

## ADDITIONAL INFORMATION FOR THURSDAY'S MEETING

To facilitate this week's call, the following detailed information is provided:

### Status Summary:

The committee is continuing work on Issue No. 2 on the checklist. Issue No. 2 concerns whether specific restrictions should be imposed on a taxpayer's ability to change its method of sourcing receipts on a prospective basis – as reflected in proposed draft amendment Reg. IV.17(a)(7)(D) located here (**on page 68**) [http://www.mtc.gov/getattachment/Uniformity/Project-Teams/Public-Hearing-3-2016/Hearing-Officer-Report-General-Allocation-and-Appportionment-Regs-\(revised\).pdf.aspx](http://www.mtc.gov/getattachment/Uniformity/Project-Teams/Public-Hearing-3-2016/Hearing-Officer-Report-General-Allocation-and-Appportionment-Regs-(revised).pdf.aspx)

The Hearing Officer's Report found the Sec. 17(a)(7)(D) restrictions unnecessary and recommended removing them. The committee voted to reject the Hearing Officer's recommendation. It separately voted to retain the restrictions as originally drafted.

The committee nevertheless discussed providing the executive committee with an alternative. So it was agreed that at the coming meeting the committee would address: the requirements for accuracy, notice, and documentation, as well as the connection between the first and second sentence of the provision at issue, whether (D) might simply reference the requirements of (C), and if the accuracy requirement is removed from (D), should it also be removed from (E).

### Information Received Subsequent to the Last Meeting:

Michael Fatale, Massachusetts, who is unable to be on the call this week, has sent the following proposal (reproduced here) for an alternative for the executive committee:

I think offering a fallback position to the executive committee in the event that the executive committee does not want to reject the hearing officer's report on subsection (D) (what we have been speaking about) makes sense (although I have already voted to reject the hearing officer's proposed changes to subsection (D) as a threshold position).

The fallback position that I would offer – consistent with what I think Phil Skinner and Phil Horwitz both seemed to advocate yesterday – is eliminating all of subsection (D) (i.e., not merely sentences 2-4 as the hearing officer suggested, but sentences 1-4). If subsection (D) is stricken, subsection (E) can simply be renumbered as subsection (D). That would be a simple way of accommodating the hearing officer's proposal. I agree with the comments from yesterday to the effect that retaining the first sentence by itself would be problematic. I previously made that point in a prior call and it is documented in prior minutes. I don't think the hearing officer had any intention to invite the problems that the committee is concerned about, so I think this proposal fairly comports with his proposal.

That said, my first preference with respect to the fallback position would be to strike sentences 1-4 of subsection (D), **but to nonetheless retain the included notice provision (see suggestion below)**. That of course is a less simple proposal and is at odds with the hearing officer's comments, but I think may find support in the committee – a number of persons, even those who have questioned the accuracy notion, have supported the notice concept.

My one other point is that some persons have suggested accommodating the hearing officer's comments, but also making a comparable change striking the accuracy requirement as set forth in subsection (E) and perhaps otherwise editing subsection (E). I would not make any changes to subsection (E), in part because I

don't think they are necessary and also because I think that our fallback position should try to hue as closely as possible to the hearing officer's proposal.

PROPOSED NEW LANGUAGE IN SUBSECTION (D), WITH REDLINE VERSION BELOW:

Taxpayer Authority to Change a Method of Assignment on a Prospective Basis. A taxpayer that seeks to change its method of assigning its receipts must disclose, in the original return filed for the year of the change, the fact that it has made the change. If a taxpayer fails to adequately disclose the change the [tax administrator] may disregard the taxpayer's change and substitute an assignment method that the [tax administrator] determines is appropriate.

Taxpayer Authority to Change a Method of Assignment on a Prospective Basis. [OUT: In filing its original return for a tax year, a taxpayer may change its method of assigning its receipts under Reg. IV.17, including changing its method of approximation, from that used on previous returns. However, the taxpayer may only make this change for purposes of improving the accuracy of assigning its receipts consistent with the rules set forth in Reg. IV.17, including, for example, to address the circumstance where there is a change in the information that is available to the taxpayer as relevant for purposes of complying with these rules. Further, a] A taxpayer that seeks to change its method of assigning its receipts must disclose, in the original return filed for the year of the change, the fact that it is has made the change [OUT: , and must retain and provide to the [tax administrator] upon request documents that explain the nature and extent of the change, and the reason for the change.] If a taxpayer fails to adequately disclose the change [OUT: or retain and provide the required records upon request,] the [tax administrator] may disregard the taxpayer's change and substitute an assignment method that the [tax administrator] determines is appropriate.”

Michael shared this proposal with Phil Horwitz, Colorado, who will also be unable to be on this week's call, and Phil has communicated that he supports Michael's proposal.

In addition, other members of the committee have noted that there are other places in the existing model regulations that require disclosure of changes in methods of reporting:

- Reg. IV.1.(d)(2) (see at page 41 of the Hearing Officer Report) – concerning proration of deductions between apportionable and non-apportionable income.
- Reg. IV.2.(c) (see at page 45 of the Hearing Officer Report) – concerning classification of income as apportionable or non-apportionable income.
- Reg. IV.10.(c) (see at page 49 of the Hearing Officer Report) – concerning valuation of property for the property factor.
- Reg. IV.15.(a)(2) (see at page 58 of the Hearing Officer Report) – concerning the exclusion or inclusion of gross receipts in the receipts factor.

Also, there is another provision of the Sec. 17 draft amendments that imposes specific requirements on the selection of the method of market-sourcing:

Reg. IV.17(a)(4), states:

“In order to satisfy the requirements of Reg. IV.17, a taxpayer's assignment of receipts from sales of other than tangible personal property must be consistent with the following principles:

(A) A taxpayer shall apply the rules set forth in Reg. IV.17 based on objective criteria and shall consider all sources of information reasonably available to the taxpayer at the time of its tax filing including, without limitation, the taxpayer's books and records kept in the normal course of business. A taxpayer shall determine its method of assigning receipts in good faith, and apply it consistently with respect to similar transactions and year to year. A taxpayer shall retain

contemporaneous records that explain the determination and application of its method of assigning its receipts, including its underlying assumptions, and shall provide those records to the [Agency ] upon request.

(B) Reg. IV.17 provides various assignment rules that apply sequentially in a hierarchy. For each sale to which a hierarchical rule applies, a taxpayer must make a reasonable effort to apply the primary rule applicable to the sale before seeking to apply the next rule in the hierarchy (and must continue to do so with each succeeding rule in the hierarchy, where applicable). For example, in some cases, the applicable rule first requires a taxpayer to determine the state or states of assignment, and if the taxpayer cannot do so, the rule requires the taxpayer to reasonably approximate the state or states. In these cases, the taxpayer must attempt to determine the state or states of assignment (i.e., apply the primary rule in the hierarchy) in good faith and with reasonable effort before it may reasonably approximate the state or states.

(C) A taxpayer's method of assigning its receipts, including the use of a method of approximation, where applicable, must reflect an attempt to obtain the most accurate assignment of receipts consistent with the regulatory standards set forth in Reg. IV.17, rather than an attempt to lower the taxpayer's tax liability. A method of assignment that is reasonable for one taxpayer may not necessarily be reasonable for another taxpayer, depending upon the applicable facts.

These requirements will continue to apply regardless of what the committee decides to do with respect to Reg. IV.17(a)(7)(D).