

ANALYSIS OF SUGGESTED ADDITION TO SEC. 18 (c) – As proposed by the Hearing Officer and adopted for implementation by the Executive Committee with one modification.

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July 14, 2014

Article IV.18 -- AS REVISED BY THE UNIFORMITY COMMITTEE AND ACCEPTED BY THE EXECUTIVE COMMITTEE – WITH H.O. SUGGESTION IN RED (emphasis added).

(a) If the allocation and apportionment provisions of this Article **do not fairly represent the extent of the taxpayer's business 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.

(b) (1) If the allocation and apportionment provisions of this Article **do not fairly represent the extent of business activity in this State of taxpayers engaged in a particular industry or in a particular transaction or activity**, the tax administrator may, in addition to the authority provided in section (a), establish appropriate rules or regulations for determining alternative allocation and apportionment methods for such taxpayers.

(2) A regulation adopted pursuant to this section **shall be applied uniformly, except** that with respect to any taxpayer to whom such regulation applies, **the taxpayer may petition for, or the tax administrator may require, adjustment pursuant to Section 18(a)**.

(c) The party petitioning for, or the [tax administrator] requiring, the use of any method to effectuate an equitable allocation and apportionment of the taxpayer's income pursuant to (a), must prove: **(1) that the allocation or apportionment provisions of this Article do not fairly represent the extent of the taxpayer's activity in this State; and (2) that the alternative to such provisions is reasonable**. The same burden of proof shall apply whether the taxpayer is petitioning for, or the [tax administrator] is requiring, the

use of any reasonable method to effectuate an equitable allocation and apportionment of the taxpayer's income.

THE EXECUTIVE COMMITTEE'S INSTRUCTION TO THE UNIFORMITY COMMITTEE (as captured in Sheldon's memo to the committee):

Adopt the Hearing Officer's proposed Art.IV.18(c), which would impose the burden of proof on the party (either the taxpayer or the tax administrator) seeking to apply an alternative apportionment of the taxpayer's income. The Executive Committee also indicated that the burden of proof should be placed on the taxpayer if the revenue department applied alternative apportionment as a result of the taxpayer's changing its long-standing filing status.

ALTERNATIVE SUGGESTION TO ADDRESS "LONGSTANDING" ISSUE:

In addition to the two alternatives already proposed, I propose the following to address the long-standing filing status issue:

"Notwithstanding the foregoing, if the tax administrator can show that in any three of the prior five tax years, the taxpayer had used an allocation or apportionment method or methods other than those required by this Article or rules or regulations issued pursuant to subsection (b), then the tax administrator shall not bear the burden of proof in imposing a different method pursuant to (a)."

Chiefly, this has the advantage of creating a bright-line rule.

ANALYSIS OF BEN MILLER'S SUGGESTED ADDITION:

Ben states in his letter to the Uniformity Committee:

The recommendation of the Hearing Officer to add a subsection (c) to address the question of the burden of proof and state that it applies to both the taxpayer and the tax administrator is appropriate and follows the practice and judicial decisions of the states collectively.

An additional subsection might be added to state that the adoption of a rule or regulation by the tax administrator after appropriate hearings meets the burden of proof that the standard provisions do not fairly reflect represent the activities of the taxpayer in this state. My suggested language is

(c)(2) Adoption of a regulation after hearing pursuant to subsection 18(b) shall be presumed to meet the burden of proof as provided for in subsection 18(c)(1).

This addition was not called for by the executive committee and appears unnecessary. By proposing his additional language Ben suggests that it is not clear already from subsection (b) that “the adoption of a rule or regulation by the tax administrator after appropriate hearings meets the burden of proof that the standard provisions do not fairly reflect represent the activities of the taxpayer in this state.” There are two problems with this suggestion.

First, (b), as proposed by the Uniformity Committee and adopted by the Executive Committee, imposes its own “burden” for promulgating a valid regulation. It states: *If the allocation and apportionment provisions of this Article do not fairly represent the extent of business activity in this State of taxpayers engaged in a particular industry or in a particular transaction or activity, the tax administrator may, in addition to the authority provided in section (a), establish appropriate rules or regulations for determining alternative allocation and apportionment methods for such taxpayers.* Whatever the burden may be on the tax administrator to show that the regulation is valid, it is embedded in this provision. Assuming the regulation is valid, and applicable to the taxpayer, I believe there should be no question as to whether by following the regulation, the tax administrator has also met his burden under (c), which is identical.

Second, Ben’s addition logically only makes sense if the tax administrator is seeking to apply the regulation to the taxpayer. But (b) gives the tax administrator the authority to apply the regulation already. If, instead, the tax administrator is seeking to vary from the rule in the applicable regulation, which is what (c) addresses, then the burden in (c)(i) is *not* to show that the regulation is valid under (b)’s standard, but to show that the *variation* from the regulation is necessary to achieve fair apportionment. That burden could not possibly have been met by promulgating the regulation.