant to the proposed regulation would be presumed to be taxable in those states. Calculating the Apportionment of Business Income would be more than burdensome. It would require a costly overhaul of our computer systems to enable us to categorize income by state. Furthermore, we would need to employ additional qualified tax personnel to comply with the proposed reporting requirements.

We think the proposed regulation places an unreasonable compliance burden on small financial institutions. This legislation would place us at a severe disadvantage to larger banks with greater resources. Credit card operations for small issuers are marginally profitable at best. If this legislation is adopted as proposed, the additional administrative costs would eliminate our profit margin, forcing us and many other small issuers to withdraw from the credit card business. We suggest that the regulation exempt institutions with less than \$500 million in total assets or less than \$300 million in credit card receivables.

Sincerely,

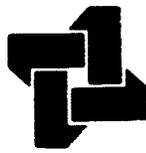
A handwritten signature in cursive script that reads "Marie Cutillo".

Marie Cutillo
Assistant Vice President



EXHIBIT B: 28

**Letter from Stephen R. Cameron
(First National Bank of Louisiana)
(December 29, 1989)**



FIRST NATIONAL BANK
OF LOUISVILLE

Post Office Box 36000 Louisville, Kentucky 40233 Telephone 502-582-1111

December 29, 1989

Mr. Paul Mines
Multistate Tax Commission
Suite 409
444 North Capitol Street, N.W.
Washington, D.C. 20001

Dear Mr. Mines:

The following represents our comments and thoughts on the Proposed Regulations for the Attribution of the Income of Financial Institutions. National City Corporation is a \$22 billion bank holding company that has related companies in states including Ohio, Kentucky, Indiana, and Florida. National City Corporation's subsidiaries offer a wide range of financial services including credit card and retail payment processing, leasing, merchant banking, mortgage banking, trust and investment management, small business investment, venture capital services and perform these services in a significant number of states throughout the country.

First of all, we appreciate the fact that the Multistate Tax Commission (MTC) recognizes the tremendous need to develop a uniform set of rules and regulations for the purpose of taxing financial institutions, who, because of the age of interstate banking, are serving customers all over the United States. As you are aware, the last protection the banks had against state tax expired in 1976. Under the State Taxation of Depositories Act (Public Law 93-100), the application of taxes measured by income or receipts, or other "doing business" taxes, in states other than the states in which depositories had their principal offices was, at that time, deferred until such time as uniform and equitable methods were developed for determining jurisdiction to tax and for dividing the tax base among the states. The Act directed the Advisory Commission on Intergovernmental Relations to make a study of all pertinent matters relating to the application of state "doing business" taxes on out-of-state commercial banks, mutual savings banks, and savings and loan associations. It was subsequently decided that after September 15, 1973, and before September 12, 1976, no state could impose any tax measured by income or receipts or any other "doing business" tax on any insured depository (including national banks) not having its principal office within such state. When this law expired, most states did not tax out-of-state banks doing business in their state as they were not considered a "normal" corporation. Other companies doing interstate business generally fell under

Page 2

Mr. Paul Mines

December 29, 1989

the Uniform Division of Income for Tax Purposes Act (UDITPA), which issued rules governing the allocation and apportionment of income among states. These rules were aimed primarily at manufacturing concerns and other capital intensive companies. Banks did not fall into either one of these categories and so most states were oblivious to out-of-state banks doing business in their home state. Other states chose to tax banks under the standard apportionment factors (property, payroll, and sales), even though financial institutions were specifically excluded from such formula developed under UDITPA.

The majority of states currently have specific laws relating to financial institutions who are located within the confines of that particular state. When the principal taxing laws of a state do not apply to financial institutions, bank shares tax and ad valorem taxes upon assets, capital, or capital stock are common. In many instances, states do not allow the tax base to be apportioned, because banks have traditionally operated within the borders of their home state. Due to many recent acquisitions and out-of-state operations such as loan production offices, credit cards, mortgage banking, and leasing, many of these state tax laws pertaining to financial institutions are outdated and obsolete.

Since 1966, nineteen states have become members of the Multistate Tax Compact (MTCMPT) and ten have become associate members. The MTCMPT adopts UDITPA as an optional method of apportionment in member states. It is interesting that the states which have not adopted UDITPA have similar and/or some identical provisions for rules concerning apportionment, which indicates that these non-MTCMPT states feel that these rules are fair to both the taxpayer and the state. If this is any indication of things to come, then the financial institutions, which are not happy with the proposed regulations, need to get the rules changed to their satisfaction. Otherwise, states that do not want to establish their own regulations may decide to implement these regulations until the state can come up with their own rules.

Below, we are listing some of our comments which we have concerning the regulations:

1. Sourcing of Interest Income - In the discussion of the receipts factor, interest income would be sourced primarily by real estate or personal property securing the asset. In the event that the property is located in two or more states, it shall be deemed to be located in the state having the greatest property value. We anticipate that problems would occur when the secured property is in two or more states and one or more of the states have not adopted the MTC regulations. Taxpayers will end up in court with several states all trying to have the income apportioned to their state.

Page 3
Mr. Paul Mines
December 29, 1989

2. Merchant Discount and Other Income - Our banks issue credit cards to a substantial cardholder base. These cardholders may use their credit cards at any number of merchants located anywhere in the United States or wherever the card is accepted. When a cardholder charges merchandise with a merchant, a fee is earned on the transaction, however, our banks have no way of capturing the location of each sale by state. Trying to obtain this information by state location would be a tremendous administrative burden on all parties involved. We feel this and other fees should be sourced where the service is performed.

3. Increased Compliance Costs - The proposed regulations, as they are now, seem to place compliance burdens that are now unmatched on corporate tax departments. Tax personnel will now need to be involved in trying to source the different types of income prescribed by the regulations, and then determine apportionment factors for those states adopting the MTC regulations; for those states not adopting the MTC regulations; and those states which have composed their own regulations (Minnesota, Illinois, and Indiana). Generally, regional banks are most likely to be doing business in 25 to 30 states due to such activities as leasing, mortgage loans, credit card loans, and commercial loans. The tax liabilities in most of these states would have to be de minimus, except for those states that are contiguous to the home state. Tax department staffs would need to be increased as a result of the additional compliance requirements, especially in multi-bank holding company groups. These tax departments may be filing hundreds of returns for their banks with little or no liability. In our opinion, the nexus standards need to be increased so that this will not occur.

4. Credit for Income Tax Paid to Other States - As there will undoubtedly be forms of double taxation should the proposed regulations not be adopted by all states, we propose that there be some relief incorporated into the rules to prevent this. Kentucky domiciled banks pay a Fair Cash Value Shares Tax (FCVS) based on a five-year average of financial statement earnings and net worth of the bank. This tax is deemed an intangible tax and is in lieu of all other types of tax, including income tax. Kentucky does not allow any apportionment of the tax base outside of the state, and since our primary Kentucky bank, First National Bank of Louisville, has leasing operations alone in over 30 states, tax will be paid on more than 100% of the tax base. Not only is First National Bank of Louisville paying the high FCVS tax to Kentucky, it is paying additional state taxes on its out-of-state operations that should be excluded from its home state base. To add insult to injury, Kentucky is treating out-of-state financial institutions under the income tax rules and requiring these banks to report income based on the three factor apportionment factor. As you know, Kentucky is not the only state who does not allow apportionment to a domestic financial institution. Thus, this form of double taxation in Kentucky and other states should be addressed by requiring apportionment or allowing credits against other state taxes.

Page 4
Mr. Paul Mines
December 29, 1989

It is paramount that the financial institutions of the United States be fairly satisfied with the regulations in final form, as these rules will in most probability be around for a number of years to come. This can be seen by the acceptance of the UDITPA rules as previously mentioned. From all indications that we have received, financial institutions are not happy with the regulations as they are now. We want to stress that it is very important that the MTC consider very carefully the suggestions and comments that the banks and their industry associations are submitting, because the banking community is concerned that this system of taxation be equitable to all parties involved.

If you would like any clarification to any of the comments or suggestions we have mentioned, please feel free to contact us.

Sincerely,



Stephen R. Cameron
Senior Accounting Officer
First National Bank of Louisville
Affiliate of National City Corporation

SRC/17-109

EXHIBIT B: 29

**Letter from Gary S. Austin
(National City Corporation)
(December 29, 1989)**

December 29, 1989



NCC
NATIONAL CITY
CORPORATION

National City Center
Post Office Box 5756
Cleveland, OH 44101-0756
Phone 216/575-2000

Mr. Paul Mines
Multistate Tax Commission
444 North Capitol Street, N.W.
Suite 409
Washington, D.C. 20001

Dear Mr. Mines:

National City Corporation is a \$22 billion bank holding company that has related companies in states including Ohio, Kentucky, Indiana, and Florida. National City Corporation's subsidiaries offer a wide range of financial services including credit card and retail payment processing, leasing, merchant banking, mortgage banking, trust and investment management services. It performs these services for customers that reside in a number of states throughout the country.

National City wishes to thank the Multistate Tax Commission (MTC) for allowing it to respond to the proposed regulations. The following suggested changes would alleviate some of our concerns relating to the proposed regulations;

1. Sourcing of Interest Income - In the receipts factor, interest income would be sourced primarily by real estate or personal property securing the asset. In the event that the property is located in two or more states, it shall be deemed to be located in the state having the greatest property value. We anticipate that problems would occur when the secured property is in two or more states and in determining "property value." It is suggested that the state of residence of the financial institution be deemed the source when the property securing the assets is located in more than two states.
2. Merchant Discount and Other Income Sourcing - Credit cardholders may use their credit cards with merchants located anywhere in the United States without any control by a financial institution. When a cardholder charges merchandise, a fee is earned on the transaction by the merchant. Our banks currently have no way of capturing the location of each sale. Obtaining this information by state location would be a tremendous administrative burden on all parties involved. We feel all such fees should be sourced where the service is performed.
3. Increased Compliance Costs - The proposed regulations place substantial

compliance burdens on corporate tax departments. Tax personnel will need to be involved in sourcing the various types of income prescribed by the regulations and determining apportionment factors for those states adopting the MTC regulations, for those states not adopting all of the MTC regulations, and those states which have composed their own regulations (i.e. Minnesota and Indiana). Regional banks most likely are "doing business" in many states due to such activities as leasing, mortgage loans, credit card loans, and commercial loans. The tax liabilities in most of these states may be de minimis, except possibly for those states that are contiguous to the home state. Tax departments may be required to file hundreds of returns for their banks with little or no liability. A larger de minimis standard should be adopted. The cost of compliance could be more than the tax collected.

4. Credit for Income Tax Paid to Other States - There will be some double taxation, if the proposed regulations are not adopted by all states. Kentucky domiciled banks pay a Fair Cash Value Shares Tax (FCVS) based on a five-year average of financial statement earnings and net worth of the bank. Kentucky does not allow any apportionment of the tax base outside of the state. Any Kentucky bank that has out of state operations, will pay taxes on more than 100% of its income. Kentucky is not the only state that does not allow apportionment. There should be some relief incorporated into the rules to prevent this type of double taxation.

We hope that the MTC considers carefully the suggestions and comments the banks and various industry associations are submitting to ensure that the system of taxation is equitable to all parties involved.

Very truly yours,



Gary S. Austin
Vice President & Controller

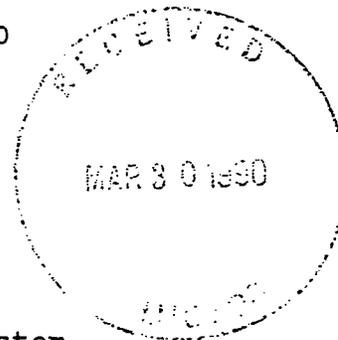
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EXHIBIT B: 30

**Letter from Philip M. Plant
(Bank of America)
(March 27, 1990)**

PHILIP M. PLANT
Vice President and
Assistant General Tax Counsel

March 27, 1990



Gerald H. Goldberg
Executive Officer
State of California
Franchise Tax Board
Sacramento, CA 95867

Re: MTC Consideration of Dual State Tax System

Dear Mr. Goldberg:

I am writing to urge that the Multistate Tax Commission (MTC) consider the merits of the so-called dual state tax system of bank taxation impliedly endorsed by the Advisory Commission on Intergovernmental Relations (ACIR) in its December 1989 information report entitled "State Taxation of Banks: Issues and Options". Should the MTC find this dual tax system unsatisfactory and declare it to be such in an appropriate resolution, it would materially assist in avoiding the spread of incompatible state taxation of banks. As California is Bank of America's home state, and as the California Franchise Tax Board is an active MTC member, I am expressing these concerns to you.

The dual tax system combines residence-based taxation of domiciliary banks with sourced-based taxation of nondomiciliary banks. The residence-based tax system imposes a tax on the entire net income of domiciliary banks regardless of source but allows an offsetting credit for taxes paid in other states. The creditable tax is measured by the lesser of income sourced to the nondomiciliary date ^{state} under its own laws or income that would be sourced to the nondomiciliary state under the home state laws. The creditable rate of tax will be the lesser of the rate actually imposed by the nondomiciliary state or the home state rate of tax.

The sourced-based tax system only taxes local net income; it divides up the tax base of the multistate bank among all the states in which it does business. Formula apportionment is almost exclusively used to divide income for this purpose. Under the dual tax system, the source-based tax approach is only used to determine the local income of nondomiciliary banks. Under virtually all of the state tax systems currently in effect, the formula

apportionment source-based approach is used to tax both domiciliary and nondomiciliary banks.

While the MTC has not yet finally promulgated its proposed regulations for the attribution of income of financial institutions, it has received extensive comment on several drafts and has consistently retained a formula apportionment source-based tax approach. As touched upon above, the formula apportionment sourced-based approach conflicts conceptually with the dual tax system approach. It is apparent that the MTC has not seriously considered the dual tax system as an alternative. I am confident that the MTC would reject this alternative when and if it reflected on the complexity and inequity arising from its application.

An MTC position on the viability of the dual tax system is urgently needed at the earliest opportunity to avoid the spread of inconsistent state tax systems. As you know, many states are presently considering new systems of taxation of nondomiciliary banks. The formula apportionment source-based approach identified in the MTC proposed regulations is an alternative available to them and has been adopted in Minnesota. Unfortunately, the dual tax system is also offered to them through the implicit endorsement of the ACIR information report. Indeed, the dual tax system may be more attractive because it is said to generate greater tax revenues in market states than the MTC approach. Indiana has accordingly adopted the dual tax system and Tennessee has considered it at one point in pending tax proposals. Unless the MTC questions the efficacy of the dual tax system, the state legislatures will remain unaware that the formula apportionment source-based approach is by far the superior alternative.

The ACIR information report encourages adoption of the dual tax system. While stating that it is not yet possible to describe the "best" bank tax, the report goes on to reflect a strong bias in favor of the dual tax system which it asserts has only two disadvantages: (1) it is different from the currently prevalent sourced-base formula apportionment approach and (2) it would close "tax loopholes" and thus trigger resistance from multistate banks. Obviously, these "disadvantages" are a thinly disguised enticement for states to adopt this approach. I believe that any fair-minded individual would want to reflect further on the potential difficulties associated with the dual tax system such as extreme complexity, increased tax overlap exposure and disparate taxation of banks domiciled in high tax rate and low tax rate jurisdictions. These defects were addressed in virtually all the comments submitted on the first draft of this information report. They are particularly well described

in the comments of Michael E. Brownell submitted on behalf of your Franchise Tax Board. (See attached). Despite such comment, these problems were ignored by the principal author Sandra B. McCray in her final version of the report which was approved without apparent substantive review by Executive Director John Kincaid.

An MTC resolution candidly recognizing the potential pitfalls of the dual tax system is needed right away and should not await the more gradual progression leading to the release of the final regulations. If the MTC waits until the summer of 1991, when the final regulations are expected to be promulgated, other states may have already seized upon the dual tax system because they were not cautioned against so doing by a respected representative of state tax administrators such as the MTC.

The MTC has an excellent opportunity to further its objective of promoting uniformity in state taxing laws by questioning the ACIR endorsement of the dual tax system and cautioning market states against adopting a dual tax system rather than a formula apportionment sourced-based approach.

Needless to say, my preference for the formula apportionment sourced-based approach over the dual tax system is not intended as a recognition that either of these minimum nexus/destination sourcing systems is desirable or constitutionally valid. The dual tax system is, however, clearly more complex and unfair.

Thank you for this opportunity to comment. Please let me know if you wish to discuss this matter further.

Sincerely,


Philip M. Plant
Vice President &
Asst. General Tax Counsel
(415) 622-2877

cc: Dan R. Bucks
Executive Director
Multistate Tax Commission
444 North Capital Street, NW, Suite 500
Washington, D.C. 20001

Eric Coffil
Franchise Tax Board
9645 Butterfield Way
Sacramento, CA 95827

pmp2:062:cnc

EXHIBIT C:

**RESOLUTIONS OF MULTISTATE TAX COMMISSION
EXECUTIVE COMMITTEE**

EXHIBIT C: 1

Resolution dated May 10, 1990

Multistate Tax Commission



RESOLUTION OF THE EXECUTIVE COMMITTEE OF THE MULTISTATE TAX
COMMISSION REGARDING THE HOLDING OF A PUBLIC HEARING UPON
PROPOSED M.T.C. REGULATION ART.IV.18.(i)

**Attribution of Income from the Business of a Financial
Institution**

WHEREAS, the Multistate Tax Commission (hereafter "Commission") possesses the authority pursuant to Article VII. of the Multistate Tax Compact (hereafter "Compact") to develop and recommend proposals for the purpose of increasing uniformity in the administration of state and local taxes; and

WHEREAS, the Uniformity Committee of the Commission has met on several occasions to study, develop and propose a uniform method for the attribution of net income derived from the business of a financial institution that operates on a multistate basis; and

WHEREAS, the Uniformity Committee has recommended to the Executive Committee that a public hearing be held upon the proposed regulation Art.IV.18.(i) attached hereto; and

WHEREAS, the Executive Committee determines that is in the interest of state taxpayers and state tax administrators alike that the states determine the most appropriate and administratively feasible method for uniformly applying their tax laws to the multistate business that is carried on by financial institutions; and

WHEREAS, it is in the public interest that a public hearing be held upon said proposed regulation in order to receive public comments thereon.

NOW, THEREFORE, BE IT RESOLVED THAT a public hearing upon said proposed Regulation Art.IV.18(i) be held at a convenient location to the interested public on such date as determined by the Hearing Officer pursuant to the provisions contained in Article VII. of the Compact; and

BE IT FURTHER RESOLVED THAT Alan H. Friedman, General Counsel to the Commission is hereby appointed to act as Hearing Officer for said public hearing; and that he is directed to submit his report

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Suite 409
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Telephone (202) 624-8699

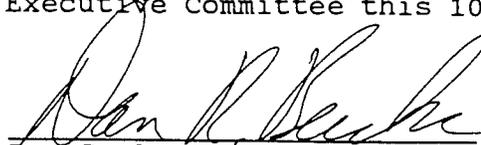
New York Audit Office:
25 W. 43rd Street, Suite 212
New York, NY 10036
Telephone (212) 575-1820

Chicago Audit Office:
221 N. LaSalle Street, Suite 1906
Chicago, IL 60601
Telephone (312) 263-3232

Houston Audit Office:
15835 Park Ten Place, Suite 104
Houston, TX 77084
Telephone (713) 492-2260

and recommendations to the Commission within a reasonable period of time following the completion of said public hearing and in advance of the Commission's Annual Meeting to be held in 1991.

Adopted by the Executive Committee this 10th day of May, 1990.



Dan Bucks
Executive Director

Multistate Tax Commission



MULTISTATE TAX COMMISSION PROPOSED REGULATION ATTRIBUTING INCOME FROM THE BUSINESS OF A FINANCIAL INSTITUTION

Reg. IV.18.(i). Special Rules: Financial Institutions.

The following special rules are established with respect to the attribution of income derived from the business of a financial institution.

(A) **Application of Regulation.** This regulation shall apply to attribute the income derived from the business of a financial institution to only those states in which the taxpayer either exercises its corporate franchise or transacts business as defined hereunder. Except as may be specifically limited by this regulation, it is the intention of this regulation to subject to taxation all of the income of a financial institution that is within the constitutional power of this state to tax.

(B) **Definitions and General Provisions.** Except as specifically defined herein, all terms used in this regulation shall have the same meaning as such terms have under [here include your State citation to the Multistate Tax Compact or other applicable state law] and the rules and regulations promulgated thereunder.

- (1) "Borrower" means the individual or entity who is primarily liable on a debt instrument. If more than one individual or entity is primarily liable on a debt instrument, each such individual or entity shall be considered the borrower to the extent of its interest in the debt instrument. For purposes of this regulation, a partnership shall be treated as a separate entity.
- (2) "Business of a Financial Institution" includes the business activities, including finance leasing, that:
 - (a) a regulated financial corporation may be authorized to do under state or federal law or the business that its subsidiary is authorized to do by the proper regulatory authorities;
 - (b) any corporation organized under the authority of

the United States or organized under the laws of this state or any other state or country does, or has authority to do, which is substantially similar to the business which a corporation may be created to do under [insert citations of state's laws governing the creation of banks and trust companies, industrial banks, savings and loan associations, credit unions, etc.] or any business which a corporation or its subsidiary is authorized to do by said laws; or

- (c) any corporation organized under the authority of the United States or organized under the laws of this state or any other state or country does or has authority to do if such corporation derives more than fifty percent of its gross income from lending activities (including the discounting of obligations) in substantial competition with the businesses described in subsections (a) and (b) above. For purposes of this subsection, the computation of the gross income of a corporation shall not include income from nonrecurring, extraordinary items.

(3) "Deposit" means:

- (a) the unpaid balance of money or its equivalent received or held by a financial institution in the usual course of business and for which it has given or is obligated to give credit, either conditionally or unconditionally, to a commercial, checking, savings, time, or thrift account whether or not advance notice is required to withdraw the credited funds, or which is evidenced by its certificate of deposit, thrift certificate, investment certificate, or certificate of indebtedness, or other similar name, or a check or draft drawn against a deposit account and certified by the financial institution, or a letter of credit or a traveler's check on which the financial institution is primarily liable; provided, that, without limiting the generality of the term "money or its equivalent," any such account or instrument must be regarded as evidencing the receipt of the equivalent of money when credited or issued in exchange for checks or drafts or for a promissory note upon which the person obtaining any such credit or instrument is primarily or secondarily liable or for a charge against a deposit account or in settlement of checks, drafts, or other instruments forwarded to such bank for collection;

- (b) trust funds received or held by such financial institution, whether held in the trust department or held or deposited in any other department of such financial institution;
 - (c) money received or held by a financial institution, or the credit given for money or its equivalent received or held by a financial institution in the usual course of business for a special or specific purpose, regardless of the legal relationship thereby established, including, without being limited to, escrow funds, funds held as security for an obligation due the financial institution or others (including funds held as dealers reserves) or for securities loaned by the financial institution, funds deposited by a debtor to meet maturing obligations, funds deposited as advance payment on subscriptions to United States Government securities, funds held for distribution or purchase of securities, funds held to meet its acceptances or letters of credit, and withheld taxes; provided that there shall not be included funds which are received by the financial institution for immediate application to the reduction of an indebtedness to the receiving financial institution, or under condition that the receipt thereof immediately reduces or extinguishes such an indebtedness;
 - (d) outstanding drafts (including advice or authorization to charge a financial institution's balance in another such institution), cashier's checks, money orders, or other officer's checks issued in the usual course of business for any purpose, but not including those issued in payment for services, dividends, or purchases or other costs or expenses of the financial institution itself;
 - (e) money or its equivalent held as a credit balance by a financial institution on behalf of its customer if such entity is engaged in soliciting and holding such balances in the regular course of its business.
- (4) "Deposit Related Fees." For purposes of the receipts factor, deposit related fees include all fees associated with the administration of deposit accounts.
 - (5) "Exercising a Corporate Franchise or Transacting Business in a State." Except as may be specifically provided for in this regulation, a financial institution is exercising

a corporate franchise or transacting business in this state if it:

- (a) owns, leases or otherwise has an interest in any real or tangible personal property located in this state or maintains an office or other place of business in this state;
- (b) makes any direct loan secured by any real or tangible personal property located in this state;
- (c) has an employee, representative or independent contractor conducting business activities in its behalf in this state; or,
- (d) engages in regular solicitation in this state (whether at a place of business, by travelling loan officer or other representative, by mail, by telephone or other electronic means), and the solicitation results in the creation of a depository or direct debtor/creditor relationship with a resident of this state. For purposes of this subsection, mere processing or transfer through financial intermediaries of checks, credit card receivables, commercial paper and the like does not create a debtor/creditor relationship.

A financial institution is presumed, subject to rebuttal, to be engaged in regular solicitation within this state if, during the tax period, it:

(i) has entered into direct debtor/creditor relationships with one hundred (100) or more residents of this state; or

(ii) has an average during the tax period of ten million dollars (\$10,000,000) or more of assets and deposits attributable to sources within this state; or

(iii) has in excess of five hundred thousand dollars (\$500,000) in receipts attributable to sources within this states.

(e) Notwithstanding any other provision contained in this subsection to the contrary, a financial institution is not considered to be either exercising a corporate franchise or transacting business in this state if its sole and exclusive activities in this state are limited to evaluating, acquiring, maintaining and/or disposing of any of the following property, including any security or collateral relating to such property:

(i) any participation or syndicated loans;

(ii) a real estate mortgage investment conduit, a real estate investment trust, or a regulated investment company as those terms are defined by the Internal Revenue Code of 1986, as amended;

(iii) money market instruments or securities;

(iv) loan-backed, mortgage-backed, or receivable-backed security representing either: ownership in a pool of promissory notes, mortgages, or receivables or certificates of interest or participation in such notes, mortgages, or receivables, or debt obligations or equity interests which provide for payments in relation to payments or reasonable projections of payments on notes, mortgages, or receivables;

(v) any interest in a loan or other asset or property attributed to this state under subsection (D)(2)(a) through (h) and in which the payment obligations were solicited and entered into by an independent person not acting on behalf of the taxpayer;

(vi) any interest in the right to service or collect any income from any loan, asset or other property attributed to this state under subsection (D)(2)(a) through (h) and in which the payment obligations were solicited and entered into by an independent person not acting on behalf of the taxpayer;

(vii) a funded or unfunded agreement to extend or guarantee credit, whether conditional, mandatory, temporary, standby, secured or otherwise;

(viii) an interest of a person other than an individual, estate, or trust, in any intangible, real, or tangible personal property acquired in satisfaction, whether in whole or in part, of any asset embodying a payment obligation which is in default, whether secured or unsecured, provided the property is disposed of within a reasonable period of time.; or

(ix) property or funds held in an escrow or trust account that is maintained in connection with the property described in this subsection (B)(5)(e).

(6) "Finance leasing": [reserved]

- (7) "Financial Institution" includes the following:
- (a) A holding company.
 - (b) Any regulated financial corporation.
 - (c) Any other corporation organized under the laws of the United States or organized under the laws of this state or any other state or country which is carrying on the business of a financial institution.
- (8) "Holding Company" means any corporation subject to [insert citation of the state law governing the creation of bank holding companies] or registered under the Federal Bank Holding Company Act of 1956, as amended, or registered as a savings and loan holding company under the Federal National Housing Act, as amended.
- (9) "Independent person not acting on behalf of the taxpayer" means, for purposes of subsections (A)(5)(e)(v) and (vi) as follows:
- (a) At the time of the acquisition of the asset, loan or property, the taxpayer must not directly or indirectly own fifteen percent (15%) or more of the outstanding stock or, in the case of a partnership, fifteen percent (15%) or more of the capital or profits interest, of the entity from which the taxpayer originally acquired the asset, loan or property. In determining indirect ownership, the taxpayer is deemed to own all of the stock, capital interest, or profits interest owned by another person if the taxpayer directly owns fifteen percent (15%) or more of the stock, capital interest, or profits interest in that other person. In addition, the taxpayer is deemed to own all stock, capital interest, and profits interest directly owned by any intermediary parties in the transaction, to the extent a fifteen percent (15%) or more chain of ownership of stock, capital interest, or profits interest exists between the taxpayer and any intermediary party;
 - (b) the entity from which the taxpayer acquired the asset, loan or property must regularly sell, assign, or otherwise transfer interest in such assets, loans or property to three (3) or more persons during the full twelve (12) month period immediately preceding the month of acquisition; and
 - (c) the entity from which the taxpayer acquired the

asset, loan or property must not sell, assign or otherwise transfer ninety percent (90%) or more of its exempt assets, loans or property to the taxpayer during the full twelve (12) month period immediately preceding the month of acquisition.

- (10) "Loan Related Fees." For purposes of the receipts factor, loan related fees include all fees associated with the generation and administration of loans, including loan servicing fees.
- (11) "Loan Servicing Fees." For purposes of the receipts factor, loan servicing fees include fees charged by a financial institution that sells, assigns or otherwise transfers loans to a purchasing financial institution in instances in which the transferring financial institution continues to process the loan payments.
- (12) "Money Market Instruments" mean Federal funds sold and securities purchased under agreements to resell, commercial paper, banker's acceptances, and purchased certificates of deposit and similar instruments to the extent that such instruments are reflected as assets under generally accepted accounting principles.
- (13) "Participation Loan" means an arrangement in which a financial institution makes a loan to a borrower and thereafter sells, assigns or otherwise transfers all or a portion of the loan to a purchasing financial institution.
- (14) "Presumption." A presumption subject to rebuttal, as provided in this regulation, shall be rebuttable by clear and convincing proof established by [the party seeking to oppose the application of the presumption.][either the financial institution or [here include title of your State taxing agency]].
- (15) "Property Located in this State".
 - (a) Tangible Property: General Rule. -- Except as otherwise provided in this section, real and tangible personal property which is security for a loan or property subject to a lease shall be considered to be located in the state in which such property is physically situated. It shall be presumed, subject to rebuttal, that the property is physically situated in the same state as the billing address of the borrower or lessee.
 - (b) Moveable tangible property. -- Tangible personal property which is characteristically moving

property, such as motor vehicles, rolling stock, aircraft, vessels, mobile equipment, and the like shall be considered to be located in a state if:

- (i) the operation of the property is entirely within the state; or
- (ii) the operation of the property is in two or more states, but the principal base of operations from which the property is sent out is in the state.

It shall be presumed, subject to rebuttal, that the location of operation of the property and the principal base of operations from which the property is sent out shall be in the same state as the billing address of the borrower or lessee.

- (16) "Receipts" for the purpose of the receipts factor means gross income, including net taxable gain on disposition of assets (including securities, loans, personal and real property and money market transactions) when derived from transactions and activities in the regular course of the taxpayer's trade or business.
- (17) "Regulated Financial Corporation" means any institution the deposits or accounts of which are insured under the Federal Deposit Insurance Act or by the Federal Savings and Loan Insurance Corporation; any institution which is a member of a Federal Home Loan Bank; any other bank or thrift institution incorporated or organized under the laws of the United States or any State which is engaged in the business of receiving deposits or which holds a bank charter, any corporation organized under the provision of 12 U.S.C. 611 to 631 (Edge Act Corporations); any credit union incorporated or organized under the laws of any State; and any agency, branch or subsidiary of a foreign depository as defined in 12 U.S.C. 3101.

It is presumed, subject to rebuttal, that any subsidiary and any holding company of a regulated financial corporation shall be a financial institution for the purpose of this regulation.

- (18) "Resides/Residence/Resident." A person shall be considered to reside or make his or her residence in or be a resident of a state if, in the case of an individual, he/she resides there for 183 or more days of the relevant tax period. For purposes of this regulation, corporations and partnerships shall be treated as residents of their states of commercial

domicile. An individual, a partnership or a corporation shall be presumed, subject to rebuttal, to reside at (i.e., be a resident of, make his residence at) the address to which the statement of account is regularly mailed.

- (19) "Securities" means United States Treasury securities, obligations of United States Government agencies and corporations, obligations of State and their political subdivisions, corporate stock and other corporate securities, participations in securities backed by mortgages held by United States or State government agencies, loan-backed securities and similar investments to the extent that such investments are reflected as assets under generally accepted accounting principles.
- (20) "State" means a state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, or any territory or possession of the United States or any foreign country.
- (21) "Subsidiary" means a corporation whose voting stock is more than 50% owned, directly or indirectly, by a financial institution.
- (22) "Syndication Loan" means a multi-financial institution loan transaction in which all of the lenders are named as parties to the loan and have privity of contract with the borrower.
- (23) "Taxable" and "Taxable in another State." For the purpose of the receipts factor, a taxpayer is taxable in another state if: (a) in that state, he is subject to a franchise tax measured by net income, a net income tax, a franchise tax for the privilege of doing business, or a corporate stock tax, or (b) that State has jurisdiction to subject the taxpayer to such a tax regardless of whether, in fact, the State does or does not.
- (24) "Taxpayer" means a financial institution which is subject to taxation in a state because it is exercising its corporate franchise or is transacting business in a corporate or organized capacity in the state and has gross income attributable under this regulation to sources within this state.

(C) **Business Income.** All income (taxable under the laws of this State) which arises from the business of a financial institution shall be deemed derived from transactions in the regular course of the taxpayer's business and subject to apportionment under this regulation. All such income which arises

from activities of a financial institution which are not the business of a financial institution as defined in this rule shall be apportioned or allocated in accordance with the rules set forth in [here include your State citation to UDITPA or the Multistate Tax Compact].

(D) **Apportionment of Business Income.**

(1) **General Method.**

(a) If a financial institution is carrying on the business of a financial institution both within and without this state and if, by reason of such business activity, it is taxable in another state, the portion of the net income (or net loss) arising from such business which is derived from sources within this state shall be determined by apportionment in accordance with this regulation.

(b) The tax applicable to financial institutions whose net income (or net loss) is apportionable according to the rules in this section shall be determined by multiplying the tax base by a fraction the numerator of which is the sum of the receipts factor, the property factor, and the payroll factor as defined in this regulation and the denominator of which is three. If any factor(s) is missing, the remaining factors are added together and the sum is divided by the number of remaining factors. A factor is missing if both its numerator and denominator are zero, but it is not missing merely because its numerator is zero.

(2) **Receipts Factor.** In general. -- The receipts factor is a fraction the numerator of which is the receipts of the taxpayer within this state during the tax period and the denominator of which is the total receipts of the taxpayer wherever earned during said tax period. The numerator of the receipts factor shall include, in addition to items otherwise assignable under [here include your State citation to the Multistate Tax Compact or other applicable state law]:

(a) Receipts from the lease or rental of real or tangible personal property (including both finance leases and true leases) if the property is located in this state.

(b) Interest income and other receipts from assets in the nature of loans which are secured primarily by real estate or tangible personal property if such security property is located in this state. In the

event that such security property is located in two or more states, it shall be deemed to be located in the state having the greatest property values.

- (c) Interest income and other receipts from consumer loans not secured by real or tangible personal property that are made to residents of this state (whether at a place of business, by travelling loan officer, by mail, by telephone or other electronic means or otherwise).
- (d) Interest income and other receipts from commercial loans and installment obligations not secured by real or tangible personal property if and to the extent that the borrower or debtor is a resident of this State.
- (e) Interest income and other receipts from a financial institution's portion of loans, including syndication and participation loans, under the rules set forth in subsections (a) through (d) above.
- (f) Interest income and other receipts, including service charges, from financial institution credit card and travel and entertainment credit card receivables and credit card holders' fees to the extent that the borrower or debtor is a resident of this State.
- (g) Merchant discount income derived from financial institution credit card holder transactions with a merchant located in this state. In the case of merchants located within and without this state, only receipts from merchant discounts attributable to sales made from locations within this state shall be attributed to this State. It shall be presumed, subject to rebuttal, that the location of a merchant is the address shown on the invoice submitted by the merchant to the taxpayer.
- (h) Receipts from the performance of services are attributed to this state if:
 - (i) the service receipts are loan related fees, including loan servicing fees, and the borrower resides in this state; except that, at the taxpayer's election, receipts from loan related fees which are either (a) "pooled" or aggregated for collective financial accounting treatment or (b) manually written as non-recurring extraordinary charges to be

processed directly to the general ledger may either be attributed to a state based upon the borrowers' residences or upon the ratio that total interest sourced to that state bears to total interest from all sources;

- (ii) the service receipts are deposit related fees and the depositor resides in this state, except that, at the taxpayer's election, receipts from deposit related fees which are either (a) "pooled" or aggregated for collective financial accounting treatment or (b) manually written as non-recurring extraordinary changes to be processed directly to the general ledger may either be attributed to a state based upon the depositors' residences or upon the ratio that total deposits sourced to that state bear to total deposits from all sources;
 - (iii) the service receipt is a brokerage fee and the account holder is a resident of this state;
 - (iv) the service receipts are fees related to estate or trust services and the decedent for whom the estate relates was a resident of this state immediately before death; or the grantor who either funded or established the trust is a resident of this state; or,
 - (v) the service receipt is associated with the performance of any other service not identified above and the service is performed in this state; or if performed both in and outside this state and a greater proportion of the service is performed in this State than in any other State, as determined on the basis of the cost of performance.
- (i) Receipts from the issuance of travelers checks and money orders if such checks and money orders are purchased in this state.
 - (j) Receipts from investments of a financial institution in securities and from money market instruments, based upon the ratio that total deposits from this state, its residents, its political subdivisions, agencies and instrumentalities bear to the total deposits from all states, their residents, their political subdivisions, agencies and instrumentalities. For purposes of this subsection, deposits made by this

State, its residents, its political subdivisions, agencies and instrumentalities shall be attributed to this state regardless of whether or not such deposits are accepted or maintained by the taxpayer at locations within this state.

In the case of an unregulated financial institution subject to this regulation, such receipts shall be apportioned to this state based upon the ratio that its gross business income earned from sources within this state bears to the gross business income earned within all States.

- (k) All receipts allocated by this rule to a state in which the taxpayer is not taxable shall be attributed pursuant to the laws of the state of the taxpayer's commercial domicile.
- (3) Property Factor. In general. -- The property factor is a fraction the numerator of which is the average value of the taxpayer's real and tangible personal property owned or rented and used in, and intangible property attributed to this state during the tax period and the denominator of which is the average value of all of the taxpayer's real and tangible personal property owned or rented and used in, and intangible property attributed to all states during the tax period.

For purposes of this regulation, the value of property owned by the taxpayer shall be its original cost; the value of real or tangible personal property rented by the taxpayer shall be eight times its net annual rental rate. The net annual rental rate for any item of rented property is the annual rate paid by the taxpayer for such property less the aggregate annual subrental rates paid by subtenants of the taxpayer. Goodwill shall not be included in the property factor.

The numerator of the property factor shall include, in addition to items otherwise assignable under [here include your State citation to the Multistate Tax Compact or other applicable state law], the following:

- (a) Coin and currency located in this state.
- (b) Lease financing receivables if and to the extent that the property is located within this state.
- (c) Assets in the nature of loans which are secured by real or tangible personal property if and to the extent that the security property is located within this state. In the event that such security

property is located in two or more states, it shall be deemed to be located in the state having the greatest property values.

- (d) Assets in the nature of consumer loans and installment obligations which are unsecured or secured by intangible property, if the loan was made to a resident of this state.
- (e) Assets in the nature of commercial loans and installment obligations which are unsecured or secured by intangible property, if the borrower is a resident of this state.
- (f) Funds deposited by this state, its agencies, instrumentalities, political subdivisions and residents shall be attributed to this state regardless of whether or not such deposits are accepted or maintained by the taxpayer at locations within this state.
- (g) A financial institution's portion of a participation or syndication loans, under the rules set forth in subsections (b) through (e) above.
- (h) A financial institution's credit card and travel and entertainment credit card receivables to the extent that the borrower or debtor is a resident of this State.
- (i) Assets in the nature of securities and money market instruments, based upon the ratio that total deposits from this State, its agencies, instrumentalities, political subdivisions and residents bear to the total deposits from all States, their residents, their political subdivisions, agencies and instrumentalities.

In the case of an unregulated financial institution subject to this regulation, such assets shall be apportioned to this state based upon the ratio that its gross business income earned from sources within this state bears to the gross business income earned within all States.

All intangible property located by this rule in a state in which the taxpayer is not taxable shall be attributed pursuant to the laws of the state of the taxpayer's commercial domicile.

- (4) Payroll Factor. In general. -- The payroll factor is a fraction the numerator of which is the total amount paid

by the taxpayer for compensation during the year, and the denominator of which is the total amount of compensation paid in every state.

(E) **Special Rules.** If the allocation and apportionment provisions of this regulation do not fairly represent the extent of the taxpayer's activity in this state, the taxpayer may petition for or the tax administrator may require, in respect to all or any part of the taxpayer's business activity, if reasonable:

- (1) Separate accounting;
- (2) The exclusion of any one or more of the factors;
- (3) The inclusion of one or more additional factors which will fairly represent the taxpayer's business activity in this state; or
- (4) The employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

Finreg:5/9/90\ahf

EXHIBIT C: 2

Resolution dated November 9, 1990

Multistate Tax Commission



RESOLUTION OF THE EXECUTIVE COMMITTEE OF THE MULTISTATE TAX
COMMISSION ON INTERIM REPORT OF HEARING OFFICER RE PROPOSED M.T.C.
REGULATION IV.18.(i): ATTRIBUTION OF INCOME
FROM THE BUSINESS OF A FINANCIAL INSTITUTION

WHEREAS, the Executive Committee has received the Interim Report of Hearing Officer Regarding Adoption of Proposed M.T.C. Regulation IV.18.(i): Attribution of Income from the Business of a Financial Institution dated November 9, 1990; and

WHEREAS, the Executive Committee has reviewed said Interim Report and determines that said Interim Report should be accepted in its entirety; and

WHEREAS, the pending regulatory proposal was originally scheduled for Commission action at its July, 1991 meeting; and

WHEREAS, the importance of the pending regulatory process requires that economic and other data be developed in the public record that is sufficient for the purposes of the Hearing Officer in the making of his recommendations to the Executive Committee herein; and

WHEREAS, the Executive Committee wishes to provide additional time for a thorough and studied consideration of the proposed Regulation and the facts and circumstances relating thereto; and

WHEREAS, the pending case of Ford Motor Credit Company, Inc. v. Florida Department of Revenue, No. 88-1847 will likely be decided by the U.S. Supreme Court within the next several months and that such decision may provide valuable insight into the method by which income derived from intangibles may be attributed.

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NOW, THEREFORE, IT IS HEREBY RESOLVED that the Executive Committee adopts all of the findings, conclusions and recommendations of the Hearing Officer as set forth in his Interim Report dated November 9, 1990.

IT IS FURTHER RESOLVED that the Executive Committee directs the Hearing Officer to keep the Executive Committee apprised of all developments in this matter.

IT IS FURTHER RESOLVED that the Executive Director develop and submit proposals for securing the data referred to in the Hearing Officer's Interim Report.

IT IS FURTHER RESOLVED, in the interest of providing sufficient time for the further development of the proposed Regulation, that it not be scheduled for action by the Commission in July of 1991; and that it will be scheduled for action by the Commission after completion of the public hearing process and upon further direction of the Executive Committee.

Adopted by the Executive Committee of the Multistate Tax Commission on this 9th day of November, 1990.

ATTEST: /s/ Dan R. Bucks
Dan R. Bucks
Executive Director

EXHIBIT C: 3

Resolution dated May 6, 1994

Multistate Tax Commission



**RESOLUTION OF THE EXECUTIVE COMMITTEE
OF THE MULTISTATE TAX COMMISSION
PURSUANT TO BYLAW 7 REGARDING FINANCIAL INSTITUTIONS**

WHEREAS, the Hearing Officer, Alan H. Friedman, after public hearing duly held pursuant to Article VII(2) of the Multistate Tax Compact and Bylaw 7(a) of the Commission, has submitted his "Final Report of Hearing Officer Regarding Proposed Multistate Tax Commission Formula for the Uniform Apportionment of Net Income from Financial Institutions" dated April 28, 1994; and

WHEREAS, the Hearing Officer has recommended, among other things, the adoption by the interested states of the Multistate Tax Commission of a formula for the uniform apportionment and allocation of net income derived by financial institutions; and

WHEREAS, Bylaw 7(g) requires such a recommendation be circulated to the affected members of the Multistate Tax Commission to determine if they will consider the recommendation for adoption within their respective jurisdictions; and

WHEREAS, the Hearing Officer has advised the Executive Committee that certain technical changes to the proposal are likely to be made by him over the next few weeks, given that interested persons have now had an opportunity to review the proposal in its entirety.

NOW, THEREFORE, IT IS RESOLVED THAT the Executive Director is directed to survey the affected Commission member states pursuant to said Bylaw 7(g) and to report the results thereof to the Chairman of the Executive Committee as soon as practicable, but no later than July 15, 1994; and

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IT IS FURTHER RESOLVED THAT the recommendation so surveyed shall be either that attached as Exhibit A to the Final Report of Hearing Officer or one containing the technical changes made thereon as indicated Section II.A. and footnote 11 of said Final Report.

Entered this 6th day of May, 1994 by the Executive Committee of the Multistate Tax Commission.

Attest: /s/ Dan R. Bucks
 Dan R. Bucks
 Executive Director

EXHIBIT D

NOTICES OF PUBLIC HEARINGS AND ATTENDANCE LISTS

EXHIBIT D: 1

Notices of Public Hearing

Multistate Tax Commission



NOTICE OF PUBLIC HEARING

The Multistate Tax Commission will hold a series of public hearings on the following subject:

Proposed Allocation and Apportionment Regulation IV.18.(i)
(Financial Institutions)

A copy of the proposed Regulation IV.18.(i) may be obtained by writing to:

Michael Mazerov, Director of Policy and Research
Multistate Tax Commission
444 No. Capitol St., N.W.
Washington, D.C. 20001

The hearings shall be held at the following places at the dates and times specified below:

Washington, D.C.: Tuesday, August 21, 1990 at 9:30 A.M. Hall of the States, 444 No. Capitol St., N.W., Room 239.

San Francisco, CA: Thursday, August 23, 1990 at 9:30 A.M. San Francisco Chamber of Commerce Boardroom, 465 California St., 9th Fl.

Chicago, IL: Monday, December 3, 1990 at 9:30 A.M. LaSalle-Wacker Building, 12th Floor Boardroom, 221 No. LaSalle St.

Atlanta, GA: Tuesday, December 4, 1990 at 9:30 A.M. Inforum (Atlanta Market Center), 235 William St., Conference Room 6.

Should sufficient interest be expressed by affected industry representatives or other interested persons after the holding of these four hearings, the Hearing Officer will endeavor to accommodate that interest by holding one additional hearing in another location before issuing his Hearing Officer's Report.

The Commission invites all interested parties to participate in the hearing. Those desiring to make oral presentations to the Hearing Officer must notify him in writing at least ten (10) days

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prior to the hearing date. Anyone desiring to submit written comments may do so with the Hearing Officer at least three (3) days prior to the hearing date.

The Hearing Officer is:

Alan H. Friedman
386 University Avenue
Los Altos, CA 94022
Tel.: (415)-941-0556

Multistate Tax Commission



NOTICE OF PUBLIC HEARING

The Multistate Tax Commission will hold three sessions of a public hearing on the following subject:

The development and adoption of Proposed Multistate Tax Commission Regulation VI.18.(i) dealing with the attribution of income from the business of a financial institution.

To this end, the Hearing Officer will receive public input in person and in writing from all interested persons addressing the following matters:

1. *How should states treat intangible property in the form, e.g., unsecured or secured loans, securities, etc. for income attribution purposes?*
2. *Should the receipts factor reflect the delivery of financial institutions' services on a destination basis or on a majority of "cost of performance" basis?*
3. *What is the most appropriate definition of the terms "financial institution" and "business of a financial institution" for the purpose of statutory or regulation coverage?*
4. *With regard to states that apply the unitary business principle and combined reporting, what, if any, approach should the proposal take with regard to such principles.*
5. *What, if any, approach should the proposal take with regard to nexus and/or de minimis concepts?*
6. *Whether a throwback, throwout or another approach is appropriate to address the attribution of receipts that are sourced to states in which the taxpayer is not subject to taxation?*
7. *Such other issues and suggestions that state representatives and other members of the taxpaying community may wish to present for consideration.*

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A copy of the most recent draft version of the proposed uniform statute/regulation (MTC Reg.IV.18.(i)) may be obtained by writing or calling:

Teresa Moore
Multistate Tax Commission
444 North Capitol St., N.W.
Washington, D.C. 20001
Phone: (202)-624-8699

The Hearing Officer that has been assigned to this matter is:

Alan H. Friedman, General Counsel
Multistate Tax Commission
386 University Avenue
Los Altos, CA 94022
Phone: (415)-941-0556

Two of the public sessions, which have already been announced, will be held at the locations, dates and times specified as follows:

1. Thursday, May 27, 1993 beginning at 10:00 a.m. at the Ronald Reagan State Office Building, 300 South Spring Street, Los Angeles, California, first floor Auditorium.
2. Thursday, July 15, 1993, beginning at 10:00 a.m. at the Hall of the States, 444 No. Capitol St., N.W., Room 333, Washington, D.C.

The third public session will be held on September 30, 1993, beginning at 10:00 a.m. at 1345 Avenue of the Americas, Arthur Andersen Conference Center, second floor, New York, New York.

The Multistate Tax Commission invites all interested parties to participate in the public sessions of this hearing. Those desiring to make oral presentations to the Hearing Officer must notify him in writing at least two working days prior to the holding of the public session. An attempt will be made to accommodate those who wish to present oral testimony but are unable to travel to the location for the public sessions. Any person desiring to testify by use of telecommunications should make that desire known at the time he/she discloses an interest in making a presentation. Depending upon feasibility, an attempt will then be made to assign specific time slots to those parties requesting the opportunity to testify by telecommunications. Anyone desiring to submit written comment may do so by submitting them to the

Hearing Officer at any time prior to the last date for public session or such later date as may be announced for the closing of the public hearing.

Multistate Tax Commission



ATTENDANCE LIST

MULTISTATE TAX COMMISSION HEARING ON PROPOSED REG. IV.18(j)

Attribution of Income of Financial Institutions

New York, NY

September 30, 1993

<u>NAME</u>	<u>REPRESENTING</u>	<u>ADDRESS</u>
Jo Ames	Ernst & Young - National Tax 1200 19th St, N.W. Washington, D.C. 20036	202/663-9598
Julie McCallip	North American Mortgage Co. 3883 Alleyway Dr. Santa Rosa, CA 95403	(707) 523-5548
PETER MCGOWAN	MERRILL LYNCH	WORLD FINANCIAL CTR. N.Y. NY
Anita Haroutounian	First Boston Corporation 5 World Trade Center	NY, NY
Terry Shirley	State of Maine	(207) 822-6370
Pete Tsoukalas	State of Maine	Augusta, ME
Maria Jones	Rosenman & Collin	575 Madison Ave. NY
Gary Cole	Coopers & Lybrand	1301 Ave. of the Americas, NY
John Rice	Coopers & Lybrand	1301 Ave. of Americas, NYC
DON DANZIERI	HOKKAIDO TAKUSHUKU BANK 2 WORLD TRADE CENTER	99TH FLOOR, NY, NY 10048
BARRY J. O'BRIEN	LEHMAN BROTHERS	3 WFC NY NY

Multistate Tax Commission



ATTENDANCE LIST

MULTISTATE TAX COMMISSION HEARING ON PROPOSED REG.IV.18(j)

Attribution of Income of Financial Institutions

New York, NY

September 30, 1993

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ATTENDANCE LIST

MULTISTATE TAX COMMISSION HEARING ON PROPOSED REG. IV.18(j)

Attribution of Income of Financial Institutions

Los Angeles, California

March 27, 1993

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JANET PASS	KPMG PEAT MARWICK	725 S. FIGUEROA
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ATTENDANCE LIST

MULTISTATE TAX COMMISSION HEARING ON PROPOSED REG. IV.18(j)

Attribution of Income of Financial Institutions

Los Angeles, California

March 27, 1993

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Multistate Tax Commission



MULTISTATE TAX COMMISSION

PROPOSED MTC REG. IV.18(i)
(Attribution of Income from Financial Institutions)

Public Hearing Session
Washington, D.C.
July 15, 1993

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Multistate Tax Commission



MULTISTATE TAX COMMISSION

PROPOSED MTC REG. IV.13 (i)
(Attribution of Income from Financial Institutions)

Public Hearing Session
Washington, D.C.
July 15, 1993

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Multistate Tax Commission



MULTISTATE TAX COMMISSION

PROPOSED MTC REG.IV.13(i)
(Attribution of Income from Financial Institutions)

Public Hearing Session
Washington, D.C.
July 15, 1993

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Multistate Tax Commission



MULTISTATE TAX COMMISSION

PROPOSED MTC REG. IV.18(i)
(Attribution of Income from Financial Institutions)

Public Hearing Session
Washington, D.C.
July 15, 1993

ATTENDANCE LIST

NAME	Address
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Trish Wolff	805 15th St. NW #300 Washington, DC 20005
Nancy Fluri	MFC Financial 100 S. Charles St. Baltimore, MD 21201

EXHIBIT D: 2

Proposed definition of "finance leasing"

Multistate Tax Commission



Multistate Tax Commission Public Hearing Regarding
Proposed Regulation IV.18.(i)
(Financial Institutions)

DEFINITION OF "FINANCE LEASING".

The term "finance leasing" was not earlier defined in the proposed Regulation IV.18.(i). See, proposed Reg.IV.18.(i)B.(2), Reg.IV.18.(i)B.(6), and Reg. IV.18.(i)D.(2)(a). The definition of such term to be included in the proposed Regulation is as follows:

Reg.IV.18.(i)B.(6). "Finance leasing" or "finance lease" shall mean any type of capital lease to which a financial institution is a party, including sales-type, leveraged, and direct financing leases, that involves the transfer to the lessee of substantially all of the risks and burdens of ownership in the property subject to the lease. A "finance leasing or finance lease" is further evidenced by the lessee reporting such lease as an asset and a liability for financial accounting purposes. To the extent that it cannot be determined whether a capital lease falls within this definition of "finance leasing" or "finance lease", reference shall be made to the classification of leases set forth in Statement of Financial Accounting Standards No. 13, "Accounting for Leases" in effect as of the date of the adoption of this Regulation.

The public is invited to offer comment upon the foregoing definition, as well as upon any other provision of the Proposed Regulation by writing to:

Alan H. Friedman
Hearing Officer
386 University Avenue
Los Altos, CA 94022

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444 North Capitol Street, N.W.
Suite 409
Washington, D.C. 20001
(202) 624-8699

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EXHIBIT D: 3

**Copy of Notice of Public Hearing - ABA Banker's Weekly, Vol. 9, No. 29
(July 24, 1990)**

FARM CREDIT SYSTEM STANDS READY TO COMPETE

THINK ABOUT IT! ON PAGE 8

Newspaper Treatment

ABA Bankers Weekly

July 24, 1990

The Newspaper of the American Bankers Association

Volume 9, No. 29

ABA urges bankers to participate in multistate-taxation proceedings

The Multistate Tax Commission has scheduled a series of hearings to cover its proposed regulations governing taxation of out-of-state banks.

ABA will testify against the proposal at the Aug. 21 hearing in Washington, D.C. ABA is encouraging member banks to testify or provide written comments to MTC.

ABA's position is that a two-year moratorium should be imposed on this issue so further study can be completed. Cost of compliance by the states would exceed any tax collected, ABA said.

The regulations would permit a state to tax the income earned by an out-of-state bank with no physical presence in that state if the bank has as few as 100 credit-card customers or \$5 million in loans or \$5 million in deposits in that state.

Although MTC regulations are

only guidelines, MTC member states — generally those in the West and Midwest — can enact the regulations as written.

Other hearings are planned for Aug. 23 in San Francisco, Dec. 3 in Chicago and Dec. 4 in Atlanta. An additional hearing may be scheduled if response from the

banking industry warrants it, MTC said.

Bankers wishing to testify must notify the hearing officer in writing 10 days prior to the hearing. The hearing officer is Alan H. Friedman, 386 University Ave., Los Altos, Calif. 94022; telephone (415) 941-0556.

EXHIBIT D: 4

Lists of Persons Attending Public Hearing Sessions

ATTENDANCE LIST

Multistate Tax Commission Public Hearing Regarding Proposed Regulation IV.18.(i) (Financial Institutions)

Washington, D.C.
August 21, 1990

NAME	ADDRESS	REPRESENTING
VICTOR ZAMMIT	277 PARK AVE, N.Y., N.Y.	ERNST & YOUNG
LLOYD J. LOORAM	1345 AVE. OF AM. N.Y. N.Y.	ARTHUR ANDERSON + CO.
PAUL CLAYTOR	1120 CONNECTICUT, WASH	AMERICAN BANKERS ASSN
HENRY RUSHMORE	1120 CONNECTICUT AVE. WASH	" " "
William J Hunter	1150 Trowl ST. Brookfield VT	" " "
Jeanne Jones	1120 Connecticut Ave, New Wash, DC	" " "
STEVE O'CONNOR	1776 G ST	Freddie Mac
Eric J Cottle	PO 1468, Legal Div. Sacto CA 95807	Calif Franchise Tax Bd
MARY BETH RANKIE	CORP. TAX DIV - HDQ 8416, 919 E. MAIN ST. RICHMOND VA, 23219	CRESTAR BANK
MERLE BUFF	AMERICAN EXPRESS COMPANY, WORLD FINANCIAL CENTER, NY, NY	
Bill Hayden	350 Third Ave NY, NY 10043	Citibank NA
Jeff Seether	399 Park Avenue New York, N.Y. 10043	Citibank
Haskell Edelstein	399 Park Ave. 2 nd fl. New York, N.Y. 10043	Citibank
John O'Drury	76 Long Tax PO Box 600 Norfolk, Va 23501	Southern Financial Corp.
WALTER SELTZER	4615 E AVE, N.Y.C. 10017	STATE BANK OF SOUTH AUSTRALIA
Dan Bucks	444 N. Capitol SE N.W.	MTC
Daniel V. Spang	304 TURNPIKE RD. SOUTHBORO, MA.	CREDIT UNION NATIONAL ASSOC. (CUNA)
Colleen Kelly	805 15 th St NW #300 Washington, D.C. 20005	Credit Union National Assoc. (CUNA)
Karen Tiller	"	"
Larry Blandford	"	"
Luis Portio	"	"
Michael Johansen	Md. Dept. of Fiscal Services Room 226 90 State Circle Annapolis, MD 21401	
John Kinney	ERNST & YOUNG, 1775 LINDEN ST, MILWAUKEE, WI 53233	ERNST & YOUNG

NAME

ADDRESS

REPRESENTING

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Financial Institutions

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Name

Address

Representative

Jaqueline L. Samuels

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First
Interstate

JEFFREY L. HYDE

Arthur Andersen & Co
1666 K St. NW
Washington, D.C. 20006

ATTENDANCE LIST

Multistate Tax Commission Public Hearing Regarding Proposed Regulation IV.18.(i) (Financial Institutions)

San Francisco, CA
August 23, 1990

NAME	ADDRESS	REPRESENTING
Mark Fisher	Oellette & Touche One World Trade Center Long Beach CA	Self / clients
Eugene Corrigan	Ernst & Young 555 Capitol Mall, Ste 650 SACRAMENTO, CA 95814	
ARNOLD WEBER	ATTORNEY AT LAW 57 POST STREET, #612 SAN FRANCISCO, CA 94104	
JOYCE URUSHIMA	PRICE WATERHOUSE 1800 HARRISON ST SUITE 1500 OAKLAND CA 94612	
Phil Hansen	Ford Financial Services 733 Front St San Francisco 94111	
JOHN REILLY	CORPORATE TAX DEPT. 700 MARKET STREET S.F. 94102	FIRST NATIONWIDE BANK
KENN KOVITZ	EXECUTIVE LAW EDITOR COMMERCE CLEARING HOUSE SAN RAFAEL, CA 94903	
Jon Nakamura	Calif Bankers Assoc 455 Market St 17th Fl.- SF CA 94105	Calif Banking Industry
Jeffrey M. Vesely	PILLSBURY, MADISON + SUTRO P.O. Box 7880 San Francisco, CA 94120	

ATTENDANCE LIST

Multistate Tax Commission Public Hearing Regarding Proposed
Regulation IV.18.(i) (Financial Institutions)

San Francisco, CA
August 23, 1990

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<u>JACK HODGES</u>	<u>343 SANSOME ST SF CA 94104</u>	<u>WELLS FARGO + Co.</u>
<u>PHILIP M PLANT</u>	<u>555 CALIF ST SF CA 94102</u>	<u>BANK OF AMERICA</u>
<u>ALBIN C. KOCH</u>	<u>400 3900 W. ALAMEDA, TOLUCA LAKE, CA. 94505</u>	<u>HORGAN, ROSBA BECKHAM & COEN.</u>
	<u>BRUBBECK, PHLEGER + HARRISON</u>	
	<u>SPEAR STREET TOWER</u>	
	<u>ONE MARKET PLAZA</u>	
<u>ROY E CRAWFORD</u>	<u>SAN FRANCISCO CA 94105</u>	<u>WELLS FARGO-</u>

ATTENDANCE LIST

Multistate Tax Commission Public Hearing Regarding Proposed Regulation IV.18.(i) (Financial Institutions)

Chicago, IL
December 3, 1990

NAME	ADDRESS	REPRESENTING
David G. Manning	300 W. Edwards, Spfld, IL	Community Bankers Assoc of IL
PAUL CLAYTOR	231 SOUTH LASALLE CHICAGO, IL 60647	CONTINENTAL BANK
BRUCE C JANDUSKY	50 SOUTH LaSalle St Chicago, Ill 60175	The Northern Trust Company
Thomas C. Cordwell	3256 Ridge Rd. Lansing IL 60438	First Nat'l Bank of IL
Philip Klein	190 S. LaSalle St Chicago, IL 60602	Hays, Brown + Platt
WILLIAM J. HOOPER	111 N CANAL ST CHICAGO, IL 60606	ILLINOIS BANKERS ASSN.
Edward W. Kim	50 S. LaSalle, M-11 CHICAGO, IL 60675	Northern Trust Co.
Robert C. Bob Sash	Arthur Andersen 10 S. LaSalle Chicago IL 60603	Arthur Andersen
DORICE E PEPIN	Arthur Andersen 10 S LaSalle Chgo IL 60614	Arth Andersen
DARRELL COPPIN	KPMC PEAT MARWICK 303 E. WACKER DRIVE CHICAGO, ILL. 60603	

ATTENDANCE LIST

Multistate Tax Commission Public Hearing Regarding Proposed
Regulation IV.18.(i) (Financial Institutions)

Atlanta, GA
December 4, 1990

NAME	ADDRESS	REPRESENTING
THOMAS KAAMER	HELLER FINANCIAL, INC. 200 N. LA SALLE ST. CHICAGO, IL 60601	
COREY STRICKER	"	"
Thayer J. Herke	First Natl Bank of Chgo 1 South Wacker	
Pick Althoff	Chicago, IL 60606	Samwa Business Credit Corporation
Ed Kim	Northern Trust	
Clere Tande	1650 Farnam street Omaha NE	Kutak Rock + Campbell
Kristin Hall	Harris Trust + Savings Bank 111 W. Monroe Chicago IL 60690	
Vicki Pozzo	Illinois Credit Union League, 1807 W. Dixon, P.O. 310 Naperville, IL 60556	
Bruce J. Baker	Dean Witter Financial Services Group, Inc. 2500 Lake Cook Road Riverwoods, Illinois 60015	
Charles Wooding	First National Bank of Chicago One First National Plaza Suite #308	

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Multistate Tax Commission Public Hearing Regarding Proposed Regulation IV.18.(i) (Financial Institutions)

Atlanta, Georgia
December 4, 1990

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Tom Neubig	Suite 700 1801 K St. N.W. Washington, D.C. 20006	Price Waterhouse
Jo Mitchell	Tax Dept P.O. Box 4899 Atlanta, GA 30302	C+S / SOVRAN
Fred E. Ferguson	Price Waterhouse 1801 K Street, NW Suite 700 Washington, DC 20006	Financial Institutions State Tax Coalition
ROBERT F McAMMON, JR	CORESTATES FINANCIAL CORP P.O. Box 7618 F.C. 1-3-168-3 PHILADELPHIA PA 19101-7618	CORESTATES FINANCIAL CORP
Kenneth Cline	American Banker 3390 Peachtree Rd Suite 1000 Atlanta GA 30326	
Mary KLOPFENSTEIN	ARTHUR ANDERSEN & CO 133 PEACHTREE ST. N.E. ATLANTA, GA 30303	ARTHUR ANDERSEN
Mark M. Coraich	Arthur Andersen & Co 133 Peachtree St. Atlanta, Georgia 30303	Arthur Andersen & Co.
DeAnne Raven	SC Tax Study Comm. P.O. Box 142 Columbia, SC 29202	SC Tax Study Committee
S. HUNTER HOWARD JR	P.O. BOX 125 COLUMBIA SC 29214	SETC

Multistate Tax Commission



ATTENDANCE LIST

MULTISTATE TAX COMMISSION HEARING ON PROPOSED REG. IV.18(j)

Attribution of Income of Financial Institutions

New York, NY

September 30, 1993

<u>NAME</u>	<u>REPRESENTING</u>	<u>ADDRESS</u>
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Jeffrey Seretker	Citibank	399 Park Ave. NY, NY 10043
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HENRY RUEMPLER	Amer. Bankers Assn.	1120 Connecticut Ave. NW WASH. D.C. 20036
Michael Hyman	NYC Dept of Finance	1 Centre St, Rm 506 NY, NY 10007
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GORDON MARTIN	WEITAC BANKING	N.Y. N.Y.

Multistate Tax Commission



ATTENDANCE LIST

MULTISTATE TAX COMMISSION HEARING ON PROPOSED REG. IV.18(j)

Attribution of Income of Financial Institutions

New York, NY

September 30, 1993

<u>NAME</u>	<u>REPRESENTING</u>	<u>ADDRESS</u>
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Joseph DiGennaro	Chemical Bank	130 John St., NY NY 10038
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Dr. Rajana Madhusudhan	NJ Treasury	NJ Div. of Taxation, OTA 50 Barrack Street CN 269, Trenton NJ 08646
Amy Pickard	Pennsylvania Dept of Revenue	1147 Strawberry Square HARRISBURG PA 300 ST. PAUL PLACE 17066
GEORGE HUPFER	Commercial Credit	BALTIMORE, MD. 21202
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Multistate Tax Commission



ATTENDANCE LIST

MULTISTATE TAX COMMISSION HEARING ON PROPOSED REG. IV.18(j)

Attribution of Income of Financial Institutions

New York, NY

September 30, 1993

<u>NAME</u>	<u>REPRESENTING</u>	<u>ADDRESS</u>
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Multistate Tax Commission



ATTENDANCE LIST

MULTISTATE TAX COMMISSION HEARING ON PROPOSED REG. IV.18(j)

Attribution of Income of Financial Institutions

New York, NY

September 30, 1993

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Multistate Tax Commission



ATTENDANCE LIST

MULTISTATE TAX COMMISSION HEARING ON PROPOSED REG. IV. 18(j)

Attribution of Income of Financial Institutions

New York, NY

September 30, 1993

<u>NAME</u>	<u>REPRESENTING</u>	<u>ADDRESS</u>
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Robert J. Buckley	Arthur Andersen	48 WALL ST NY, NY
PAUL BUCHMAN	Bank of NY	805 15th Str. NW # 300 Washington, DC 20005
Wid Wolff	CUNA - Affiliates	
DOUG LINDHOLM	PRICE WATERHOUSE	1801 K ST NW Ste 700 Washington, DC 20006
DOM FIORE	GE CAPITAL	777 Long Ridge Rd. STAMFORD, CT. 06927
Fred E. Ferguson	Arthur Andersen	Washington, DC
Holly Chamberlin	KEY CORP	PO Box 88 Albany NY 12202

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EXHIBIT E

INTERIM REPORTS OF HEARING OFFICER

EXHIBIT E: 1

**Interim Report of Hearing Officer
(November 9, 1990)**

Multistate Tax Commission



Multistate Tax Commission
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Phone (415) 941-0556
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ALAN H. FRIEDMAN, General Counsel

Multistate Tax Commission
444 North Capitol St., N.W.
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Phone (202) 624-8699

INTERIM REPORT OF HEARING OFFICER REGARDING ADOPTION OF
PROPOSED M.T.C. REGULATION IV.18.(i): ATTRIBUTION OF INCOME
FROM THE BUSINESS OF A FINANCIAL INSTITUTION

On May 10, 1990, the Executive Committee of the Multistate Tax Commission adopted a resolution ordering a public hearing to be held pursuant to Article VII.2. of the Multistate Tax Compact regarding the adoption of proposed M.T.C. Regulation IV.18.(i): Attribution of Income from the Business of a Financial Institution. Two sessions of that public hearing have already been held and two sessions remain to be held. Even though the public hearing process has not as yet been completed, the Hearing Officer now has sufficient information that suggests he issue this Interim Report in order to submit certain recommendations to the Executive Committee with respect to the future course of these proceedings. Since the Hearing Officer has not had the benefit of the submissions yet to be made, it is to be emphasized that he is making no recommendations at this time with regard to the substance of any provision contained in the proposed Regulation.

INTERIM FINDINGS

The Hearing Officer, based upon the public record developed thus far, finds that the record falls short of providing sufficient data upon which he can appropriately determine several issues that impact the effectiveness of various provisions contained in the proposed Regulation. For example, the record is thus far bereft of economic and other data regarding such issues as (1) the approximate amount of "nowhere" income that results from the apportionment methodologies currently employed by the states to impose their income or franchise taxes upon financial institutions

transacting business in interstate commerce; (2) the extent to which foreign financial institutions register with the states and pay their income or franchise taxes; (3) the extent to which community banks may be affected by the proposed Regulation in terms of competitive advantages and disadvantages that may result from a state's adoption thereof; and the like.

In addition, the Hearing Officer notes that one of the elements contained in the proposal - the "regular solicitation" nexus aspect of the proposal (referred hereafter as "economic presence") - has been called into question by certain representatives of the financial institutions industry. The Hearing Officer finds that it is in the best interests of the states and the affected industry members that this limited issue be judicially addressed and settled as soon as practicable. The Hearing Officer anticipates that the states' various litigation efforts with regard to the case of National Bellas Hess, Inc. v. Department of Revenue of State of Illinois, 386 U.S. 753 (1967), or the pending case of Alabama v. Credit Card Companies, No. 88-288-G, Fifteenth Judicial Circuit (3/7/90), app. pend., may provide some guidance within the next one to two year period as to the extent and application of the economic presence nexus principle.

The Hearing Officer firmly believes that an out-of-state business may create an "economic presence" in its market state, through regular or systematic solicitation by any means; and that such presence would be sufficient to constitutionally require that business to comply with various state tax duties, even though that business is not physically present within the state. However, many members of the financial industry will not accept that proposition unless and until the United States Supreme Court clearly affirms that legal principle.

Lastly, the case of Ford Motor Credit Company, Inc. v. Florida Department of Revenue, No. 88-1847 is now pending before the United States Supreme Court. The decision in the Ford Motor Credit case

may well provide added guidance as to the power of the state of commercial domicile to impose an unapportioned tax upon intangibles or income derived from the ownership thereof.

CONCLUSIONS AND RECOMMENDATIONS

Based upon the foregoing findings, the Hearing Officer concludes that a sufficiently studied and thorough development of the proposed Regulation cannot readily be accomplished during the presently scheduled timetable for the completion of the regulatory process. Therefore, the Hearing Officer recommends that the current timetable for completion of the pending regulatory process be held in abeyance until further directed by the Executive Committee. During the interim period, the Hearing Officer recommends the following specific actions be taken:

1. That the Hearing Officer hold the two remaining public sessions and such other sessions as he determines appropriate and keep the public record open until further directed by the Executive Committee.
2. That the Hearing Officer continue to seek from the states and the financial institutions industry such additional data that may be necessary to support a final Hearing Officer recommendation.
3. That the Multistate Tax Commission, through its Executive Committee, continue to monitor and support various state efforts to obtain an early judicial declaration concerning the "economic presence" and other nexus principles that may be appropriate for industries that transact business across state lines without being physically present in the market state.
4. That the Hearing Officer continue to review appropriate principles for establishing nexus with regard to the financial institutions industry in addition to that provided in the

current draft of the proposed Regulations.

5. That the Hearing Officer continue to provide the point of contact for industry input in order to further the states' understanding of the potential impact of the proposed Regulation.

6. That, given the time necessary for the further development and consideration of the public record, this matter not be scheduled for Commission action in July of 1991 as originally proposed; but it be scheduled for action upon completion of the public hearing process and as further directed by the Executive Committee.

This Interim Report of the Hearing Officer is submitted this 9th day of November, 1990.



Alan H. Friedman
Hearing Officer

EXHIBIT E: 2

**Interim Report of Hearing Officer
(May 10, 1993)**

Multistate Tax Commission



May 10, 1993

Sharon Morrow
Chair, Executive Committee
Multistate Tax Commission
c/o D.C. Dept. of Fin. & Rev.
Suite 400
441 4th Street, NW
Washington, D.C. 20001

Re: *Interim Report of Hearing Officer Regarding Proposed Regulation IV.18.(i) Apportioning the Income of Financial Institutions*

Dear Chair Morrow:

I am submitting the enclosed Interim Report Regarding Proposed Regulation IV.18.(i) Apportioning the Income of Financial Institutions for your information. The Report will be sent to the Tax Administrators of all Commission member states for their review and consideration.

This Report and the proposal submitted with it represents a major milestone in the development of a uniform method for apportioning income derived from the multistate business activities conducted by financial institutions. As you will note from the Report, the proposal is the product of over a year's effort by scores of persons representing both government agencies and financial institutions. The next step, as authorized by the Executive Committee at its last meeting, is to present this proposal for public review and comment. Two of three sessions of a public hearing have now been set, with the third to be set in the near future. I would hope to complete the public hearing and final report stage by the end of this calendar year.

I remain available for any questions that you or any other member of the Commission may have with regard to the proposal.

Very truly yours,

Alan H. Friedman
Hearing Officer

cc: Member State Tax Administrators

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Houston Audit Office:

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Multistate Tax Commission



INTERIM REPORT OF HEARING OFFICER REGARDING PROPOSED REGULATION IV.18(i) APPORTIONING THE INCOME OF FINANCIAL INSTITUTIONS

INTRODUCTION

The following is intended as an interim report to the Executive Committee of the Multistate Tax Commission regarding the current status of the effort to develop a uniform apportionment method for the attribution of income earned by financial institutions.¹ Attachment 1. is a draft proposal of one such method of attribution which will be introduced in the resumed public hearing process for comment and consideration. This proposal is the product of the joint effort of government and industry representatives that was supported by the Commission and the Federation of Tax Administrators (the "MTC/FTA Working Group on Financial Institutions"). As noted below, fairly broad industry input was developed and provided primarily through the coordinated efforts of a coalition of several large financial institutions organized and acting under the acronym of F.I.S.T.² A listing of the principal individuals who assisted in this effort is appended as Attachment 2.

The draft formula presented here was developed through the collective efforts of extremely able and experienced persons representing both government and industry interests. It represents the result of a cooperative effort that continues between government and industry, as well as between and within various factions of government as well. On the one hand, representatives of jurisdictions such as New York State, South Dakota and New York City represented a more commercial domicile or "money-center" approach. On the other, representatives of states such as Minnesota, Tennessee, New Hampshire, North Dakota and several others represented

¹ For a bit of relatively recent history concerning this effort, see "Report of Subcommittee on Apportionment of Income from Financial Institutions" dated March 30, 1991 from Alan H. Friedman, Convener, to Heidi Heitkamp, North Dakota State Tax Commissioner, Chair, MTC/FTA Working Group on Financial Institutions and attachments. This Report can be obtained by contacting the Multistate Tax Commission at 202-624-8699.

² F.I.S.T. stands for "Financial Institutions State Taxation" Coalition. While the acronym suggests something other than an extended and open hand, the Coalition, as noted in this Report, did not act in the manner suggested by its moniker.

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a substantial revenue loss to the state. Lastly, in this regard, a continuing commitment has been expressed by the F.I.S.T. coalition to work in support the states' legislative and regulatory adoption of the uniform apportionment method, so long as that method is "fair and administrable" and adopted by a significant number of jurisdictions.

THE EFFORT TO ACHIEVE UNIFORMITY AMONG THE STATES

The basic purpose of this effort - the achievement of a fair, administrable and uniform apportionment methodology - will be greatly undermined should states modify, in any substantial manner, the attribution or factor weighting rules that are suggested by a uniform apportionment method. Unilateral modifications raise the serious risk (theoretically at least) of affected institutions being subject to apportionment and taxation of either more or less than 100% of their net income. While the United States Supreme Court has tolerated a certain amount of over-apportionment of income, neither over-apportionment, nor under-apportionment to any substantial degree should be an acceptable goal for a rational, fair state tax system affecting interstate business enterprises.

Should a sufficient number of states, as well as a few of the more directly affected states, not adopt either the attached suggested approach or some other uniformly supported method, it is likely and understandable for the industry representatives to withdraw their current support of this effort. Should the states fall short of obtaining a fair, uniform and administrable apportionment approach in this most important area, voluntary industry compliance will be seriously impeded; and "business as usual" - division between taxpayer and government, contentiousness and conflict - will likely fill the void left from the emptying of this cooperative effort. All involved in this effort - industry representatives, tax officials and legislators - are requested to keep in focus the cooperative manner by which the following draft statute was created, its weighing of competing interests between government and industry, as well as among the government entities themselves.

SCOPE OF THE DRAFT STATUTE - THE DEFINITION OF FINANCIAL INSTITUTION; NEXUS: COMBINED REPORTING

The scope of the definition of a financial institution that is provided in Appendix A. to the proposal has been drafted in an effort to include traditional national and state banks, as well as other business entities that substantially deal in money or moneyed capital and compete with banks in the same marketplace. Should a state wish to broaden further or narrow the scope of coverage, it is free to do so without undermining the principal purpose of this uniformity effort. The focus of the current effort is principally on achieving apportionment uniformity, with scope of statute coverage being of secondary importance.

Respectfully submitted on May 10, 1993.

Alan H. Friedman

Alan H. Friedman
Hearing Officer

Am

ATTACHMENT 1.

**PROPOSED UNIFORM ALLOCATION AND APPORTIONMENT
METHOD FOR FINANCIAL INSTITUTIONS**

STATUTORY PROPOSAL FOR APPORTIONMENT AND ALLOCATION OF NET INCOME OF FINANCIAL INSTITUTIONS

Section 1. Imposition of Franchise Tax.¹

A franchise tax measured by net income is imposed on every financial institution for the privilege of doing business in this state and for exercising its franchise in a corporate or organized capacity.

Section 2. Apportionment and Allocation.

(a) A financial institution having income from business activity which is taxable both within and without this state shall allocate and apportion its net income as provided in this Act. All items of nonbusiness income (income which is not includable in the apportionable income tax base) shall be allocated pursuant to the provisions of []². All business income (income which is includable in the apportionable income tax base) shall be apportioned to this state by multiplying such income by the apportionment percentage.

(b) The apportionment percentage is determined by adding the taxpayer's receipts factor (as described in section 4 of this article), property factor (as described in section 5 of this article), and payroll factor (as described in section 6 of this

¹ This proposal assumes a tax measured by net income. There are a variety of other types of taxes that states may apply to financial institutions. While this proposal suggests a franchise tax that is measured by net income, other types of taxes that apply to financial institutions may be subjected to allocation and apportionment by the same or similar mechanism that is suggested here, and this section, as well as others, will need further modification. A franchise tax is selected here because it is clear that such a statute will not be precluded by federal law from including income earned from federal government obligations in its taxable base.

² While it is understood that all income derived from currently known activities of a financial institution, whether from deposit, lending and other credit activities or from investment activities dealing with tangible and intangible property, is business income, this sentence allows for the future possibility that some activity may be unrelated to the business activities commonly associated with financial institutions, but still authorized by law. Since this discrete business activity is theoretically possible, the proposed statute will more readily conform on its face to the dictates of the Allied Signal, Inc. v. Director, Div. of Taxation, 112 S.Ct. 2365 (1992).

article) together and dividing the sum by three. If one of the factors is missing, the two remaining factors are added and the sum is divided by two. If two of the factors are missing, the remaining factor is the apportionment percentage. A factor is missing if both its numerator and denominator are zero, but it is not missing merely because its numerator is zero.

(c) Each factor shall be computed according to the method of accounting (cash or accrual basis) used by the taxpayer for the taxable year.³

(d) If the allocation and apportionment provisions of this Act do not fairly represent the extent of the taxpayer's business activity in this state, the taxpayer may petition for or the State Tax Administrator may require, in respect to all or any part of the taxpayer's business activity, if reasonable:

(1) separate accounting;

(2) the exclusion of any one or more of the factors,

(3) the inclusion of one or more additional factors which will fairly represent the taxpayer's business activity in this State; or

(4) the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

Section 3. Definitions.

As used in this [Act], unless the context otherwise requires:

(a) "**Billing address**" means the location indicated in the books and records of the taxpayer as the address where any notice, statement and/or bill relating to a customer's account is mailed.

(b) "**Borrower or credit cardholder located in this state**" shall mean (1) a borrower, other than a or credit card holder, that is engaged in a trade or business which maintains its commercial domicile in this state; and (2) a borrower that is not engaged in a trade or business or a credit card holder whose billing address is in this state.

³ *Industry representatives have raised a compliance issue based upon the information that is to be used for calculating the factors - either financial book or tax basis. An industry suggested regulation is attached at Appendix A. which will be subject to comment during the public hearing process.*

(c) **"Commercial domicile"** means the headquarters of the trade or business, that is, the place from which the trade or business is principally managed and directed.

(d) **"Compensation"** means wages, salaries, commissions and any other form of remuneration paid to an employee for personal services that are included in such employee's gross income under the Federal Internal Revenue Code. In the case of employees not subject to the Federal Internal Revenue Code, e.g., those employed in foreign countries, the determination of whether such payments would constitute gross income to such employees under the Federal Internal Revenue Code shall be made as though such employees were subject to the Federal Internal Revenue Code.

(e) **"Credit card"** means credit, travel or entertainment card.

(f) **"Credit card issuer's reimbursement fee"** means the receipt a taxpayer receives from a merchant's bank because one of the persons to whom the taxpayer has issued a credit card has charged merchandise or services provided by the merchant to the credit card.

(g) **"Employee"** means, with respect to a particular taxpayer, any individual who, under the usual common-law rules applicable in determining the employer-employee relationship, has the status of an employee of that taxpayer.

(h) **"Financial institution"** means [insert state's definition here].⁴

(i) **"Gross rents"** means the actual sum of money or other consideration payable for the use or possession of property.⁵

(j) **"Loan"** means any extension of credit resulting from direct negotiations between the taxpayer and its customer, and/or the purchase, in whole or in part, of such extension of credit from another. Loans include participations, syndications, and leases treated as loans for federal income tax purposes.

⁴ No definition of "financial institution" is proposed at this time, leaving the state to define their own coverage. However, the Hearing Officer reserves the option to make a final recommendation regarding coverage at a future time. The definition provided in Appendix B is set forth for comment and consideration in the determination of what types of business organizations and activities may be made subject to the recommended formula.

⁵ In the interest of seeking additional uniformity, suggested regulatory language further defining the term "gross rents" is offered at Appendix C.

Loans shall not include: loans representing property acquired in lieu of or pursuant to a foreclosure under section 595 of the Federal Internal Revenue Code; futures or forward contracts; options; notional principal contracts such as swaps; credit card receivables, including purchased credit card relationships; non-interest bearing balances due from other depository institutions; cash items in the process of collection; federal funds sold; securities purchased under agreements to resell; assets held in a trading account; securities; interests in a REMIC, or other mortgage-backed or asset-backed security; and other similar items.⁶

(k) **"Merchant discount"** means the fee (or negotiated discount) charged to a merchant by the taxpayer for the privilege of participating in a program whereby a credit card is accepted in payment for merchandise or services sold to the card holder.

(l) **"Participation"** is an extension of credit in which an undivided ownership interest is held on a *pro rata* basis in a single loan or pool of loans and related collateral. In a loan participation, the credit originator initially makes the loan and then subsequently resells all or a portion of it to other lenders. The participation may or may not be known to the borrower.

(m) **"Principal base of operations"** with respect to movable property means the place of more or less permanent nature from which movable property is regularly directed or controlled. With respect to an employee, the "base of operations" means the place of more or less permanent nature from which the employee regularly starts his or her work and to which he or she customarily returns in order to receive instructions from the taxpayer, or communicates from his or her customers or other persons, or performs any other functions necessary to the exercise of his or her trade or profession at some other point or points.

(n) **"Real property owned"** and **"tangible personal property owned"** means real and tangible personal property, respectively, (1) on which the taxpayer may claim depreciation for federal income tax purposes, or (2) property to which the taxpayer holds legal title and on which no other person may claim depreciation for federal income tax purposes (or could claim depreciation if subject to federal income tax). Real and tangible personal property include land, stocks in goods and real and tangible personal property rented to the taxpayer. Real and tangible personal property do not include coin, currency, or property acquired in lieu of or pursuant to a foreclosure.

⁶ *The term "loan" is intended to have a broad meaning and the list of exclusions from the definition of "loan" is intended to be exclusive. For example, because an interest bearing balance due from another depository is not specifically mentioned in subparagraph (j), the underlying activity for such an account would be considered a loan.*

(o) "Regular place of business" means an office at which the taxpayer carries on its business in a regular and systematic manner and which is continuously maintained, occupied and used by employees of the taxpayer.

(p) "Syndication" is an extension of credit in which two or more persons fund and each person is at risk only up to a specified percentage of the total extension of credit or up to a specified dollar amount.⁷

(q) "Taxable in another state" means that a taxpayer is either:

(1) subject to a franchise tax measured by net income, a net income tax, a franchise tax for the privilege of doing business, or a corporate stock tax in another state; or

(2) that state has jurisdiction to subject the taxpayer to a net income tax regardless of whether, in fact, the state does or does not do so.⁸

Section 4. Receipts Factor.

(a) **General.** The receipts factor is a fraction, the numerator of which is the receipts of the taxpayer in this state during the taxable year and the denominator of which is the receipts of the taxpayer within and without this state during the taxable year. The method of calculating receipts for purposes of the denominator is the same as the method used in determining receipts for purposes of the numerator.

The receipts factor shall include only those receipts described herein which are included in the computation of the apportionable income base for the taxable year.

⁷ This definition permits the taxing jurisdiction to look to either the Call Reports, Federal Reserve Form FR Y-9C dealing with Consolidated Financial Statements for Bank Holding Companies, or the financial institution's records to determine the amount of receipts attributable to syndications.

⁸ The question of whether financial institutions are subject to a state's taxing jurisdiction will sometime depend upon what standard is to apply to determine the adequacy of nexus under applicable jurisdictional principles. Since financial institutions are service providers, as opposed to sellers of tangible personal property, Public Law 86-272 would not apply to such institutions. However, considerations under the Due Process and Commerce Clauses need be analyzed to determine issues of both taxability and throwback. See Quill v. North Dakota, 112 S.Ct. 1904 (1992).

(b) Receipts from the lease of real property. The numerator of the receipts factor includes receipts from the lease or rental of real property owned by the taxpayer if the property is located within this state or receipts from the sublease of real property if the property is located within this state.

(c) Receipts from the lease of tangible personal property.

(1) Except as described in paragraph (2) of this subdivision, the numerator of the receipts factor includes receipts from the lease or rental of tangible personal property owned by the taxpayer if the property is located within this state when it is first placed in service by the lessee.

(2) Receipts from the lease or rental of movable tangible personal property owned by the taxpayer, such as aircraft, rolling stock, water vessels, or mobile equipment, are 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 is determined by multiplying the receipts from the lease or rental 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. If the extent of the use of any movable tangible personal 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.

(d) Interest from loans secured by real property.

(1) The numerator of the receipts factor includes interest and fees or penalties in the nature of interest from loans secured by real property if the property is located within this state. If the property is located within this state and one or more other states, the receipts described in this subdivision are included in the numerator of the receipts factor if more than fifty percent of the fair market value of the real property is located within this state. If more than fifty percent of the fair market value of the real property is not located within any one state, then the receipts described in this subdivision shall be included in the numerator of the receipts factor if the borrower is located in this state.

(2) A loan is secured by real property if fifty percent or more of the principal amount of the loan is secured by real property at the time that the original loan agreement was made.

(3) The determination of whether the real property securing a loan is located within this state shall be made as of the time the original agreement was made and any and all subsequent substitutions of collateral shall be disregarded.

(e) **Interest from loans not secured by real property.** The numerator of the receipts factor includes interest and fees or penalties in the nature of interest from loans not secured by real property if the borrower is located in this state.

(f) **Net gains from the sale of loans.** The numerator of the receipts factor includes net gains from the sale of loans, including participations and syndications. Net gains from the sale of loans includes income recorded under the coupon stripping rules of section 1286 of the Internal Revenue Code.

(1) The amount of net gains (but not less than zero) from the sale of loans secured by real property included in the numerator is determined by multiplying such net gains by a fraction the numerator of which is the amount included in the numerator of the receipts factor pursuant to subdivision (d) of this section and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans secured by real property.

(2) The amount of net gains (but not less than zero) from the sale of loans not secured by real property included in the numerator is determined by multiplying such net gains by a fraction the numerator of which is the amount included in the numerator of the receipts factor pursuant to subdivision (e) of this section and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans not secured by real property.

(g) **Receipts from credit card receivables.** The numerator of the receipts factor includes interest and fees or penalties in the nature of interest from credit card receivables and receipts from fees charged to card holders, such as annual fees, if the billing address of the card holder is in this state.

(h) **Net gains from the sale of credit card receivables.** The numerator of the receipts factor includes all net gains (but not less than zero) from the sale of credit card receivables multiplied by a fraction, the numerator of which is the amount included in the numerator of the receipts factor pursuant to subdivision (g) of this section and the denominator of which is the taxpayer's total amount of interest and fees or penalties in the nature of interest from credit card receivables and fees charged to card holders.

(i) **Credit card issuer's reimbursement fees.** The numerator of the receipts factor includes all credit card issuer's reimbursement fees multiplied by a fraction, the numerator of which is the amount included in the numerator of the receipts factor pursuant to subdivision (g) of this section and the denominator of which is the taxpayer's total amount of interest and fees or penalties in the nature of interest from credit card receivables and fees charged to card-holders.

(j) **Receipts from merchant discount.** The numerator of the receipts factor includes receipts from merchant discount if the commercial domicile of the merchant is in this state. Such receipts shall be computed net of any cardholder charge backs, but shall not be reduced by any interchange transaction fees or by any issuer's reimbursement fees paid to another for charges made by its card holders.

(k) **Loan servicing fees.**

(1) The numerator of the receipts factor includes loan servicing fees derived from loans secured by real property multiplied by a fraction the numerator of which is the amount included in the numerator of the receipts factor pursuant to subdivision (d) of this section and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans secured by real property.

(2) The numerator of the receipts factor includes loan servicing fees derived from loans not secured by real property multiplied by a fraction the numerator of which is the amount included in the numerator of the receipts factor pursuant to subdivision (e) of this section and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans not secured by real property.

(l) **Receipts from services.** The numerator of the receipts factor includes receipts from services not otherwise apportioned under this section if the service is performed in this state. If the service is performed both within and without this state, the numerator of the receipts factor includes receipts from services not otherwise apportioned under this section, if a greater proportion of the income-producing activity is performed in this state based on cost of performance.

(m) **Receipts from investment assets and activities and trading assets and activities.**

(1) Interest, dividends, net gains and other income from investment assets and activities and from trading assets and activities shall be included in the receipts factor. Investment assets and activities and trading assets and activities include but are not limited to: investment securities; trading account assets; federal funds; securities purchased and sold under agreements to resell or repurchase; options; future contracts; forward contracts; notional principal contracts such as swaps; equities; and foreign currency transactions. With respect to the investment and trading assets and activities described in subparagraphs (A) and (B) of this paragraph, the receipts factor shall include the amounts described in such subparagraphs.

(A) The receipts factor shall include the amount by which interest from federal funds sold and securities purchased under resale agreements exceeds interest expense on federal funds purchased and securities sold under repurchase agreements.

(B) The receipts factor shall include the amount by which interest, net gains and other income from trading assets and activities, including but not limited to assets and activities in the matched book, in the arbitrage book, and foreign currency transactions, exceed net losses from such assets and activities.

(2) The numerator of the receipts factor includes interest, dividends, net gains and other income from investment assets and activities and from trading assets and activities described in paragraph (1) that are attributable to this state.

(A) The amount of interest, dividends, net gains and other income from investment assets and activities in the investment account to be attributed to this state and included in the numerator of the receipts factor is determined by multiplying all such income from such assets and activities by a fraction, the numerator of which is the average value of such assets which are properly booked for tax purposes at a regular place of business of the taxpayer within this state and the denominator of which is the average value of all such assets.

(B) The amount of interest from federal funds sold and purchased and from securities purchased under resale agreements and securities sold under repurchase agreements attributable to this state and included in the numerator of the receipts factor is determined by multiplying the amount described in subparagraph (A) of paragraph (1) from such funds and such securities by a fraction, the numerator of which is the average value of federal funds sold and securities purchased under agreements to resell which are properly booked for tax purposes at a regular place of business of the taxpayer within this state and the denominator of which is the average value of all such funds and such securities.

(C) The amount of interest, dividends, net gains and other income from trading assets and activities, including but not limited to assets and activities in the matched book, in the arbitrage book and foreign currency transactions, but excluding federal funds sold and purchased, attributable to this state and included in the numerator of the receipts factor is determined by multiplying the amount described in subparagraph (B) of paragraph (1) by a fraction, the numerator of which is the average value of such trading assets which are properly booked for tax purposes at a regular place of business of the taxpayer within this state and the denominator of which is the average value of all such assets.

(D) For purposes of this paragraph, average value shall be determined using the rules for determining the average value of tangible personal property set forth in subdivisions (c) and (d) of section five.

(3) In lieu of using the method set forth in paragraph (2) of this subdivision, the taxpayer may elect, or the State Tax Administrator may require in order to fairly represent the business activity of the taxpayer in this state, the use of the method set forth in this paragraph.

(A) The amount of interest, dividends, net gains and other income from investment assets and activities in the investment account to be attributed to this state and included in the numerator of the receipts factor is determined by multiplying all such income from such assets and activities by a fraction, the numerator of which is the gross income from such assets and activities which are properly booked for tax purposes at a regular place of business of the taxpayer within this state and the denominator of which is the gross income from all such assets and activities.

(B) The amount of interest from federal funds sold and purchased and from securities purchased under resale agreements and securities sold under repurchase agreements attributable to this state and included in the numerator of the receipts factor is determined by multiplying the amount described in subparagraph (A) of paragraph (1) from such funds and such securities by a fraction, the numerator of which is the gross income from such funds and such securities which are properly booked for tax purposes at a regular place of business of the taxpayer within this state and the denominator of which is the gross income from all such funds and such securities.

(C) The amount of interest, dividends, net gains and other income from trading account assets and activities, including but not limited to assets and activities in the matched book, in the arbitrage book and foreign currency transactions, attributable to this state and included in the numerator is determined by multiplying the amount described in subparagraph (B) of paragraph (1) by a fraction, the numerator of which is the gross income from such trading assets and activities which are properly booked for tax purposes at a regular place of business of the taxpayer within this state and the denominator of which is the gross income from all such assets and activities.

(4) If the taxpayer elects or is required by the State Tax Administrator to use the method set forth in paragraph (3) of this subdivision, it shall use this method on all subsequent returns unless the taxpayer receives prior written permission from the State Tax Administrator, or the State Tax Administrator requires, the use of a different method.

(5) The taxpayer shall have the burden of proving that an investment asset or activity or trading asset or activity was properly booked for tax purposes at a regular place of business outside of this state by demonstrating that the day-to-day decisions regarding the asset or activity occurred at a regular place of business outside the state. Where the day-to-day decisions regarding an investment asset or activity or trading asset or activity occur at more than one regular place of business and one such regular place of business is in this state and one such regular place of business is outside this state, such asset or activity shall be considered to be located at the regular place of business of the taxpayer where the investment or trading policies or guidelines with respect to the asset or activity are established. Unless the taxpayer demonstrates to the contrary, such policies and guidelines shall be presumed to be established:

(A) in the case of a taxpayer organized under the laws of the United States or of any state, at the commercial domicile of the taxpayer; or

(B) in the case of a taxpayer organized under the laws of a foreign country, in the state which the taxpayer has declared to be its home state pursuant to the provisions of the International Banking Act of 1978. If a taxpayer described in this clause has not made such a declaration or is not required to make such a declaration, the asset or activity shall be presumed to be located at the taxpayer's place of business in the United State to which the greatest number of employees are regularly connected or out of which they are working, irrespective of where the services of such employee are performed, as of the last day of the taxable year.

(n) **All other receipts.** The numerator of the receipts factor includes all other receipts pursuant to the rules set forth in ... [INSERT YOUR STATE'S REGULAR SITUSING RULES FOR THE RECEIPTS NOT COVERED BY THIS SECTION.]

(o) **Attribution of certain receipts to commercial domicile.** All receipts which would be assigned under this section to a state in which the taxpayer is not taxable shall be included in the numerator of the receipts factor, if the taxpayer's commercial domicile is in this state.

Section 5. Property Factor

(a) **General.** The property factor is a fraction, the numerator of which is the average value of the taxpayer's real property, tangible personal property, loans and

credit card receivables located and used⁹ within this state during the taxable year and the denominator of which is the average value of all such property located and used both 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

⁹ While the phrase "located and used" quite applicable with regard to real and tangible personal property, it is much less so with regard to intangibles such as loans and credit card receivables. This provision is not intended to condition the location or assignment of these intangibles on their use in the state. With regard to these intangibles, the location of the intangible will control and their use, for example where the proceeds of a loan are applied or where the interest payment or loan repayment may be made, are neither relevant nor operative.

be used consistently by the taxpayer with respect to property within and without the state and on all subsequent returns unless the taxpayer receives prior written 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 leased 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 subdivision 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 written 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 subdivision, 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) Movable tangible property, such as aircraft, rolling stock, water vessels, or mobile equipment, are 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 movable tangible 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 -

(i) it is properly booked for tax purposes at a regular place of business of the taxpayer within this state; or

(ii) in the case of a taxpayer organized under the laws of the United States or of any state, the loan is properly booked for tax purposes at a place which is not a regular place of business of the taxpayer and such taxpayer's commercial domicile is within this state; or

(iii) in the case of a taxpayer organized under the laws of a foreign country, the loan is properly booked for tax purposes at a place which is not a regular place of business of the taxpayer and such taxpayer has declared this state to be its home state pursuant to the provisions of the International Banking Act of 1978. If a taxpayer described in this clause has not made such a declaration or is not required to make such a declaration, the loan shall be presumed to be located at the place in the United States to which the greatest number of employees are regularly connected or out of which they are working, irrespective of where the services of such employee are performed, as of the last day of the calendar year.

(B) The state in which a loan has a preponderance of substantive contact with a regular place of business of the taxpayer shall be the state in which a loan is properly booked.¹⁰

(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 subdivision (g) of this section.

Section 6. Payroll factor.

(a) General. The payroll factor is a fraction, the numerator of which is the total amount paid in this state during the taxable year by the taxpayer for compensation and the denominator of which is the total compensation paid both within and without this state during the taxable year. The payroll factor shall

¹⁰ The phrase "preponderance of substantive contact" used in Section 5(g)(1)(B) to locate loans and credit card receivables requires further definition normally left for inclusion in regulations supporting the statute. Regulatory language is suggested at Appendix D.

include only that compensation which is included in the computation of the taxpayer's apportionable income tax base for the taxable year.

(b) Compensation relating to nonbusiness income and independent contractors.

The compensation of any employee for services or activities which are connected with the production of nonbusiness income (income which is not included in the apportionable income base) and payments made to any independent contractor or any other person not properly classifiable as an employee shall be excluded from both the numerator and denominator of the factor.

(c) When compensation paid in this state. Compensation is paid in this state if any one of the following tests, applied consecutively, is met:

(1) The employee's services are performed entirely within this state.

(2) The employee's services are performed both within and without the state, but the service performed without the state is incidental to the employee's service within the state. The term "incidental" means any service which is temporary or transitory in nature, or which is rendered in connection with an isolated transaction.

(3) If the employee's services are performed both within and without this state, the employee's compensation will be attributed to this state:

(A) if the employee's principal base of operations is within this state; or

(B) if there is no principal base of operations in any state in which some part of the services are performed, but the place from which the services are directed or controlled is in this state; or

(C) if the principal base of operations or the place from which the services are directed or controlled is not in any state in which some part of the service is performed but the employee's residence is in this state.

APPENDIX A.

Suggested Regulation - "Basis of information included in apportionment factors".

At the election of the taxpayer, the information used in the calculation of the apportionment factors as provided in Sections 4 through 6 [of the Act] may be based either upon information contained in the taxpayer's financial books and records (book basis) or in the taxpayer's federal income tax return (tax basis), so long such information used fairly represents the extent of the taxpayer's activities in the state. Once such election is made of either book basis or tax basis, such basis shall be used by the taxpayer for all future years, unless permission is obtained in writing from the State Tax Administrator to use another basis.

APPENDIX B

Suggested definition of "financial institution" - [The following definition of "financial institution" is offered solely as a guide for those states that wish to follow it. It is to be emphasized that the pending proposal is one that is designed to assign uniformly the net income of a financial institution as that term may be defined by a state.]

Term: Financial Institution.

"Financial institution includes:

- (a) Any corporation or other business entity registered under state law as a bank holding company or registered under the Federal Bank Holding Company Act of 1956, as amended, or registered as a savings and loan holding company under the Federal National Housing Act, as amended;
- (b) A national bank organized and existing as a national bank association pursuant to the provisions of the National Bank Act, 12 U.S.C. §§21 et seq.;
- (c) A federal savings and loan association;
- (d) Any bank or thrift institution incorporated or organized under the laws of any state;
- (e) A mutual savings bank incorporated or organized under the laws of the United States or of any state;
- (f) Any corporation organized under the provisions of 12 U.S.C. 611 to 631.
- (g) Any agency or branch of a foreign depository as defined in 12 U.S.C. 3101;
- (h) A credit union;
- (i) A production credit association organized under the Federal Farm Credit Act of 1933, all of whose stock held by the Federal Production Credit Corporation has been retired;
- (j) Any corporation whose voting stock is more than fifty percent (50%) owned, directly or indirectly, by any person or business entity

described in subsections (a) through (i) above other than an insurance company taxable under [insert applicable state statute] or a _____ company taxable under [insert applicable state statute];

(k) A corporation or other business entity that derives more than fifty percent (50%) of its total gross income from financial accounting purposes from finance leases. For purposes of this subsection, a "finance lease" shall mean -

any lease transaction which is the functional equivalent of an extension of credit and that transfers substantially all of the benefits and risks incident to the ownership of property. The phrase shall include any "direct financing lease" or "leverage lease" that meets the criteria of Financial Accounting Standards Board Statement No. 13, "Accounting for Leases" or any other lease that is accounted for as a financing by a lessor under generally accepted accounting principles.

For this classification to apply,

(i) the average of the gross income in the current tax year and immediately preceding two tax years must satisfy the more than fifty percent (50%) requirement; and

(ii) gross income from incidental or occasional transactions shall be disregarded; or

(l) Any other person or business entity which derives more than fifty percent (50%) of its gross income from activities that a person described in subsections (b) through (i) above is authorized to transact. For the purpose of this subsection, the computation of gross income shall not include income from nonrecurring, extraordinary items.

APPENDIX C.

Suggested Regulation - "Gross rents described." (Section 3.(i)).

"Gross rents" shall include, but not be limited to:

(1) any amount payable for the use or possession of real property or tangible property whether designated as a fixed sum of money or as a percentage of receipts, profits or otherwise,

(2) any amount payable as additional rent or in lieu of rent, such as interest, taxes, insurance, repairs or any other amount required to be paid by the terms of a lease or other arrangement, and

(3) a proportionate part of the cost of any improvement to real property made by or on behalf of the taxpayer which reverts to the owner or lessor upon termination of a lease or other arrangement. The amount to be included in gross rents is the amount of amortization or depreciation allowed in computing the taxable income base for the taxable year. However, where a building is erected on leased land by or on behalf of the taxpayer, the value of the land is determined by multiplying the gross rent by eight and the value of the building is determined in the same manner as if owned by the taxpayer.

(4) The following are not included in the term "gross rents":

(i) amounts payable as separate charges for water and electric service furnished by the lessor;

(ii) amounts payable as service charges, such as janitorial services, furnished by the lessor;

(iii) amounts payable for storage, provided such amounts are payable for space not designated and not under the control of the taxpayer; and

(iv) that portion of any rental payment which is applicable to the space subleased from the taxpayer and not used by it.

APPENDIX D.

Suggested Regulation - "Preponderance of substantive contact for locating certain loans and credit card receivables; presumption." (Section 5(g)(1)(B)).

(1) In order to determine the state in which loans or credit card receivables are properly booked under the "preponderance of substantive contact" test for the purpose of locating said property under Section 5(g)(1)(B), consideration is to be given to such things as: solicitation, investigation, negotiation, approval and administration. 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.

(B) *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 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.

(C) *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.

(D) *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.

(E) *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.

(2) In applying the standards for determining the state to which a loan is to be located, a preponderance of substantive contact shall be presumed, subject to rebuttal, to exist at a taxpayer's regular place of business to which it has been booked, if the loan is approved and administered there.¹¹

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¹¹ *It was urged by some of the industry representatives that a presumption or convention of sorts be adopted to reduce the opportunity for more than one state to assign the same loan or credit card receivable to itself. Since the suggested property factor favors money-center state assignment for intangible property, the suggested preference here is consistent with that approach.*

ATTACHMENT 2.

STATE/INDUSTRY MEETING GROUP ON FINANCIAL INSTITUTIONS

Convener: Alan Friedman,
Multistate Tax Commission

Alternate Convener: Fred E. Ferguson
Karen J. Boucher
Arthur Andersen

STATE PARTICIPANTS

<u>Name</u>	<u>Agency</u>
Eric Coffill	California Franchise Tax Board
Ed Campion	California Franchise Tax Board
Gerald Goldberg	California Franchise Tax Board
Ben Miller	California Franchise Tax Board
John Libby	Connecticut Department of Revenue Services
Rod Felix	Florida Department of Revenue
John Malach	Illinois Department of Revenue
Barbara Phillips	Indiana Department of Revenue
Mark Beshears	Kansas Department of Revenue
Thomas Sheridan	Kansas Department of Revenue
Virgil J. Brady	Louisiana Department of Revenue
Michael E. Boekhaus	Minnesota Department of Revenue
Bill Lunka	Minnesota Department of Revenue
Stanley R. Arnold	New Hampshire Department of Revenue

Maurice Gilbert	New Hampshire Department of Revenue
Daniel H. Levine	New Jersey Department of Taxation
Marilyn N. Kaltenborn	New York Department of Taxation and Finance
Deborah Liebman	New York Department of Taxation and Finance
Richard Garrison	New York Department of Taxation and Finance
Bill Ryan	New York Department of Taxation and Finance
James W. Wetzler	New York Department of Taxation and Finance
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Michael Hyman	New York City Department of Finance
Jonathan R. Robin	New York City Department of Finance
Jerry Rosenthal	New York City Department of Finance
William Thomas	New York City Department of Finance
Ashley C. Morris	North Carolina Department of Revenue
Heidi Heitkamp	North Dakota Tax Department
Ron Schreiner	South Dakota Department of Revenue
James Fry	South Dakota Department of Revenue
Anne Dougherty	Tennessee Department of Revenue
Wade Anderson	Texas Comptroller of Public Accounts
Steve Zegalo	Washington Department of Revenue

Keith Larson

West Virginia Department of Tax and Revenue

Monitoring for Co-sponsor
Federation of Tax
Administrators:

Harley Duncan and
Mary Jane Egr

Federation of Tax Administrators

INDUSTRY PARTICIPANTS

<u>Name</u>	<u>Company or Association</u>
Henry Ruempler	American Bankers Association
Joanne Ames	American Bankers Association
Philip M. Plant	Bank of America NT & SA
Dan S. Lazar	Bank of New York Company, Inc.
Paul Buchman	Bank of New York Company, Inc.
Marty Linzer	Bankers Trust Co.
Harry Montgomery	Bankers Trust Co.
Robert Godwin	Boatmen's Bancshares Inc.
Joseph L. Taetle	Chase Manhattan Bank, N.A.
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Michael J. Palko	Great Western Financial Corporation
Brad Ellison	Great Western Financial Corporation
Nancy Worman	KeyCorp
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Allan B. Lubarsky	Morgan Guaranty Trust Co. of NY

Myron Rosenberg

Brent C. Andersen

Haskell Edelstein

John H. Kasser

Terry J. Baker

Jonathan W. Allen

Morgan Guaranty Trust Co. of NY

NationsBank

Price Waterhouse & Co. (formerly
Citicorp/Citibank, N.A.)

South Holland Trust & Savings Bank
Group, Inc.

SunTrust Banks, Inc.

Wachovia Corporation

ATTACHMENT 3.

NOTICE OF PUBLIC HEARING

NOTICE OF PUBLIC HEARING

The Multistate Tax Commission will hold three sessions of a public hearing on the following subject:

The development and adoption of Proposed Multistate Tax Commission Regulation VI.18.(i) dealing with the attribution of income from the business of financial institutions.

To this end, the Hearing Officer will receive public input in person and in writing from all interested persons addressing the following matters:

1. *What is the most appropriate definition of the terms "financial institution" and "business of a financial institution" for the purpose of statutory or regulatory coverage of the different kinds of financial institutions that are in substantial competition with one another?*
2. *Should the receipts factor reflect the delivery of a financial institution's services on a destination basis or on a majority of "cost of performance" basis?*
3. *How should states treat intangible property in the form of unsecured or secured loans, investments in securities, etc. for income attribution purposes?*
4. *With regard to states that apply the unitary business principle and combined reporting, what, if any, approach should the proposal take with regard to such principles.*
5. *What, if any, approach should the proposal take with regard to nexus and/or de minimis concepts?*
6. *Should a throwback, throwout or another approach be used to address the attribution of receipts that are sourced to states in which the taxpayer is not subject to taxation?*
7. *Such other issues and suggestions that state representatives and other members of the taxpaying community may wish to present for consideration.*

A copy of the most recent draft version of the proposed uniform statute/regulation (MTC Reg.IV.18.(i)) may be obtained on and after May 13, 1993 by writing or calling:

Teresa Moore
Multistate Tax Commission
444 North Capitol St., N.W.
Washington, D.C. 20001
Phone: (202)-624-8699

The Hearing Officer that has been assigned to this matter is:

Alan H. Friedman, General Counsel
Multistate Tax Commission
386 University Avenue
Los Altos, CA 94022
Phone: (415)-941-0556

The two public sessions will be held at the locations, dates and times specified as follows:

1. Thursday, May 27, 1993, beginning at 10:00 a.m. at the Ronald Reagan State Office Building, 300 South Spring Street, Los Angeles, California, first floor Auditorium.
2. Thursday, July 15, 1993, beginning at 10:00 a.m. at the Hall of the States, 444 No. Capitol St., N.W., Room 333, Washington, D.C.

A third public session will be held in New York in late summer and supplemental public notice will be made of the date, time and specific location of that session.

The Multistate Tax Commission invites all interested parties to participate in the public sessions of this hearing. Those desiring to make oral presentations to the Hearing Officer must notify him in writing at least two working days prior to the holding of the public session. An attempt will be made to accommodate those who wish to present oral testimony but are unable to travel to the location for the public sessions. Any person desiring to testify by use of telecommunications should make that desire known at the time he/she discloses an interest in making a presentation. Depending upon feasibility, an attempt will then be made to assign specific time slots to those parties requesting the opportunity to testify by telecommunications. Anyone desiring to submit written comment may do so by submitting them to the Hearing Officer at any time prior to the last date for public session or such later date as may be announced for the closing of the public hearing.

EXHIBIT E: 3

**Partial and Interim Report of Hearing Officer
(April 12, 1994)**

Multistate Tax Commission



PARTIAL AND INTERIM REPORT OF HEARING OFFICER REGARDING THE APPORTIONMENT OF INCOME FROM THE BUSINESS OF A FINANCIAL INSTITUTION

I NATURE OF THIS REPORT

The following is a partial and interim Report of Hearing Officer which presents certain information to the Executive Committee of the Multistate Tax Commission regarding a uniform method by which the net income from the business of a financial institution should be apportioned. This is a "partial" report in that it sets forth the bare bones of the uniformity proposal recommendation developed thus far through the public hearing process and leaves out the history of the proposal, a review of the public input and reasons for the recommendations. This is an "interim" report because a full Final Report will be submitted to the Executive Committee and the final wording of the uniformity proposal will likely vary in some regard to that presented here.

The reason that this Partial and Interim Report is being submitted now is to provide those interested states an early opportunity to review the proposal in its near-final form should those states have pending or prospective legislative or regulatory efforts. The final wording of the proposal may change somewhat with the issuance of the Final Report; and any public distribution of this Partial and Interim Report should clearly note the final steps that remain before any proposal becomes a Commission recommendation. It is anticipated that the Final Report of Hearing Officer will be presented to the Executive Committee before its meeting on May 6, 1994.

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II
UNIFORMITY RECOMMENDATION IN PROGRESS

Subject to the possibility that changes may be made to the proposed uniformity recommendation by the Hearing Officer in the Final Report of Hearing Officer, the Hearing Officer recommends that should a state have a current or prospective need to consider legislative or regulatory language addressing the apportionment of net income from the business of a financial institution, that such state should consider the language contained in Attachment 1 to this Partial and Interim Report. Attachment 1 is the mark-up version of that reflects by strikeout and underlining the changes that the Hearing Officer has made thus far from the version that was developed through the Multistate Tax Commission/Federation of Tax Administrators State/Industry Meetings Group. The Hearing Officer has not attached a clean copy (one without the mark-up notations) of this version, since it represents "work-in-progress" at this time.

The Executive Committee should note in particular the alternative language set forth below regarding Section 2(s), the definition of "taxable" and "taxable in another state". Also set forth below is alternative language for Section 6 (b) that addresses the circumstance where more than one state seeks assignment of the identical item of payroll, property or receipt.

The two alternatives addressing the definition of "taxable " or "taxable in another state" are as follows:

ALTERNATIVE 1:

(s) **"Taxable"** means that a taxpayer is subject to a franchise tax measured by net income, a net income tax, a franchise tax for the privilege of doing business, or an apportioned corporate stock or earned surplus tax in another state.

ALTERNATIVE 2:

(s) **"Taxable in another state"** means that a taxpayer is either:

(1) subject to a franchise tax measured by net income, a net income tax, a franchise tax for the privilege of doing business, or an apportioned corporate stock or earned surplus tax in another state; or

(2) that state has jurisdiction to subject the taxpayer to a net income tax regardless of whether, in fact, the state does or does not do so.

Alternative 1 operates as a full throwback of receipts to the state of commercial domicile when, due to any reason, the receipts are not taken into the market state's receipts factor. This result, consistent with a request by South Dakota, approximates the result that would be required under UDITPA's assignment of 100% of the receipts that arise from the sale of services to the state in which the majority of costs of performance occurred.

Alternative 2, the version that was offered through the State/Industry Meetings (SIMS) process, would treat the receipts of financial institutions as if they were received from the sale of tangible personal property under UDITPA. This approach would throw back the receipts from services to the state of commercial domicile only when the market state has no jurisdiction over the financial institution; and even when it does have such jurisdiction, if the market state does not impose any tax obligation on the financial institution, the receipts will still not be thrown back. In this event, less than 100% of the receipts are assigned to the states.

As noted in Attachment 1, the Hearing Officer has favored Alternative 1 - the approach that approximates the treatment that the financial institutions would have received had UDITPA applied to their receipts as arising from the sales of services, not of goods.

The two alternatives for Section 6(b) set forth below address situations where two or more states seek assignment to their respective numerators of the identical payroll, property or receipt are as follows:

ALTERNATIVE 1:

(b) When it appears that this state and one or more other states that have adopted the same or substantially similar provisions to those contained in [this Act] have included or will include the same receipt, property or payroll in their respective factor numerators, at the written request of the taxpayer, this state shall confer with such other state or states to discuss which state should be properly assigned said receipt, property or payroll. Such conference shall identify what law, regulation or written guideline, if any, has been adopted in each state with respect to the issue.

(1) In discussing a conflict as to which state is to receive the assignment of any receipt at issue, a preference shall be given to assigning said receipt to the state in which the customer, borrower or other payor of the receipt is located, unless to do so (i) would clearly conflict with any law, regulation, or written guideline of this state; and (ii) would not clearly reflect the income-producing activity of the taxpayer within this state.

(2) In discussing a conflict as to which state is to receive the assignment of any property in the form of any loan or credit card receivable at issue, a preference shall be given to the state in which the taxpayer's commercial domicile is located, unless to do so (i) would conflict with any law, regulation, or written guideline of this state and (ii) would not clearly reflect the income-producing activity of the taxpayer within this state.

ALTERNATIVE 2:

(b) When it appears that this state and one or more other states that have adopted the same or substantially similar provisions to those contained in [this Act] have included or will include the same receipt, property or payroll in their respective factor numerators, at the written request of the taxpayer **and upon a showing that such inclusion has or will result in more than 100% of the taxpayer's net income being subjected to taxation**, this state shall confer with such other state or states to discuss which state should be properly assigned said receipt, property or payroll. Such

conference shall identify what law, regulation or written guideline, if any, has been adopted in each state with respect to the issue.

(1) In discussing a conflict as to which state is to receive the assignment of any receipt at issue, a preference shall be given to assigning said receipt to the state in which the customer, borrower or other payor of the receipt is located, unless to do so (i) would clearly conflict with any law, regulation, or written guideline of this state; and (ii) would not clearly reflect the income-producing activity of the taxpayer within this state.

(2) In discussing a conflict as to which state is to receive the assignment of any property in the form of any loan or credit card receivable at issue, a preference shall be given to the state in which the taxpayer's commercial domicile is located, unless to do so (i) would conflict with any law, regulation, or written guideline of this state and (ii) would not clearly reflect the income-producing activity of the taxpayer within this state.

As noted on Attachment 1, the Hearing Officer has included Alternative 1, however the Hearing Officer has not reached a conclusion as to favoring one alternative approach over the other. Alternative 1 is set forth in Attachment 1 because it parallels a similar suggestion that the Hearing Office had earlier made with respect to the states' interpretations of Public Law 86-272. See paragraph VI. of Attachment 1 to the Final Report of Hearing Officer Regarding Public Law 86-272 Statement. It is requested that the Executive Committee select one of the two alternatives for the purpose of including the preferred one in the Bylaw 7 surveys of the member states with respect to both this proposal and the Public Law 86-272 proposal.

While there are additional changes from the SIMS version that the Hearing Officer is recommending (most of which have relatively little apportionment impact), the Sections 2(s) and 6(b) alternatives are set out here because they both substantially differ from that offered through the SIMS process. In light of these particular recommended changes, as well as others that either the state or industry participants to SIMS or any other interested person might wish to comment upon, the Hearing Officer recommends that the Executive Committee remain open to the receipt of

additional written comments on the recommendation as it progresses toward final Executive Committee and/or Commission action.

This Partial and Interim Report is submitted to the Executive Committee of the Multistate Tax Commission this 12th day of April, 1994.



Alan H. Friedman
Hearing Officer

EXHIBIT F

**PARTICIPANT LISTS AND AGENDAS:
STATE/INDUSTRY MEETING GROUP (SIMS)**

EXHIBIT F: 1

**Statement by Dan R. Bucks, Executive Director
Multistate Tax Commission to State/Industry Meetings**

STATEMENT TO STATE/INDUSTRY MEETING
MULTISTATE TAXATION OF FINANCIAL INSTITUTIONS

by

Dan R. Bucks, Executive Director, Multistate Tax Commission

Much of the discussion of methods of apportioning income earned in the financial industry has focused on the topic of the distribution of income shares among the states. Specifically, the industry, and to a lesser degree, some states have discussed this topic in terms of "market states" vs. "supply states."

This issue is easily overemphasized as compared to other issues. Questions of nexus standards, enforceability and ease of administration are among those that ought to be given major consideration as well. Indeed, if enforceability of an apportionment method is not considered along with the distributional question, assumptions about how income would be distributed among market and supply states can prove to be entirely wrong in actual practice.

For example, if an apportionment method is expected to distribute 75% of income on a supply factor basis and 25% on a market factor basis, but 50% of the income actually evaporates into thin air because the apportionment mechanism is unenforceable, then only 37.5% of the income will be distributed to supply factors, 12.5% to market factors and 50% to "nowhere land." Such a distribution is clearly less acceptable than an apportionment method that distributes 50% of the income to supply factors, 50% to the market and is enforceable to the point where 90% of the income will be reported. In that case 45% of the income would be distributed to supply factors, 45% to market factors and 10% to "nowhere land." Enforceability must be considered as a part of the apportionment question to minimize gaps between intended and actual distributions of income.

Every state is, to a greater or lesser degree, both a market and supply state. Consequently, distribution formulas should be discussed in terms of their use of market and supply factors or elements. Discussing formulas in terms of being either "market state" or "supply state" formulas is misleading because there is no such thing as a 100% market state or supply state -- there are only degrees of market and supply states.

More importantly, the degree of market or supply activities within each state is subject to significant change for this industry. The financial industry, aided by contemporary electronic technologies, is a highly mobile and rapidly changing industry. What today is considered to primarily a market state for financial services can quickly become a predominantly supply state. South Dakota, for example, underwent just such a

transition in a few years in the late seventies and early eighties. Current legislation authorizing interstate banking will likely accelerate changes in the location of activities for this industry. Thus, assumptions about how apportionment formulas may affect particular states can be -- no, most likely will be -- undermined by economic changes in the financial industry. If change is considered the rule for this industry, the most prudent policy perspective for states to adopt may be to favor apportionment formulas that are enforceable and that reflect both supply and market factors in some balanced way so that substantial swings in revenue do not occur as economic conditions change.

I think there is a need for some greater precision in the discussion of apportionment formulas. In particular, I would note that the proposal the MTC submitted to hearing has been characterized by some observers as a "market state approach." I think that characterization is inaccurate. The formula in that proposal includes a payroll factor and a sales factor that each give a 33% weight respectively to supply and market factors. The property factor gives weight to both supply and market elements. Tangible property and securities are distributed on a supply basis (with securities and passive investments distributed on a deposits formula), and loans are distributed on a market basis. Thus, the degree to which the property factor is balanced between market and supply factors depends on the distribution of assets between, on the one hand, tangible property and securities, and on the other hand, loans. If there is a 50/50 distribution of these assets within the industry or an enterprise, the proposal submitted to hearing would distribute income on an approximately 50/50 basis between supply and market factors as follows:

DISTRIBUTIONAL IMPACT OF PROPOSAL AT HEARING*

FACTOR	SUPPLY	MARKET
Payroll	33%	
Property	17%	17%
Sales		33%
TOTAL	50%	50%

*The numbers in the table are based on the assumption that the combined value of tangible property and securities is equal to the value of loans.

When discussed in somewhat more precise terms, the proposal submitted by the MTC to hearing cannot be characterized as a "market state" proposal. It is a mixed "supply/market" proposal,

with the degree of mix dependent upon particular economic facts. Regardless of what judgments any parties wish to make about distributional issues, I think we can make greater progress in arriving at an understanding of these topics if we discuss distributional questions in precise terms.

My comments on the proposal the MTC has submitted to hearing should not be interpreted as advocacy of that proposal to the exclusion of other proposals. The Commission does not advocate a position on state taxing methods until it adopts a uniformity recommendation, and we have not done so on this subject. The hearing stage, which is where the issue currently rests within the MTC, is a certain point in our policy development process. A hearing officers' final report, Executive Committee review of the report, and a survey of affected states lie ahead before a Commission votes on a recommendation for the taxation of financial institutions. At this stage, the MTC remains open to considering changes in the proposal at hearing and to alternative approaches.

The goal of the MTC in the financial institutions area, as in all other multistate tax policy issues, is to find common ground around which the maximum number of states can rally voluntarily. We are advocates of this goal and not, at this stage, of any particular policy position.

In summary, enforceability is a topic that needs to be addressed whenever distributional issues are considered. Economic change should be considered the rule, not the exception, and policy judgments should be made taking account of the reality of change. We should be as precise as possible in discussing any aspect of this subject, especially distributional issues. Finally, the MTC is seeking to find common ground for achieving the maximum degree of voluntary uniformity among the states on this issue.

EXHIBIT F: 2

**State/Industry Meetings (SIMS) Agenda
San Francisco, CA (July 15-16, 1991)**

MULTISTATE TAXATION OF FINANCIAL INSTITUTIONS

STATE/INDUSTRY MEETINGS (SIMS)

Sponsored By:

Multistate Tax Commission
Federation of Tax Administrators (Invited)

and

Financial Institutions State Tax Coalition
American Bankers Association

July 15 - 16, 1991
Price Waterhouse Offices
Bank of America Building
555 California Street
36th Floor Conference Room
San Francisco, California 94104
Telephone: 415/393-8500

FINANCIAL INSTITUTIONS SIMS AGENDA

Monday, July 15, 1991

1:30 - 2:45 p.m.

Introductions and Purpose

Conference Room
36th Floor

- o Introductions
- o Statement of Purpose
- o Approve Agenda
- o Agreement on Procedures
- o Dealing with Issues in Conflict
- o Other Administrative

Opening Comments

Brief opening comments by a representative of each sponsoring organization, including a statement of desired results from the Financial Institutions SIMS.

State Position Statements

Presentations of current positions of the MTC and representative states (e.g., California, Indiana, Iowa, Minnesota, New York, South Dakota, Tennessee, and West Virginia) with respect to the taxation of financial institutions and whether a different approach can be considered.

2:45 - 3:00 p.m.

BREAK

3:00 - 3:45 p.m.

Industry Position Statement

Conference Room
36th Floor

FIST Alternative and ABA Alternative

Presentation by FIST and ABA of alternative proposals to the current state approaches and the MTC proposed regulation.

3:45 - 5:30 p.m.

Discussion of the Issues

Conference Room
36th Floor

State and industry members to discuss the policy and technical issues raised by FIST and ABA alternative and current approaches being taken by the states.

Assignment of Issues to SIMS Subcommittees

State and industry members will volunteer for and be assigned to smaller groups to meet on Tuesday morning to refine the major policy and technical issues that remain to be addressed.

5:30 p.m.

ADJOURNMENT

6:00 p.m.

RECEPTION

Bank of America Building
The Carnelian Room
52nd Floor

7:00 p.m.

DINNER (On Own)

Tuesday, July 16, 1991

8:30 - 9:00 a.m.

CONTINENTAL BREAKFAST

Conference Room
36th Floor

9:00 - 12:00 Noon

SIMS Subcommittee Meetings

Conference Rooms
35th, 36th, and
38th Floors

Members of these subcommittees shall meet in an effort to reach a consensus or clear definition of issues remaining to be addressed through more discussions and technical drafting. It is anticipated that these subcommittees will operate in a dialogue mode with respect to these issues, but, if time permits, a

Financial Institutions SIMS
AGENDA
July 15 - 16, 1991
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drafting attempt could also be made (even if the policy issues still remain open).

12:00 Noon - 1:30 p.m. **LUNCH BREAK (On Own)**

1:30 p.m. - 3:15 p.m. SIMS Committee of Whole

Conference Room
36th Floor

A representative of each SIMS Subcommittee shall provide a short report on the efforts, recommendations and conclusions of the respective Subcommittees. After the reports are given, a general discussion of the issues raised shall be conducted.

3:15 - 4:00 p.m.

Wrap-up and Decision as to Where to Go From Here

Conference Room
36th Floor

This discussion will focus on whether there remains enough prospect for reaching some acceptable common approach on the substantive issues to warrant the creation of a SIMS Technical Drafting Subcommittee to draft one or more alternative proposals for consideration. A second Financial Institutions SIMS meeting has been reserved for:

December 4 - 5, 1991
New York, NY

EXHIBIT F: 3

**State/Industry Meetings (SIMS) Agenda
New York, NY (April 29-30, 1992)**

MULTISTATE TAXATION OF FINANCIAL INSTITUTIONS

STATE/INDUSTRY MEETINGS (SIMS)

Sponsored By:

Multistate Tax Commission
Federation of Tax Administrators

and

Financial Institutions State Tax Coalition
American Bankers Association

COMBINED MEETING

April 29, 1992, 1:30 p.m. - 5:30 p.m. and

April 30, 1992 8:30 a.m. - 5:00 p.m.

Doral Inn - Washington Room, 6th Floor

541 Lexington Avenue at 49th Street

New York, New York 10022

Telephone: 212/755-1200, ext. 145

Fax: 212/753-9288

FINANCIAL INSTITUTIONS SIMS FINAL AGENDA

Wednesday, April 29, 1992

9:00 a.m. - 12:00 Noon

Pre-Meeting Caucuses

State Representatives -

Doral Inn
Lincoln Room
6th Floor

Industry Representatives -

Price Waterhouse Offices
Glass Conference Room
39th Floor

State and New York City representatives meet together in the Lincoln Room, 6th Floor of the Doral Inn. Industry representatives meet together in the Glass Conference Room, 39th Floor of the Price Waterhouse Offices. The joint meeting between State and Industry representatives may begin as soon as both groups are ready. The joint meeting will begin no later than at 1:30 p.m.

12:00 Noon - 1:30 p.m.

LUNCH BREAK (ON OWN)

1:30 p.m. - 3:00 p.m.
Doral Inn
Washington Room
6th Floor

Purpose and Administrative

- o Welcome by Co-Chairs
- o Introductions
- o Statement of Purpose
- o Administrative Matters

Opening Comments and Position Statements

Brief opening comments to be made by each participant attending regarding current position on the state uniformity efforts and expectations regarding those efforts.

3:00 p.m. - 3:15 p.m.

BREAK

3:15 p.m. - 5:30 p.m.
Doral Inn
Washington Room
6th Floor

Presentation and Discussion of Report of State
Subcommittee on Apportionment of Income from
Financial Industry

The background and substance of the Report of State Subcommittee will be presented for discussion.

Financial Institutions SIMS
FINAL AGENDA
April 29 - 30, 1992
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5:30 p.m.

ADJOURNMENT

6:00 p.m. - 7:00 p.m.
Doral Inn
Washington Room
6th Floor

RECEPTION

7:00 p.m.

DINNER (ON OWN)

Thursday, April 30, 1992

8:30 a.m. - 9:00 a.m.

CONTINENTAL BREAKFAST

Doral Inn
Washington Room
6th Floor

9:00 a.m. - 10:30 a.m.

Discussion of Report of State Subcommittee
(Continued)

Doral Inn
Washington Room
6th Floor

10:30 a.m. - 10:45 a.m.

BREAK

Financial Institutions SIMS
FINAL AGENDA
April 29 - 30, 1992
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10:45 a.m. - 12:00 Noon
Financial Industry

Doral Inn
Washington Room
6th Floor

Discussion of Alternative Approaches to Taxation of

State and Industry representatives are invited to present and discuss any additional approaches or processes by which to achieve a fair, technically sound and administrable result in the taxation of multistate financial services.

12:00 Noon - 1:30 p.m.

LUNCH BREAK (ON OWN)

1:30 p.m. - 3:15 p.m.

Discussion of Alternative Approaches to Taxation of
Financial Industry (Continued)

Doral Inn
Washington Room
6th Floor

3:15 p.m. - 3:30 p.m.

BREAK

3:30 p.m. - 3:32 p.m.
(Alan's suggested time)

Discussion of Respective State and Industry
Positions on Congressional Preemption of State
Taxation of Financial Industry

Doral Inn
Washington Room
6th Floor

Financial Institutions SIMS
FINAL AGENDA
April 29 - 30, 1992
Page 5

3:32 p.m. - 5:00 p.m.

Doral Inn
Washington Room
6th Floor

Wrap Up and Decision as to Where to Go From
Here

This discussion will focus on whether, based upon the meetings, there remains enough prospect for reaching some acceptable common approach to warrant the creation of a State/Industry Technical Drafting Subcommittee to refine the current suggested approaches or to draft one or more alternative proposals for consideration at a future meeting. If so, the Subcommittee should be selected and given its direction. If not, the participants will be invited to state their positions and intentions.

5:00 p.m.

ADJOURNMENT

fist:sims0492:fnlage.nyc

MULTISTATE TAXATION OF FINANCIAL INSTITUTIONS
STATE/INDUSTRY MEETINGS (SIMS)

April 29-30, 1992

STATE PARTICIPANTS
As of 4/20/92

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Fax: 203/566-6403

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Secretary of Revenue

Kansas Department of Revenue
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Thomas Sheridan
Administrator

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John Malach
Chairman, Board of Appeals

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Virgil J. Brady
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Stanley R. Arnold
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Maurice Gilbert
Director of Audit

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Chief, Office of Tax Analysis**

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**James W. Wetzler
Commissioner**

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**North Dakota Tax Department
State Capitol
600 East Boulevard Ave.
Bismarck, ND 58505-0599
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**Heidi Heitkamp
Tax Commissioner**

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**Pennsylvania Department of Revenue
1141 Strawberry Square
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**Kathleen Belson
Director, Bureau of Policy**

South Dakota

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Ron Schreiner
Secretary

Texas

Tax Administration
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Mary Jane Egr
Research Attorney

EXHIBIT F: 4

**State/Industry Meetings (SIMS) Agenda
Chicago, IL (November 23-24, 1992)**

MULTISTATE TAXATION OF FINANCIAL INSTITUTIONS

State/Industry Meeting
Conference Room, Arthur Andersen & Co.
One State Street
Chicago, IL
November 23-24, 1992

AGENDA**November 23, 1992****8:30 AM - 10:30 AM**

GOVERNMENT AND INDUSTRY REPRESENTATIVES TO MEET SEPARATELY. THE JOINT MEETING MAY BEGIN AS SOON AS BOTH GROUPS ARE READY. IF BOTH GROUPS ARE NOT READY TO MEET EARLIER, THE JOINT MEETING WILL BEGIN AT 10:30 AM.

10:30 AM - 11:00 AM

WARM-UP, ADMINISTRATIVE MATTERS AND REVIEW OF GENERAL PROGRESS

11:00 AM - NOON

PRESENTATION AND DISCUSSION OF DRAFT DEFINITIONS

NOON - 1:00 PM LUNCH BREAK

WORKING LUNCH PROVIDED - DISCUSSION OF DRAFT DEFINITIONS CONTINUED OVER LUNCH

1:00 PM - 1:30 PM BREAK**1:30 PM - 2:00 PM**

PRESENTATION OF DRAFT OF PAYROLL FACTOR BY CO-LEADERS OF TEAM 15 AND DISCUSSION

2:00 PM - 3:15 PM

PRESENTATION OF DRAFT OF RECEIPTS FACTOR BY CO-LEADERS OF TEAM 18 AND DISCUSSION

3:15 PM - 3:30 PM BREAK**3:30 PM - 5:30 PM**

COMPLETION OF DISCUSSION OF RECEIPTS FACTOR DRAFT

November 24, 1992

8:30 AM - 10:00 AM

PRESENTATION OF DRAFT OF PROPERTY FACTOR BY CO-LEADERS OF TEAM 16 AND DISCUSSION

10:00 AM - 10:15 AM BREAK

10:15 AM - NOON

COMPLETION OF DISCUSSION OF PROPERTY FACTOR DRAFT

PRESENTATION OF DEPOSITS/SOURCE OF FUNDS FACTOR DRAFTS BY CO-LEADERS OF TEAM 7/17 AND DISCUSSION

PRESENTATION OF REPORTS OF TEAMS 19 (RECORDKEEPING BURDEN) AND 21 (BOOK VS. TAX BASIS REPORTING)

NOON - 1:00 PM LUNCH BREAK (ON OWN)

1:00 PM - 3:00 PM

WRAP UP AND DECISION AS TO WHERE TO GO FROM HERE.

Throwback

Nexus

Combination/Consolidation

Other outstanding issues

Format and process for statute or rule adoption

3:00 PM ADJOURN AND HEAD TO O'HARE

NOTE: OUR AGENDA IS QUITE TIGHT AND THIS WILL BE THE FIRST OPPORTUNITY YOU WILL HAVE TO COMMENT ON DRAFTS ON WHICH YOU HAVE NOT HAD EARLIER INPUT. NOW IS THE TIME FOR YOUR COMMENTS; HOWEVER, IN ORDER TO MAINTAIN A SENSIBLE SCHEDULE, WE SHOULD NOT TURN THE MEETING INTO A TECHNICAL DRAFTING SESSION. ANY SUBSTITUTE LANGUAGE YOU WISH TO PRESENT SHOULD BE SUBMITTED IN WRITING TO FRED AND BE EITHER AT OR SHORTLY AFTER THE CHICAGO MEETING FOR PROPER ROUTING TO THE RESPECTIVE TEAM CO-LEADERS.

EXHIBIT G

**AGENDA: MTC/FTA FINANCIAL INSTITUTIONS
BUSINESS WORKSHOP**

FINANCIAL INSTITUTIONS BUSINESS WORKSHOP
CO-SPONSORED BY THE MULTISTATE TAX COMMISSION
AND THE FEDERATION OF TAX ADMINISTRATORS

Grand Hyatt Hotel
Washington, DC

October 8 -9, 1991

AGENDA

Tuesday, October 8, 1991

8:00 AM - 4:30 PM

I. INTRODUCTION TO WORKSHOP

II. BANKING BUSINESS BASICS

This introductory session builds upon the participant's basic understanding of the banking business.

Topics include:

The changing definition of banking

Financial statements in the banking industry

Banking profitability

III. RETAIL BANKING

This session reviews the business and profitability issues involved in retail banking.

Topics include:

Consumer lending

Direct vs. indirect

Secured v. unsecured

Real estate

Credit card operations

Deposit gathering

Electronic banking

ATMs

Point-of-sale (POS) systems

LUNCH BREAK (WORKING LUNCH)

IV. WHOLESALE BANKING

This session addresses the unique services that banks provide to their corporate customers.

Topics include:

Corporate finance

Corporate lending

Loan participations

Factoring

Asset-based financing

Leasing

Commercial real estate

Fee-generating activities

Service products

Cash management

Funds transfer

International banking

Letters of credit

Bankers acceptances

Investment banking

Commercial paper

LBOs and HLTs

Securitization

Underwriting

V. TRUST SERVICES

This session treats the various trust and securities processing services provided by banks.

Topics include:

Agent services

Personal services

Institutional trusts

Asset management

Global custody

VI. TREASURY FUNCTIONS

This session deals with the functions of the internal treasury department of a bank.

Topics include:

Trading

Securities

Foreign exchange

Asset/liability management

U.S. Treasuries

Fed funds

Repurchase agreements

Wednesday, October 9, 1991

8:00 AM - 12:30 PM

VII. OPERATIONS AND ADMINISTRATION

This session addresses the issues on the operational side of a bank in dealing with tax and audit requirements.

VIII. INCOME AND ASSET REPORTING

This session addresses some of the accounting and regulatory reporting aspects of banking.

Topics include:

Balance sheet and income statement analysis

SEC, GAAP and regulatory requirements

IX. STRUCTURE AND REGULATION

This session reviews the more significant of the federal regulatory agencies that oversee bank operations, soundness and various reporting requirements.

Topics include:

Comptroller of the Currency

Federal Reserve Board

FDIC

Securities Exchange Commission

Reports filed with the regulators

Structure of banks (holding company, subsidiaries and their activities)

Risk-based rules regarding capital

X. U.S. OPERATIONS OF FOREIGN BANKS

This session deals with foreign bank activities in the U.S.

LUNCH BREAK (ON YOUR OWN)

**THE REMAINDER OF THE WORKSHOP SHALL BE LIMITED
TO GOVERNMENT REPRESENTATIVES ONLY**

1:30 PM - 5:00 PM

XI. CURRENT AND EVOLVING ISSUES

This session deals with the issues faced by federal and state tax auditors in reviewing bank records.

XII. DISCUSSION AND EVALUATION OF INFORMATION

The government representatives will evaluate the information provided in the Workshop and discuss the next steps to be taken in the development of state taxation approaches to financial institutions.

RECEPTION (5:30 PM - 7:00 PM)

WORKSHOP LEADERS

Sessions II. through VI.

**Banking Business Basics, Retail Banking,
Wholesale Banking, Trust Services, Treasury Functions**

GREGORY GUNTHER: *President, Enhanced Communications, Inc. (ECI), a designer and presenter of training courses in the financial institutions industry. ECI has presented various training courses to institutions including American Banker, American Express, Chase Manhattan Bank, Chemical Bank, Dun and Bradstreet, First Interstate, J.P Morgan, Norwest, and Price Waterhouse.*

Session VII.

Operations and Administration

SUNIL ANTANI

Executive Vice-President, MNC Financial

Session VIII.

Income and Asset Reporting

LARRY ASHMORE

First Vice-President, SunTrust Bank

Session IX.

Structure and Regulation

EUGENE W. GREEN:

**Deputy Chief Accountant
Office of the Chief Accountant
Comptroller of the Currency**

Session X.

U.S. Operations of Foreign Banks

JOHN L. CARR, ESQ: *Shaw, Pittman, Potts & Trowbridge and contributing author to International Financial Law and Regulation of Foreign Banks in the United States*

Session XI.

Current and Evolving Audit Issues

RICHARD FLEMING: *Bank Specialist, Internal Revenue Service*

EDWARD CAMPION: *Tax Audit Specialist
California Franchise Tax Board*

ROLAND SADOWSKY: *Corporate Tax Auditor III
New York State Department of Taxation and Finance*

Session XII.

Discussion and Evaluation of Workshop Information

HEIDI HEITKAMP: *Tax Commissioner, State of North Dakota*

HARLEY DUNCAN: *Executive Director
Federation of Tax Administrators*

MARILYN KALTENBORN: *Chief of Tax Regulations
New York Department of Taxation and Finance*

ERIC COFFILL: *Senior Staff Counsel, Multistate Tax Affairs
California Franchise Tax Board*

ALAN FRIEDMAN: *General Counsel
Multistate Tax Commission*

ADDITIONAL WORKSHOP RESOURCES

C. JAMES JUDSON, ESQ.:

Davis Wright Tremaine, Lawyers; Chairman of the firm's Business Law Group; frequent lecturer and author in areas of federal and state tax issues concerning financial institutions; editor of American Bar Association's State Taxation of Banking Institutions; member and past Chairman of ABA Committee on Banking and Savings Institutions, ABA Tax Section.

Mr. Judson has agreed to provide his expert services throughout the entirety of the Workshop. He will provide his comments and respond to your questions as to any of the subjects where it might be necessary to further illustrate or complement the session presentations. Mr. Judson's experience in the financial industry's transactional side permits him to provide the "color" commentary to many of the subjects dealt with in the Workshop.

WORKSHOP MATERIALS

Reading of the "Banking is Business" manual in advance of the Workshop is strongly recommended for all of the participants. While it may present new information for some and a basic refresher for others, it will provide a common place upon which many of the Workshop sessions will be based. Please note that although some portions of the manual contemplate the doing of workshop-type exercises, time does not permit us to engage in that type of training. You will receive additional written materials when you arrive at the Workshop that will assist you in following the fairly quick-paced presentations that will be presented.