MEMORANDUM

To: Income and Franchise Tax Uniformity Subcommittee
   Wood Miller, Chairman, Income and Franchise Tax Subcommittee;

From: Bruce Fort, Counsel, Multistate Tax Commission

Date: July 17, 2009

Subject: Proposed Amendment to Model Regulation IV.18.(a); Use of Equitable Apportionment Formulas

The Income Tax and Uniformity Subcommittee last addressed this issue at a June 3, 2009 teleconference. Two new versions of proposed modifications to the current regulation were presented at that conference in an effort to see if agreement could be reached by the states. The teleconference produced spirited debate and discussion once again but no votes were taken. The teleconference ended with a request from the Chair that representatives should continue to discuss the matter with their respective agencies and that they should be prepared to take a binding vote on whether to recommend one of the two proposals to the full uniformity committee at our annual meeting on July 27th. Those two proposals are listed below.

Once again, the states have expressed general agreement that the current model regulation is overly restrictive in allowing the use of equitable apportionment, but the states have not agreed to a formula which would allow more leeway in applying equitable apportionment and have not come to agreement on how much latitude should be allowed to administrators and taxpayers.

It should be noted that many members of the subcommittee have also requested model language incorporating burdens of proof and procedural rules for invoking the provisions of Section 18. The drafting committee did not include language addressing those proposals since it was felt that the proposals might complicate the resolution of the still-undecided substantive question of what restrictions the regulation should contain.

The first proposal retains the requirement for an “unusual” fact pattern in granting use of an alternative formula, while the second proposal eliminates that requirement but retains the phrase “only in limited and specific cases.” A copy of our current model
regulation is reprinted below with the paragraph which would be replaced by the modified language highlighted.

Current Model Regulation:

Reg. IV.18.(a). Special Rules: In General. Article IV.18. provides that if the allocation and apportionment provisions of Article IV 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.

Article IV.18. permits a departure from the allocation and apportionment provisions of Article IV only in limited and specific cases. Article IV.18. may be invoked only in specific cases where unusual fact situations (which ordinarily will be unique and non recurring) produce incongruous results under the apportionment and allocation provisions contained in Article IV.

In the case of certain industries such as air transportation, rail transportation, ship transportation, trucking, television, radio, motion pictures, various types of professional athletics, and so forth, the foregoing regulations in respect to the apportionment formula do not set forth appropriate procedures for determining the apportionment factors. Nothing in Article IV.18. or in this Regulation IV.18. shall preclude [the tax administrator] from establishing appropriate procedures under Article IV.10. to 17. for determining the apportionment factors for each such industry, but such procedures shall be applied uniformly.

Latest Proposals (From June 3, 2009 teleconference):

1. Article IV.18 permits a departure from the allocation and apportionment provisions of Article IV only where unusual factual situations produce incongruous results under the apportionment and allocation provisions contained in Article IV.

2. Article IV.18 permits a departure from the allocation and apportionment provisions of Article IV only in limited and specific cases where the apportionment and allocation provisions contained in Article IV produce incongruous results.