

Multistate Tax Commission

Multistate Tax Commission
386 University Avenue
Los Altos, CA 94022
Phone (415) 941-0556
Fax (415) 941-0557



ALAN H. FRIEDMAN, General Counsel

Multistate Tax Commission
444 North Capitol St., N.W.
Suite 500
Washington, D.C. 20001
Phone (202) 624-8699

REPORT OF HEARING OFFICER REGARDING PROPOSED ADOPTION OF MULTISTATE TAX COMMISSION REGULATION IV.18.(h) (Television and Radio Broadcasting)

On April 25, 1988, 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 a proposed allocation and apportionment regulation pertaining to the television and radio broadcasting industry. On June 9, 1988 an initial public hearing was held in Los Angeles, California; and, upon additional written notice, all interested parties were invited to submit additional written testimony or submissions through and including April 30, 1989.

Bylaw No. 7 of the Multistate Tax Commission requires the Hearing Officer to submit to the Commission a report which shall contain a synopsis of the hearing proceedings and a detailed recommendation for Commission action. In the case of a hearing held pursuant to Article VII(2) of the Compact, the recommendation of the Hearing Officer is to include a proposed draft of the regulation which is the subject matter of the hearing. Pursuant to these requirements, this Report is divided into three parts. The first is a synopsis of the public hearing proceedings which were held. The second part is a brief discussion of the major substantive issues to be addressed. The third part is the Hearing Officer's recommendation for Commission action concerning the possible adoption of the proposed regulation IV.18.(h).

I

SYNOPSIS OF PUBLIC PROCEEDINGS

A. Notice.

A Notice of Public Hearing was published in the Multistate Tax Review, Vol. 1988, No. 1 (May, 1988), and mailed to member state Tax Administrators. This Notice of Public Hearing called for a public hearing to be held on June 9, 1988 at the offices of the California Franchise Tax Board, 624 South Grand Avenue, 9th Floor, Los Angeles California beginning at 10:00 A.M. An additional Notice of Hearing was published in the Multistate Tax Review, Vol. 1989, No. 1 (March 1989) and mailed to Tax Administrators providing notice that written submissions would be considered if received on or before April 21, 1989.

B. Material Submitted for the Record.

The hearing, in accordance to the Notice of Public Hearing, was called to order at approximately 10:00 A.M. on June 9, 1988 by Alan Friedman, General Counsel to the Multistate Tax Commission, who presided as Hearing Officer for the Commission. There were five persons in attendance at the hearing: Earl T. Hammond, Twentieth Century Fox Film Co.; Paul Thompson, Fox Broadcasting Co.; Douglas Jaques, McDermott, Will & Emery; John S. Warren, Loeb & Loeb; Bradley S. La Couer, California Franchise Tax Board; and Benjamin F. Miller, California Franchise Tax Board. The oral statements of these persons were tape recorded; and the recordings, which are made a part of the record, are available for review upon request to the Multistate Tax Commission.

The following written materials were considered by the Hearing Officer and made a part of this record:

Exhibit 1.

A copy of the Executive Committee's Resolution dated April 25, 1988 and the proposed Regulation IV.18 (h) as originally presented for the hearing.

Exhibits 2.a., 2.b., and 2.c.

Notices of Public Hearing dated April 26, 1988 provided to the states.

Exhibit 3.

Notice of Public Hearing published in the Multistate Tax Review, Vol. 1988, No. 1 (May, 1988).

Exhibits 4.a. - 4.g.

Specific Notices of Public Hearing sent to industry representatives.

Exhibits 5.a. and 5.b.

a. Notice of Public Hearing published in the Multistate Tax Review, Vol. 1989, No. 1 (March 1989).

b. Tentative draft of proposed regulation dated 1/30/89.

Exhibits 6.a. and 6.b.

a. California FTB Regulation 25137-8: Motion Picture and Television Film Producers and Television Networks - Apportionment of Income.

b. California Franchise Tax Commission Rulemaking File: Regulation 25137-8 (2 vols.). (Due to the size of Exhibit 6.b, only its Index is reproduced here. Any person desiring to review the contents of Exhibit 6.b. may do so by contacting the Multistate Tax Commission.)

Exhibits 7.a. and 7.b.

a. California Guideline for Motion Picture and Television Film Producers and Television Network Broadcasters Apportionment Formula.

b. Various correspondence and memoranda contained in the California Franchise Tax Board files regarding the development of its Guideline for Motion Picture and Television Film Producers and Television Network Broadcasters Apportionment Formula.

Exhibits 8.a., 8.b. and 8.c.

a. New York State Department of Taxation and Finance TSB-M-81(19)C (11-20-81).

b. New York State Department of Taxation and Finance
TSB-M-86(4)C (5-19-86).

c. New York State Department of Taxation and Finance
Regulation (20 NYCRR) Section 4-4.3(f)(2).

Exhibit 9.

Pages 29 - 31 of Volume 5 of the New Jersey Tax Policy
Committee Report of February 23, 1972.

Exhibit 10.

Letter dated May 3, 1988 from Harold Aldinger,
Supervisor, Corporate Income Tax Section, Office of North
Dakota State Tax Commissioner.

Exhibits 11.a. and 11.b.

a. Letter dated May 10, 1988 from Benjamin F. Miller,
Director, Multistate Tax Affairs, California Franchise
Tax Board.

b. Letter dated June 8, 1988 from Benjamin F. Miller,
Director, Multistate Tax Affairs, California Franchise
Tax Board.

Exhibit 12.

Letter dated June 20, 1988 from Thomas C. Nardozzi,
Director, Tax Administration, National Broadcasting
Company, Inc.

Exhibit 13.

Letter dated June 20, 1988 from James M. Goldberg, Vice
President, Taxes, Capital Cities/ABC, Inc.

Exhibits 14.a., 14.b. and 14.c.

a. Letter dated June 7, 1988 from Alvan L. Bobrow,
Senior Tax Counsel, CBS, Inc.

b. Letter dated February 22, 1989 from Alvan L. Bobrow,
Senior Tax Counsel, CBS, Inc.

c. Letter dated February 28, 1989 from Alvan L. Bobrow,
Senior Tax Counsel, CBS, Inc.

II

SUBSTANTIVE ISSUES TO BE ADDRESSED

During the course of the proceedings, the industry, as well as the states, raised several concerns of substance. The following provides a brief explanation of the more substantive issues raised by the proposal.

A. Retroactivity.

Originally, the proposed regulation contained an effective date of application to income years beginning on or after January 1, 1984. Industry representatives unanimously objected to the regulations being applied on a retroactive basis. See Exhibits 12., 13., and 14.a. During the course of the proceedings the Hearing Officer released for public comment, a version of the proposed regulation that deleted reference to the date of its application. And, the final version recommended herein is void of any suggested date for its application.

The impacts of modern technology upon the methods by which goods and services are now being produced and delivered have placed a strain on the ability of the traditional UDITPA provisions to properly address the income now being earned by several industry groups. Specialized apportionment regulations for the non-mercantile, non-manufacturing industries are increasingly made necessary if the states and business segments are to apportion the income derived from within the states in a fair, reasonable and uniform manner. Reasonable people certainly can differ regarding any particular substantive provision contained in an apportionment regulation. But, few would differ as to the wisdom of adopting written regulations to govern the unique and difficult tax apportionment issues raised by specialized industries not involving mercantile or manufacturing businesses.

For those states that may have audit or administrative

proceedings currently pending, it is the Hearing Officer's conclusion that the modification provisions contained in Article IV.18. of the UDITPA and Multistate Tax Compact contain sufficient authority, even in the absence of a specific regulation, to support application of a modified formula to specialized industries, such as the network broadcasting industry. Article IV.18. authorizes states to employ a modified method of apportionment of broadcasting income derived from advertising revenues when the advertising is read or viewed and acted upon in the taxing state to create a market. See, Amerada Hess Corp. v. Conrad, 410 N.W.2d 1214 (N.D. 1987); and Twentieth Century-Fox Film Corporation v. Department of Revenue, 299 Or. 220, 700 P.2d 1035 (1985). Therefore, the Hearing Officer wishes to emphasize that the deletion of any recommended retroactive application date does not imply that the Hearing Officer concludes that the apportionment methodology contained in the proposed regulation could not be applied to tax years currently open to audit. The intent of the recommended deletion of a specific effective date from the proposed regulation here simply recognizes that each state considering the proposed regulation should determine under its own state laws and policies when to apply the principles of the regulation.

B. Sales Factor.

The proposed regulation creates an apportionment approach measured, in part, upon the size of the in-state viewing or listening audience in relation to the size of the taxpayer's over-all audience. The reasonableness of this apportionment methodology has been judicially supported. See, Twentieth Century-Fox Film Corporation v. Department of Revenue, 299 Or. 220, 700 P.2d 1035 (1985) (motion picture viewing audience used to apportion cost of film properties); and Metromedia, Inc. v. Director, Division of Taxation, 478 A.2d 742 (N.J. 1984) (apportionment of television income based on viewer audience considered by the Court to be a

reasonable method, but adoption by regulation found required).

In order for any income apportionment formula to be found consistent with the Commerce Clause of the United States Constitution, it must meet the standards of "internal" and "external" consistency discussed in the United States Supreme Court's decision in Container Corporation of America v. Franchise Tax Board, 463 U.S. 159 (1983). An apportionment formula is internally consistent if, assuming that it were applied in every jurisdiction, the formula would result in no more than all of a taxpayer's business income being subject to taxation. The "external" consistency standard is described by the Supreme Court as follows:

"... The second and more difficult requirement is what might be called external consistency--the factor or factors used in the apportionment formula must actually reflect a reasonable sense of how income is generated. The Constitution does not 'invalidat[e] an apportionment formula whenever it may result in taxation of some income that did not have its source in the taxing State ... Nevertheless, we will strike down the application of an apportionment formula if the taxpayer can prove 'by clear and cogent evidence' that the income attributed to the State is in fact 'out of all appropriate proportions to the business transacted in that State,' ... or has 'led to a grossly distorted result'."

The proposed sales factor apportionment methodology, based upon a viewing audience approach, is substantially similar to the method for apportioning television network receipts adopted by both California and New York. See, Cal. F.T.B. Reg. 25137-8 (Ex. 6.a.) and NYCRR 4-4.3(f)(2) (Ex.8.c.). Since both California and New York are the home states for a majority of the motion picture and broadcasting industries, their income allocation approaches are critical to ensure that the proposed regulation does not subject the taxpayers at issue to an unreasonable risk of double taxation of the same income. The Hearing Officer finds that the proposed

regulation does not create such an unreasonable risk and is consistent with both the external and internal consistency standards required to be met in order to pass constitutional muster.

Lastly, the regulation as originally proposed used an audience factor to apportion receipts that was based upon the ratio of in-state population to United States population. Industry representatives argued that such a ratio was not substantially correlative to the receipts derived from the transmission of programming to the viewing audiences by the different networks. They suggest that data is available from independent sources such as Nielsen and Arbitron rating services and that such data consists of a more precise method of measurement of the extent and value of the networks' respective viewing and listening audiences. In this regard it is noted that A.C. Nielsen has recently announced the development of a "passive people meter", utilizing sonar and infrared heat sensing, that would more precisely measure audience shares. The Hearing Officer has concluded that the industry representatives' request that the sales factor be based upon viewing audiences as opposed to actual population is well taken and has modified the proposed regulation to provide accordingly.

C. Payroll Factor.

Section 25137-8(c)(2)(A)(ii) of the California Franchise Tax Regulations requires the taxpayer to include in the payroll factor payments made to a corporation for providing the services of an actor or director who is an employee of the unrelated payee corporation. California's rule treats payments to the unrelated payee corporation as equivalent to direct wage payments to the taxpayer's own employees. California's approach was apparently adopted in recognition of certain economic realities that exist in the entertainment business. Historically, no special rule was required for compensation paid to actors and directors for the

production of a film, because they were under direct employment contract with the motion picture studio or other producer of the film. Only recently have such talents created their own corporations apparently to achieve certain results under federal tax law.

The recent case of Lancaster Colony Corp. v. Limbach, 37 Ohio St. 3d 198 (Ohio 1988), supports in theory the approach taken by California and by the proposed regulations. In Lancaster Colony, the taxpayer manufactured goods, but had no sales force of its own. It sold its goods only through independent contractors. The Ohio Supreme Court approved the taxpayer's right to include in the payroll factor the commission's paid to the independent contractors. The Court concluded that such inclusion more fairly depicted the taxpayer's activities in Ohio.

The Hearing Officer believes that in order to assure as much uniformity in approach as practicable, the states should not stray too far from the statutory provisions contained in Article IV. of the Compact. Article IV.1.(c). limits the payroll factor to compensation paid to "employees for personal services". It does not specifically include payments made to independent contractors; and the Hearing Officer concludes that payments to non-employees for talent services should not be automatically included in the payroll factor as is the approach taken by the California regulation. However, because one major purpose of any apportionment formula is to fairly measure the taxpayer's activities within the taxing state, the regulation itself should recognize that under the appropriate showing, payment for talent services of independent contractors who had historically been employees of the film producers may be treated as equivalent of that paid to traditional employees. Therefore, the Hearing Officer has modified the proposed regulation to permit the inclusion of payments made for talent services of independent contractors in the payroll factor upon a showing that (i) such payments were substantial in light of all employee salaries paid

by the taxpayer and (ii) failure to include such payments would be unfairly distortive of the taxpayer's activities in the state.

It should be noted that the proposed regulation includes in the property factor the value of a "film" or radio property which in turn includes "payments for actors, newscasters, directors, crew and other similar services reasonably required for such production". See, Reg. IV.18.(h)(4)(ii)A.2.b. Therefore, the regulation, as recommended, already contains recognition of the cost of independent contractors' services in the formula. The Hearing Officer anticipates, therefore, that the additional inclusion in the payroll factor of the same cost for independent contractor services will be, with rare exception, distortive to the entire formula.

The Hearing Officer nevertheless recognizes that a possibility exists that a unique factual circumstance may properly be shown to warrant such additional inclusion of payments to independent contractors and the Hearing Officer does not want to preclude consideration of such a circumstance. However, in order to achieve practical uniformity among the states as to the exercise of discretion inherent in the modified proposal, the standard of proof should be "clear and convincing evidence" and not any lesser standard.

D. Property Factor.

The proposed regulation apportions the value of film and radio properties broadcast to more than one state by the same mechanism by which receipts are apportioned--an audience factor based upon the ratio of the in-state viewing or listening audience to the total U.S. viewing or listening audience. The type of property at issue, radio and television programming, is delivered most often by direct electronic transmission or by satellite to the taxpayer's in-state affiliate or owned station for either delayed or simultaneous broadcast to the in-state audience. It is argued

by representatives of the industry that the attribution of film properties to the viewing state is in derogation of the statutory provisions that attribute business activity "from the taxpayer's use of property to the state where the property is physically used." See Ex. 14.a., pp. 7-14.

Even assuming that no physical embodiment, such as a reel of film or an audio or video-tape is delivered to or created in the taxing state, the Hearing Officer finds that said tangible property is still "used" by the taxpayer in the viewing/listening state within the meaning of UDITPA and the Multistate Tax Compact's Art.IV.10. See, Communications Satellite Corporation v. Franchise Tax Board, 156 C.A.3d 726, 203 Cal. Rptr. 779 (1984), app. dism., 105 S.Ct. 1158 (1985) (a portion of satellite used, even though not physically present within the state, is to be included in the property factor.) This in-state "use" occurs through the transmission of the programming, either directly by the taxpayer or through its in-state affiliate or owned station, to the in-state audience. The Hearing Officer is compelled here to find that if the film property were not being "used" in the viewing state, it would not be seen there. Neither a dark television screen, nor a silent radio, generates any revenue for the networks.

E. Throw-Out of Outer-Jurisdictional Property.

The proposed regulation requires that "outer-jurisdictional" property be eliminated from the property factors. Outer-jurisdictional property includes property, such as orbiting satellites, which is not physically located in any one state, but which is used in the business being conducted by the taxpayer. The use of a "throw-out" approach is not yet judicially secure, because the approach has not been frequently used and/or legally challenged. In the only reported decision dealing with the propriety of a "throw-out" (affecting the sales factor), the Pennsylvania Supreme Court held that the pre-conditions relied upon

by the Department of Revenue for employing a throw-out adjustment were not authorized by the statute. See, Paris Manufacturing Company, Inc. v. Commonwealth of Pennsylvania, 505 Pa. 15, 476 A.2d 890 (1984). In that case, the Department of Revenue was attempting to adjust the sales factor upward by the throw-out of sales made in jurisdictions in which the taxpayer was not subjected to a tax; and the Department did not otherwise show that the standard formula did "not fairly represent the taxpayer's business activity" in Pennsylvania. Therefore, the proposed use of a throw-out with regard to a more or less typical manufacturing enterprise was rejected by the Court. That circumstance is quite different than that faced by the states here, as the broadcasting industry does not engage in the type of business activity that falls clearly within the traditional application of UDITPA apportionment provisions. In addition, the Hearing Officer concludes that a reasonable reading of UDITPA and Article IV. of the Multistate Tax Compact suggests that, with regard to the property factor, the drafters thereof did not intend the denominator of the property factor to include property that did not have a physical location within any state.

F. Discrimination.

One industry representative, CBS, Inc., suggests that the adoption of the proposed regulations will constitute a discriminatory action by the states and violate its First Amendment protection, because the regulation places a tax burden solely on the business activities conducted by radio, television and cable companies. It suggests that the regulation, to be constitutional, must also apply to businesses that are competitive and "functionally similar", such as magazine publishers, data-based retrieval system businesses, motion picture and television production companies and the like. See, Ex.14.a. and 14.b.; see also, "Examples and Further Discussion of Electronically

Transmitted Tangible Personal Property"¹ attached to Ex. 14.b.

Using First Amendment arguments against a form of state taxation is not without support in case law. See, Texas Monthly, Inc. v. Bullock, ___ U.S. ___, 109 S.Ct. 890 (1989); Arkansas Writers' Project v. Ragland, ___ U.S. ___, 107 S.Ct. 1722 (1987); and Minneapolis Star & Tribune Co. v. Minnesota Commissioner of Revenue, 460 U.S. 575 (1983). And, just recently, a New York appellate court held that it was an unconstitutional infringement upon a magazine publisher's First Amendment right not to afford it the same tax apportionment scheme (destination based) that was afforded to the television and radio media under 20 NYCRR 4-4.3(f)(2), discussed infra. See, McGraw Hill, Inc. v. State Tax Commission, Supreme Court of New York, Appellate Div. No. 57346 (May 11, 1989, slip. op.). Justice Mikoll's dissent in McGraw Hill, on the other hand, suggests reasons why no violation of the First Amendment occurs in applying differing tax treatment to print and electronic media that sell advertising.

The Hearing Officer recognizes that the First Amendment issue raised by CBS, Inc., at least with respect to the print media, is not without merit and currently presents an open question that will likely be subject to a subsequent judicial debate. It is neither the role nor the intention of the Hearing Officer to offer an opinion as to the constitutionality of the proposed regulation, other than to recognize that it will remain an open question until addressed by the U.S. Supreme Court in the context of an appropriately developed record. Since New York, effective January 1, 1982, amended its tax laws to treat alike both print and

¹. The Hearing Officer neither accepts nor rejects the characterization of the property that is electronically transmitted being "tangible personal property". Some may suggest that the type of property transmitted is tangible; others may suggest that it consists of intangible rights only. The character of the property transmitted by electronic means for the purpose of the proposed regulation is irrelevant. The relevant activity is the transmission of programming, however characterized, into the homes of the viewers or listeners.

electronic media which disseminate advertising (apportioning advertising receipts on a destination basis), no further challenge can be anticipated to arise in that state in the near future. This is especially true, so long as the apportionment approach suggested in the proposed regulations remains unadopted by the destination states. It is clear that so long as the states of destination of the advertisements do not assert a right to apportion the advertising receipts, the disseminators of advertising by print and electronic means will bear a disproportionately low tax burden. The proposed regulation simply offers the missing piece of the jig-saw puzzle--a piece that bridges the advertising receipts gap which is located between the two coasts of the United States.

The Hearing Officer further concludes that substantially the same allocation and apportionment mechanism that is proposed here is readily suited for the print media, as well as other disseminators of regional and national advertising. One of the recommendations made below is that the Multistate Tax Commission members begin determining the applicability of the proposed apportionment formula used here, or some derivative thereof, to other advertising disseminators. Without prejudging the outcome of that possible future effort, it may be that no sufficient basis will be found for treating the electronic media different from the print media in apportioning advertising income. But, even if no constitutional or other legal compulsion currently exists to treat the two media similarly in this context, the states may still determine that a destination based assignment of advertising revenue earned by any type of media constitutes a reasonable and fair measure of the income producing activity in the destination states.

III RECOMMENDATIONS OF HEARING OFFICER

One of the principal purposes of Article IV.18.(d). which permits "the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income", is the development of different rules to meet the varying circumstances raised by special industries. Further, Multistate Tax Compact Reg. IV.18.(a)., adopted in 1973, anticipated the very process in which the Commission is now engaged. It provides:

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 [based upon the traditional, equally-weighted three-factor formula] do not set forth the 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.

By the adoption of Art.IV.18., the state legislatures have delegated to the tax administrators the authority to fashion allocation and apportionment approaches through both ad hoc adjustments arising on audit and through the adoption of regulations. These changes in methodology were thought necessary to ensure for both the public and the taxpayers, alike, that reasonable approaches would be applied in those circumstances in which the traditional formula "do[es] not fairly represent the extent of the taxpayer's business activity" in the taxing state.

[The business activities engaged in by cable, television and radio networks involve the purchase or creation of programming in one or a few states that is used to deliver a viewing or listening audience in many other states for which advertising can be sold. The delivering of the advertising message via the

facilities of the network is the core business activity of the network. The physical location of the medium containing that message, while of some mechanical importance for purposes of its dissemination, is largely unimportant to the generation of income which is the subject of the tax allocation formula here presented. It is the size and character of the in-state viewing and listening audience that is directly related to the amount of receipts received by the network from its advertisers. Programming is, in the main, electronically transmitted to the viewing/listening states and is used therein by the network, through its owned and affiliated stations, to carry the network advertisers' messages to the audience; and it is that activity that forms the basis for the proposed regulation.

Based upon the above discussion, the Hearing Officer concludes that the standard allocation and apportionment provisions contained in Article IV. of UDITPA and of the Multistate Tax Compact, when applied to broadcasting by radio and television networks and the operations of the cable television industry, do not fairly represent the extent of their business activities in the viewing/listening states. This conclusion remains the same irrespective of whether one categorizes the transmission of program properties as "[s]ales of tangible personal property" (Art.IV.16.) or as "[s]ales, other than sales of tangible personal property" (Art.IV.17). The Hearing Officer also concludes that the approach taken under the proposed regulation is reasonable and advances the purposes sought to be achieved through the provisions of UDITPA and Article IV. of the Compact. Therefore, the Hearing Officer recommends that the Multistate Tax Commission adopt the proposed regulation, as it has been modified from its initial proposal (Exhibit 15).

Lastly, the Hearing Officer suggests that the Commission, through its Uniformity Committee, begin review of the possible apportionment, on a basis similar to that proposed here, of income derived from other business activities associated with the dissemination of advertising on a regional and nationwide basis. Additionally, if resources permit and the Uniformity Committee

were to determine the matter to be appropriate for review, the Hearing Officer also recommends that the Committee investigate the need for a comparable income apportionment regulation that would apply to the variety of newly developed information service businesses that deliver their products or services across state boundaries through the use of electronic means that cross state boundaries. The materials submitted by CBS, Inc. with Ex. 14.b. provide a good basis upon which to begin that process.¹

Respectfully submitted this 14th day of June, 1989.

Alan H. Friedman
Hearing Officer

¹. Notwithstanding the fact that the Hearing Officer has recommended a study for possible adoption of a destination based apportionment regulation with respect to industries claimed or found to be similar to the electronic media subject to the current proposal, the Hearing Officer is not suggesting that any constitutional compulsion exists to do so. The Hearing Officer merely believes that CBS, Inc.'s suggestions in this regard have been extremely well presented, forcefully argued, and deserving of serious study.

Multistate Tax Commission



**RESOLUTION OF THE MULTISTATE TAX COMMISSION
EXECUTIVE COMMITTEE REGARDING PUBLIC HEARING ON PROPOSED
TELEVISION AND RADIO BROADCAST REGULATION**

WHEREAS, the Uniformity Committee of the Multistate Tax Commission has considered and approved for public hearing a recommendation for a regulation under Article IV. of the Multistate Tax Compact relating to the allocation and apportionment of income earned by members of the television and radio broadcast industry; and

WHEREAS, the Executive Committee has now had the opportunity to review and consider the proposed Regulation and is in agreement with the recommendation of the Uniformity Committee that a public hearing be held under Article VII. of the Compact upon the proposal;

NOW, THEREFORE, BE IT RESOLVED that a public hearing upon the proposed Television and Radio Broadcasting Regulation, a copy of which is attached hereto, be held on the 9th day of June, 1988, or on such other date as may be determined by the Hearing Officer; and

BE IT FURTHER RESOLVED that Alan H. Friedman, General Counsel to the Commission, is hereby designated and appointed to act as Hearing Officer for said public hearing; and that he is directed to submit his report and recommendation to the Commission within a reasonable time after the completion of said public hearing.

Upon motion duly made and seconded, this Resolution was adopted by the Executive Committee of the Multistate Tax Commission on the 25th day of April, 1988.

MULTISTATE TAX COMMISSION

BY:

**Dan R. Bucks
Executive Director**

EXHIBIT

1

Headquarters Office:
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024
Telephone (303) 447-9815

New York Audit Office:
25 W. 43rd Street, Suite 212
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

Multistate Tax Commission



Multistate Tax Commission

Proposed Regulation

Television and Radio Broadcasting

Reg. IV.18.(). Special Rules: Television and Radio Broadcasting.

The following special rules are established in respect to the apportionment of income from television and radio broadcasting.

(1) **In General.** When a person in the business of conducting a television or radio network has income from sources both within and without this state, the amount of business income from sources within this state shall be determined pursuant to Article IV. of the Multistate Tax Compact and the regulations issued thereunder by this state, except as modified by this rule. This regulation shall also apply to independent television and radio stations to the extent they are members of a chain of commonly owned stations all of which operate as a network or all of which are unaffiliated with a network, but which operate collectively in purchasing properties for broadcast or in marketing airtime. This regulation applies to income years beginning on or after January 1, 1984.

(2) **Business and Nonbusiness Income.** For definitions, regulations and examples for determining whether income shall be classified as "business" or "nonbusiness" income, see Reg. IV.1.

(3) **Definitions.** The following definitions are applicable to the terms contained in this regulation, unless the context clearly requires otherwise.

(i) "Film" means the physical embodiment of a play, story or other literary, commercial, educational or artistic work, as a motion picture, a video tape, disc or other medium, except that it does not include news or sports films produced for telecast or video cassettes or discs intended for home viewing.

Each episode of a series of films produced for television shall constitute a separate "film" notwithstanding that the series relates to the same principal subject and is produced during one or more television seasons.

(ii) "Release date" means the date on which a film is placed into service. A film is placed into service when it is first telecast to the primary audience for which the film was created. Thus, a film is placed in service when it is first publicly telecast for entertainment, educational or other such purposes. Each episode of a television series is placed in service when it is first telecast. A film is not placed in service merely because it is completed and therefore in a condition or state of readiness and availability for telecast or, merely because it is telecast to prospective sponsors or purchasers, or is shown in preview before a select audience.

(iii) "Rent" shall include license fees or other similar payments for the telecast of films or the broadcast of radio programming.

(iv) A "subscriber" to a subscription television telecaster is the individual residence or other outlet which is the ultimate recipient of the transmission.

(v) "Tangible personal property" used in the business, whether owned or rented, shall include but not be limited to films, sets, props, wardrobes, and other similar equipment or property.

(vi) "Telecast" or "broadcast" means the transmission of an electronic signal by radiowaves or microwaves or by wires, lines, coaxial cables, wave guides or other conduits of communications.

(4) Apportionment of Business Income.

(i) In General. The property factor shall be determined in accordance with Regulation IV.10 through 12., the payroll factor in accordance with Regulation IV.13. and 14., and the sales factor in accordance with Regulation IV.15. and 16., except as modified by this regulation.

(ii) The Property Factor

A. In General.

In the case of rented studios, the net annual rental rate shall include only the amount of the basic or flat rental charge by the studio for the use of a stage or other permanent equipment such as sound recording equipment

and the like; except that additional equipment rented from other sources or from the studio not covered in the basic or flat rental charge and used for one week or longer (even though rented on a day-to-day basis) shall be included. Lump-sum net rental payments for a period which encompasses more than a single income year shall be assigned ratably over the rental period.

1. The value of films and radio programs shall

a. be the original cost of producing the film or radio program as determined for federal income tax purposes, before any adjustment for federal credits which have not been claimed for state purposes, and

b. include payments for actors, newscasters, directors and other similar services.

2. The value of a film shall not be included in the property factor until its release date.

3. Video cassettes and discs shall be included in the property factor at their inventory cost as shown in the taxpayer's books and records.

B. Property Factor Denominator.

1. All real property and tangible personal property (other than films), whether owned or rented, which is used in the business shall be included in the denominator of the property factor.

2. Films, other than films the cost of which is expensed for this state's tax purposes at the time of production, shall be included in the property factor at original cost for twelve years beginning with the release date.

3. Films and radio programming of a topical nature, including news or current event programs, sporting events or interview shows, the cost of which is expensed for this state's tax purposes at the time of production, shall be included in the property factor at original cost for one year in the year of the release date.

4. All films or radio programming, other than those included in the denominator under clause 2. or 3. of this subparagraph, shall be aggregated and treated as a

single film property and included in the property factor. Such property shall be valued at eight times the gross receipts generated during the income year from network television or radio, television or radio syndication, cable television, subscription television, the marketing of video cassettes and discs through licensing or direct selling or similar receipts from the distribution of said film or radio property; but in no event in an amount greater than the total original cost of such aggregated film or radio property.

C. Property Factor Numerator.

1. If tangible personal property (other than films or radio programming and property otherwise specifically provided for subparagraph C.3. of this subsection) is located or used in this state for part of the income year, it shall be included in the numerator of the property factor at a value determined by applying the ratio which the number of days the property is located or used in this state bears to the total number of days such property was owned or rented during the income year. If such information cannot be determined accurately from records maintained by the taxpayer, the ratio shall be same ratio as determined pursuant to subparagraph 2. hereof.

2. The total value of films or radio programs that are included in the property factor under subparagraph B. of paragraph (ii) hereof shall be attributed to this state in the same ratio in which the total receipts in this state from such films and radio programming, as determined in subparagraphs 1., 2., and 3. of paragraph B. of this subsection pertaining to the sales factor, bears to the total receipts everywhere.

3. The value of certain types of tangible personal property that are used in this state, but are not located in any particular state, such as orbiting satellites, undersea transmission cables and the like (hereafter referred to as "outer-jurisdictional" property), that is to be attributed to this state shall be determined by applying to the total value thereof the property factor percentage determined under subparagraphs C.1. and 2. of this subsection without the inclusion of the value of such outer-jurisdictional property in the computation under said subparagraphs.

Example: XYZ Television Network Co. has a total value of its property everywhere, including a \$50,000,000 satellite that was used to telecast programs into this state, of \$500,000,000. The total value of real and tangible personal property located in this state for the entire income year was valued at \$2,000,000.00; the mobile property described in subparagraph C.1. was determined to be of a value of \$4,000,000; and such mobile property was used in this state for 100 days.

The total value of all the films described in subparagraph C.2 was \$300,000,000.00 and the receipts factor for this state has been determined to be .03. The total value of property to be attributed to this state would be determined as follows:

Value of property permanently in state: \$ 2,000,000

Value of mobile property 100/365 or
(.2739) x \$4,000,000: \$ 1,095,600

Value of films apportioned to this state
(.03 x \$300,000,000.00): \$ 9,000,000

Total value of property attributable
to state without apportionment of
satellite property: \$12,095,600

Value of satellite apportioned to state:
\$12,095,600 or (.0269) x \$50,000,000: \$ 1,345,000
\$450,000,000

Total value of all property attributed
to this state, including the satellite
property: \$13,440,600

Total property factor %
(\$13,440,600/\$500,000,000): .0269

(iii) The Payroll Factor.

A. Payroll Factor Denominator. The denominator of the payroll factor shall include all compensation paid to employees during the income year, including that paid to directors, actors, newscasters and other talent in their status as employees. No compensation paid to independent

contractors or persons other than employees shall be included in the payroll factor.

B. Payroll Factor Numerator. Compensation of employees engaged in the production of a film or radio broadcast on location shall be attributed to the state in which the services were performed. Compensation of all other employees shall be governed by the provisions of Reg. IV.13. and 14.

(iv) The Sales Factor.

A. Sales Factor Denominator. The denominator of the sales factor shall include the total gross receipts derived by the taxpayer from transactions and activity in the regular course of its trade or business, except receipts excluded under Reg. IV.18.(c).

B. Sales Factor Numerator. The numerator of the sales factor shall include all gross receipts of the taxpayer from sources within this state, including the following:

1. Gross receipts, including advertising revenue, from radio programming and films in release to television and radio stations located in this state.

2. Gross receipts, including advertising revenue, from radio programming and films in release to or by a network for network broadcast shall be attributed to this state in the ratio that the audience for such network stations (owned and affiliated) located in this state bears to the total audience for all such network stations (owned and affiliated) within the United States. The audience factor for television and radio broadcasting and telecasting shall be determined by the ratio that the population of this state bears to the population of the United States as reflected in the most current population data published by the U.S. Bureau of Census.

3. Gross receipts from films in release to subscription television telecasters shall be attributed to this state in the ratio that the subscribers for such telecaster located in this state bears to the total subscribers of such telecaster in the United States. If the number of subscribers cannot be accurately determined from the records maintained by the taxpayer, the ratio shall be determined on the basis of the applicable year's statistics on subscribers published in Cable Vision, International

Thompson Communications, Inc., Denver, Colorado, if available, or by other published market surveys, or, if none is available, by population data published by the U.S. Bureau of Census for all states in which the telecaster has subscribers.

4. To the extent that the gross receipts from such radio programming or films as determined pursuant to subparagraph 2. or 3. of paragraph B. hereof include receipts derived from the broadcast or telecast to audiences located outside of the United States ("foreign-based receipts"), the audience factor shall be further modified so that such foreign-based receipts are not used to affect the amount of receipts that are to be apportioned to the state. Such modification shall consist of applying to the ratio of in-state population (or subscribers) to United States population (or subscribers), the ratio of United States-based receipts to total gross receipts.

Example: XYZ Television Network Co. has gross receipts from all telecasting of films of \$1 billion of which a total of \$200 million was derived from advertising receipts and license fees attributable to releases of its films in foreign television markets and \$800 million was attributable to the United States market. Assume that the foreign countries into which its programs have been telecast or sold or licensed for telecast would have jurisdiction to impose their income tax upon XYZ Network Co. XYZ's in-state gross receipts attributable to its film telecasting activity would be determined as follows:

$$\frac{\$800,000,000}{\$1,000,000,000} \text{ (or .80) } \times \frac{\text{state population}}{\text{U.S. population}} \times \$1,000,000,000$$

5. Receipts from sales and rentals of video cassettes and discs shall be included in the sales factor as provided in Reg. IV.16.

Multistate Tax Commission



ALAN H. FRIEDMAN, General Counsel

To: Tax Administrators, MTC Member States

From: Alan H. Friedman, General Counsel *AHF*

Subject: Notice of Hearing Upon Television and Radio
Broadcast Regulation

Date: April 26, 1988

I am providing you with notice as required by paragraph 7. of the MTC Bylaws of the public hearing now set for June 9, 1988 with regard to a proposal regarding the allocation and apportionment of net income derived from television and radio broadcasting.

The Notice of Public Hearing and the proposed regulation is attached hereto. If either you or any of your staff has any questions regarding the proceeding or proposal, I will be available at either 1-800-327-1258 or 1-800-525-2647.

EXHIBIT
2.a.

Headquarters Office:
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024
Telephone (303) 447-9645

New York Audit Office:
25 W. 43rd Street, Suite 212
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

Multistate Tax Commission

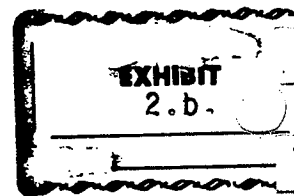


ALAN H. FRIEDMAN, General Counsel

To: Tax Administrators, MTC Associate Member States
From: Alan H. Friedman, General Counsel
Subject: Notice of Hearing Upon Television and Radio
Broadcast Regulation
Date: April 26, 1988

I am providing you with notice of the public hearing now set for June 9, 1988 with regard to a proposal regarding the allocation and apportionment of net income derived from television and radio broadcasting.

The Notice of Public Hearing and the proposed regulation is attached hereto. If either you or any of your staff has any questions regarding the proceeding or proposal, I will be available at either 1-800-327-1258 or 1-800-525-2647.



Headquarters Office:
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024
Telephone (303) 447-9645

New York Audit Office:
25 W. 43rd Street, Suite 212
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

Multistate Tax Commission



To: Tax Administrators, MTC Non-Member States
From: Alan H. Friedman, General Counsel
Subject: Notice of Hearing Upon Television and Radio
Broadcast Regulation
Date: April 26, 1988

I am providing you with notice of the public hearing now set for June 9, 1988 with regard to a proposal regarding the allocation and apportionment of net income derived from television and radio broadcasting.

The Notice of Public Hearing and the proposed regulation is attached hereto. If either you or any of your staff has any questions regarding the proceeding or proposal, I will be available at either 1-800-327-1258 or 1-800-525-2647.

EXHIBIT
2.c.

Headquarters Office:
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024
Telephone (303) 447-9645

New York Audit Office:
25 W. 43rd Street, Suite 212
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

Multistate Tax Commission



NOTICE OF PUBLIC HEARING

The Multistate Tax Commission will hold a public hearing at the offices of the California Franchise Tax Board, Los Angeles District, 624 South Grand Avenue, 9th Floor, Los Angeles, California beginning at 10:00 A.M. on Thursday, June 9, 1988 on the following subject:

Proposed addition to the Multistate Tax Commission Allocation and Apportionment Regulation IV.18 relating to the allocation and apportionment of income derived by television and radio broadcasters.

A copy of the proposed Television and Radio Broadcasting Regulation is attached to this Notice. The Commission invites all interested parties to participate in the hearing. Those desiring to make oral presentations before the Hearing Officer must notify him in writing on or before June 1, 1988. Anyone desiring to submit written comments may do so with the Hearing Officer prior to June 9, 1988. The Hearing Officer is:

Alan H. Friedman
General Counsel
386 University Ave.
Los Altos, CA 94022
Phone: 800-327-1258

EXHIBIT

3

Headquarters Office:
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024
Telephone (303) 447-9645

New York Audit Office:
25 W. 43rd Street, Suite 212
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

Multistate Tax Commission



ALAN H. FRIEDMAN, General Counsel

April 16, 1988

Marilyn Walsh
Vice President and
Director of Taxes
CBS, Inc.
51 West 57th Street
New York, NY 10019

Re: MTC Television and Radio Broadcasting Regulation

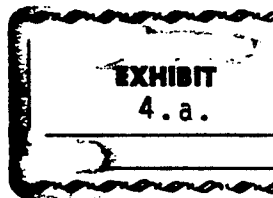
Dear Ms. Walsh:

I am enclosing for your information a Notice of Rulemaking, along with the proposed regulation concerning your industry. If you have any questions, please do not hesitate to call me at either 1-800-525-2647 or 1-800-327-1258. Your input with regard to the MTC proposal would be greatly appreciated.

Very truly yours,

Alan H. Friedman
General Counsel

P.S. Since I assume that you will be sharing this with Alvin Bobrow, I did not separately copy him with this letter.



Headquarters Office:
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024
Telephone (303) 447-9645

New York Audit Office:
25 W. 43rd Street, Suite 212
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

Multistate Tax Commission



ALAN H. FRIEDMAN, General Counsel

April 16, 1988

Barry Umansky
National Association of Broadcasters
1771 N Street, NW
Washington, D.C. 20036

Re: MTC Television and Radio Broadcasting Regulation

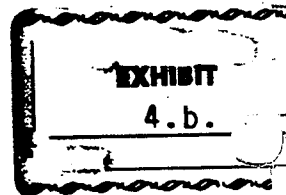
Dear Mr. Umansky:

I am enclosing for your information a Notice of Rulemaking, along with the proposed regulation concerning your industry. If you have any questions, please do not hesitate to call me at either 1-800-525-2647 or 1-800-327-1258.

Your industry's input with regard to the MTC proposal would be greatly appreciated. Therefore, I would appreciate it if you could distribute the notice and the proposed regulation to interested members of your association.

Very truly yours,

Alan H. Friedman
General Counsel



Headquarters Office:
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024
Telephone (303) 447-9645

New York Audit Office:
25 W. 43rd Street, Suite 212
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

Multistate Tax Commission



ALAN H. FRIEDMAN, General Counsel

April 16, 1988

William Sharkey
National Broadcasting Company, Inc.
30 Rockefeller Plaza
New York, NY 10020

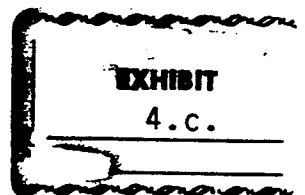
Re: MTC Television and Radio Broadcasting Regulation

Dear Mr. Sharkey:

I am enclosing for your information a Notice of Rulemaking, along with the proposed regulation concerning your industry. If you have any questions, please do not hesitate to call me at either 1-800-525-2647 or 1-800-327-1258. Your input with regard to the MTC proposal would be greatly appreciated.

Very truly yours,

Alan H. Friedman
General Counsel



Headquarters Office:
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024
Telephone (303) 447-9645

New York Audit Office:
25 W. 43rd Street, Suite 212
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

Multistate Tax Commission



ALAN H. FRIEDMAN, General Counsel

April 16, 1988

Robert Lorenz
ABC-Capital Cities, Inc.
1330 Avenue of the Americas
Thirty-fourth Floor
New York, NY 10019

Re: MTC Television and Radio Broadcasting Regulation

Dear Mr. Lorenz:

I am enclosing for your information a Notice of Rulemaking, along with the proposed regulation concerning your industry. If you have any questions, please do not hesitate to call me at either 1-800-525-2647 or 1-800-327-1258. Your input with regard to the MTC proposal would be greatly appreciated.

Very truly yours,

Alan H. Friedman
General Counsel

EXHIBIT
4.d.

Headquarters Office:
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024
Telephone (303) 447-9645

New York Audit Office:
25 W. 43rd Street, Suite 212
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

Multistate Tax Commission



ALAN H. FRIEDMAN, General Counsel

April 21, 1988

Katherine Meier
National Cable Television Association
1724 Massachusetts Ave., N.W.
Washington, D.C. 20036

Re: MTC Television and Radio Broadcasting Regulation

Dear Ms. Meier:

I am enclosing for your information a Notice of Rulemaking, along with the proposed regulation concerning your industry. If you have any questions, please do not hesitate to call me at either 1-800-525-2647 or 1-800-327-1258.

Your industry's input with regard to the MTC proposal would be greatly appreciated. Therefore, I would appreciate it if you could distribute the notice and the proposed regulation to interested members of your association.

Very truly yours,

Alan H. Friedman
General Counsel

EXHIBIT
4.e.

Headquarters Office:
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024
Telephone (303) 447-9645

New York Audit Office:
25 W. 43rd Street, Suite 212
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

Multistate Tax Commission



ALAN H. FRIEDMAN, General Counsel

April 21, 1988

Mary Mahoney
State Income Tax Coordinator
Telecommunications, Inc.
Terminal Annex
P.O. Box 5630
Denver, CO 80217

Re: MTC Television and Radio Broadcasting Regulation

Dear Ms. Mahoney:

I am enclosing for your information a Notice of Public Hearing, along with the proposed regulation concerning your industry. If you have any questions, please do not hesitate to call me at either 1-800-525-2647 or 1-800-327-1258.

Your expert input with regard to the MTC proposal would be greatly appreciated.

Very truly yours,

Alan H. Friedman
General Counsel

EXHIBIT
4.f.

Headquarters Office:
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024
Telephone (303) 447-9645

New York Audit Office:
25 W. 43rd Street, Suite 212
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

Multistate Tax Commission



ALAN H. FRIEDMAN, General Counsel

April 21, 1988

Gary Halsey
United Cable Television
P.O. Box 5840 TA
Denver, CO 80217

Re: MTC Television and Radio Broadcasting Regulation

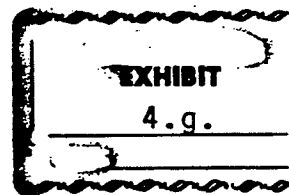
Dear Mr. Halsey:

I am enclosing for your information a Notice of Public Hearing, along with the proposed regulation concerning your industry. If you have any questions, please do not hesitate to call me at either 1-800-525-2647 or 1-800-327-1258.

Your expert input with regard to the MTC proposal would be greatly appreciated. Thank you, once again, for the information you provided me by telephone today.

Very truly yours,

Alan H. Friedman
General Counsel



Headquarters Office:
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024
Telephone (303) 447-9645

New York Audit Office:
25 W. 43rd Street, Suite 212
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

Multistate Tax Commission



NOTICE OF PUBLIC HEARING

The Multistate Tax Commission will complete its public hearing upon the following subject by keeping the record open for public comment until April 21, 1989 on the following subject:

Proposed addition to the Multistate Tax Commission Allocation and Apportionment Regulation IV.18. relating to the allocation and apportionment of income derived by television and radio broadcasters.

A copy of the proposed Television and Radio Broadcasting Regulation, as modified by the Hearing Officer after the public hearing held on June 9, 1988, may be obtained by writing to the Hearing Officer.

The Commission invites all interested parties to participate in the hearing. All oral presentations made at the public hearing held on June 9, 1988 shall be made part of the public hearing record. No further oral presentations shall be received unless a written request is received by the Hearing Officer on or before April 3, 1989. If a request for oral presentation is received, an opportunity to do so will be provided. In such event, all persons having already provided written or oral presentations will be so advised. In addition, any other person who desires to be present at any such hearing at which oral presentations will be made shall be provided notice thereof, if such person writes to the Hearing Officer on or before April 3, 1989 requesting such notice. Any person wishing to make further written comment upon the proposed Regulation may do so by mailing it to the Hearing Officer on or before April 21, 1989. The Hearing Officer is:

Alan H. Friedman
386 University Avenue
Los Altos, CA 94022
Tel.: (415)-941-0556
1-800-327-1258 (outside California)

EXHIBIT
5.a.

Headquarters Office:
1790 30th Street, Suite 314
Boulder, Colorado 80301-1024
Telephone (303) 447-9645

New York Audit Office:
25 W. 43rd Street, Suite 212
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

DRAFT: 1/30/89

[The following is a tentative draft of the proposed Television and Broadcast Regulation that has been prepared by the Hearing Officer after the receipt of public comment. To the extent that the following reflects changes to the regulation as originally proposed, the changes are only tentative, as the hearing process has not been completed and the Hearing Officer has yet to prepare his final report and recommendations to the Multistate Tax Commission. This draft is now made public in the interest of receiving additional public comment; and, therefore, it is not necessarily the final proposal. The bolded material represents most of the changes made from regulation as originally proposed; the material struck through represents most of the deleted material of substance.]

Multistate Tax Commission

Proposed Regulation

Television and Radio Broadcasting

Reg. IV.18.(). Special Rules: Television and Radio Broadcasting.

The following special rules are established in respect to the apportionment of income from television and radio broadcasting.

(1) **In General.** When a person in the business of conducting a television or radio network (including owned and affiliated stations) has income from sources both within and without this state, the amount of business income from sources within this state shall be determined pursuant to Article IV. of the Multistate Tax Compact and the regulations issued thereunder by this state, except as modified by this regulation. This regulation shall also apply to telecasting by cable television systems; and to independent television and radio stations to the extent they are members of a chain of commonly owned stations all of which operate as a network or all of which are unaffiliated with a network, but which operate collectively in purchasing properties for broadcast or in marketing airtime. ~~This regulation applies to income years beginning on or after January 1, 1984.~~

(2) **Business and Nonbusiness Income.** For definitions, regulations and examples for determining whether income shall be classified as "business" or "nonbusiness" income, see Reg. IV.1.

(3) **Definitions.** The following definitions are applicable to the terms contained in this regulation, unless the context clearly requires otherwise.

(1) "Film" means the physical embodiment of a play,

EXHIBIT
5.b.

story or other literary, commercial, educational or artistic work, as a motion picture, a video tape, disc or other medium, ~~except that it does not include video cassettes, discs or similar medium intended for sale or rental for home viewing.~~

Each episode of a series of films produced for television shall constitute a separate "film" notwithstanding that the series relates to the same principal subject and is produced during one or more television seasons.

(ii) "Outer-jurisdictional" property means certain types of tangible personal property that are owned or rented by the taxpayer and used in the business of telecasting or broadcasting, but which are not physically located in any particular state, such as orbiting satellites, undersea transmission cables and the like.

(iii) "Release date" means the date on which a film is placed into service. A film is placed into service when it is first telecast to the primary audience for which the film was created. Thus, a film is placed in service when it is first publicly telecast for entertainment, educational, commercial, artistic or other purpose. Each episode of a television series is placed in service when it is first telecast. A film is not placed in service merely because it is completed and therefore in a condition or state of readiness and availability for telecast or, merely because it is telecast to prospective sponsors or purchasers, or is shown in preview before a select audience.

(iv) "Rent" shall include license fees or other payments or consideration provided in exchange for the telecast of films or the broadcast of radio programming.

(v) A "subscriber" to a cable television system is the individual residence or other outlet which is the ultimate recipient of the transmission.

(vi) "Tangible personal property" used in the business, whether owned or rented, shall include but not be limited to films, sets, props, wardrobes, and other similar equipment or property.

(vii) "Telecast" or "broadcast" (used interchangeably) means the transmission of television or radio programming by an electronic signal conducted by radiowaves or microwaves or by wires, lines, coaxial cables, wave guides, fiber optics, or other conduits of communications.

(4) Apportionment of Business Income.

(i) In General. The property factor shall be determined in accordance with Regulation IV.10 through 12., the payroll factor in accordance with Regulation IV.13. and 14., and the sales factor in accordance with Regulation IV.15. and 16., except

as modified by this regulation.

(ii) The Property Factor.

A. In General.

1. In the case of rented studios, the net annual rental rate shall include only the amount of the basic or flat rental charge by the studio for the use of a stage or other permanent equipment such as sound recording equipment and the like; except that additional equipment rented from other sources or from the studio not covered in the basic or flat rental charge and used for one week or longer (even though rented on a day-to-day basis) shall be included. Lump-sum net rental payments for a period which encompasses more than a single income year shall be assigned ratably over the rental period.

2. The value of film and radio programming shall-

a. be the original cost of producing the film or radio program as determined for federal income tax purposes, before any adjustment for federal credits which have not been claimed for state purposes, and

b. include payments for actors, newscasters, directors, crew and other similar services reasonably required for such production.

3. The value of a film or radio program shall not be included in the property factor until its release date.

B. Property Factor Denominator.

1. All real property and tangible personal property (other than films and outer-jurisdictional property), whether owned or rented, which is used in the business shall be included in the denominator of the property factor.

2. Films, other than films the cost of which is expensed for this state's tax purposes at the time of production, shall be included in the property factor at original cost for twelve years beginning with the release date.

3. Films and radio programming of a topical nature, including news or current event programs, sporting events or interview shows, the cost of which is expensed for this state's tax purposes at the time of production, shall be included in the property factor at original cost in the year of the release date.

4. All films and radio programming, other than those included in the denominator under clause 2. or 3. of this subparagraph B., shall be aggregated and treated as a single film or radio program property and included in the property factor.

Such aggregated property shall be valued at eight times the gross receipts generated during the income year from network television or radio, television or radio syndication, cable television, subscription television, and other receipts from the broadcast, distribution, or other disposition of said film or radio properties; but in no event in an amount greater than the total original cost of such aggregated film or radio property.

5. Audio or video cassettes, discs or similar medium made of film or radio programming and intended for sale or rental by the taxpayer for home viewing or listening shall be included in the property factor at their original cost. To the extent that the taxpayer licenses or otherwise permits others to manufacture or distribute such cassettes, discs or other medium containing film or radio programming for home viewing or listening, the value of said cassettes, discs or other medium shall include the license, royalty or other fees received by the taxpayer capitalized at a rate of eight times the gross receipts derived therefrom during the income year.

6. Outer-jurisdictional property shall be excluded from the denominator of the property factor.

C. Property Factor Numerator.

1. If tangible personal property (other than films, radio programming and outer-jurisdictional property) is located or used in this state for part of the income year, it shall be included in the numerator of the property factor at a value determined by applying the ratio which the number of days the property is located or used in this state bears to the total number of days such property was owned or rented by the taxpayer during the income year. If such information cannot be determined accurately from records maintained by the taxpayer, the ratio shall be same ratio as determined pursuant to subparagraph C.2.

2. The total value of film or radio programming that is included in the property factor denominator under paragraph (4)(ii) B. shall be attributed to this state in the same ratio in which the total receipts in this state from such films and radio programming, as determined in subparagraphs 1., 2., 3., and 4. of paragraph (4)(iv) B., pertaining to the sales factor, bears to the total receipts everywhere.

3. Outer-jurisdictional property shall be excluded from the numerator of the property factor.

Example: XYZ Television Network Co. has a total value of its property everywhere, including a \$50,000,000 satellite that was used to telecast programs into this state, of \$500,000,000.00. The total value of real and tangible personal property located in this state for the entire income year was valued at \$2,000,000.00; the mobile property described in subparagraph C.1. was determined to be of a value of \$4,000,000;

and such mobile property was used in this state for 100 days.

The total value of all the films described in subparagraph C.2 was \$300,000,000.00 and the receipts factor for this state has been determined to be .03 The total value of property to be attributed to this state would be determined as follows:

Value of property permanently in state:	\$2,000,000
Value of mobile property 100/365 or (.2739) x \$4,000,000:	\$1,095,600
Value of films apportioned to this state (.03 x \$300,000,000.00):	<u>\$9,000,000</u>
Total value of property attributable to state without apportionment of satellite property:	\$12,095,600
Total property factor % (\$12,095,600/\$450,000,000):	.0269

(iii) The Payroll Factor.

A. Payroll Factor Denominator.

1. The denominator of the payroll factor shall include all compensation, including residual and profit participation payments, paid to employees during the income year, including that paid to directors, actors, newscasters and other talent in their status as employees. ~~No compensation paid to independent contractors or persons other than employees shall be included in the payroll factor.~~

2. Amounts paid or other consideration that is provided to another person, corporation or other business entity for providing the services of directors, actors, newscasters and other talent for a live television broadcast, film or radio programming may be included in the payroll factor only upon a finding by the Tax Administrator that (a) such payments or other consideration were substantial in relationship to the total compensation paid to employees; and (b) failure to include such other payments or consideration would prevent the apportionment formula from fairly representing the extent of the taxpayer's business activity in this state.

B. Payroll Factor Numerator.

Compensation for employees, as well any payments or other consideration for the providing of those talent services that are included in the payroll denominator pursuant to paragraph (4)(iii) A.2., who are engaged on location in the production of a live television broadcast, film or radio programming shall be attributed to the state in which the

services were performed. Compensation of all other employees shall be governed by the provisions of Reg. IV.13. and 14.

(iv) **The Sales Factor.**

A. Sales Factor Denominator.

The denominator of the sales factor shall include the total gross receipts derived by the taxpayer from transactions and activity in the regular course of its trade or business, except receipts excluded under Reg. IV.18.(c).

B. Sales Factor Numerator.

The numerator of the sales factor shall include all gross receipts of the taxpayer from sources within this state, including the following:

1. Gross receipts, including advertising revenue, from live television, film or radio programming in release to or by television and radio stations located in this state.

2. Gross receipts, including advertising revenue, from live television, films or radio programming in release to or by a television or radio network for broadcast shall be attributed to this state in the ratio (hereafter "audience factor") that the audience for such network stations (owned and affiliated) located in this state bears to the total audience for all such network stations (owned and affiliated) within the United States.

The audience factor for television or radio network programming shall be determined by the ratio that the taxpayer's in-state viewing (listening) audience bears to its total United States viewing (listening) audience. In the case of television, the audience factor shall be determined by reference to the rating statistics as reflected in such sources as Arbitron, Nielsen or the average circulation statistics published annually in the Television and Cable Factbook, "Stations Volume" by Television Digest, Inc., Washington, D.C. In the case of radio, the audience factor may be determined by reference to rating statistics as reflected in such sources as Arbitron or Birch/Scarborough Research.

If none of the foregoing sources are available, or, if available, none is in form or content sufficient for such purposes, then the audience factor shall be determined by the ratio that the population of this state bears to the population of the United States, as reflected in the most current population data published by the U.S. Bureau of Census, for all states which receive the network broadcasts.

3. Gross receipts from live telecasts and films in release to or by a cable television system shall be attributed to

this state in the ratio that the subscribers for such cable television system located in this state bears to the total subscribers of such cable television system in the United States. If the number of subscribers cannot be accurately determined from the records maintained by the taxpayer, the ratio shall be determined on the basis of the applicable year's subscription statistics published in Cable Vision, International Thompson Communications, Inc., Denver, Colorado, if available, or, if not available, by other published market surveys.

If none of the foregoing resources are available, or, if available, none is in form or content sufficient for such purposes, then the subscription factor shall be determined by the ratio that the population of this state bears to the population of the United States as reflected in the most current population data published by the U.S. Bureau of Census for all states in which the cable system has subscribers.

4. To the extent that the gross receipts from such live television broadcasting, film, or radio programming, as determined pursuant to paragraph (4)(iv.)B.2. or 3., include receipts derived from broadcasts to audiences located outside of the United States ("foreign-based receipts"), the audience or subscription factor shall be further modified so that such foreign-based receipts are not used to affect the amount of receipts that are to be apportioned to the state. Such modification shall consist of applying to the ratio of in-state population (or subscribers) to United States population, as reflected in the most current population data published by the U.S. Bureau of Census for all states in which the taxpayer has an audience (or subscribers), the ratio of United States-based receipts to total gross receipts.

Example: XYZ Television Network Co. has gross receipts from all broadcasting of films of \$1 billion of which a total of \$200,000,000 was derived from advertising receipts and license fees attributable to releases of its films in foreign television markets and \$800,000,000 attributable to the United States market. Assume that the foreign countries into which its programs have been telecast or sold or licensed for telecast would have jurisdiction to impose their income tax upon XYZ Network Co., then its in-state gross receipts attributable to its telecasting activity would be determined as follows:

$$\frac{\$800,000,000}{\$1,000,000,000} \text{ (or } .80) \times \frac{\text{state population}}{\text{U.S. population}} \times \$1,000,000,000$$

5. Receipts from the sale, rental, licensing or other disposition of audio or video cassettes, discs, or similar medium intended for home viewing or listening shall be included in the sales factor as provided in Reg. IV.16.

Section 25137-8 is to be adopted to read as follows:

25137-8. Motion Picture and Television Film Producers and Television Networks - Apportionment of Income.

(a) This regulation applies to motion picture and television film producers, producers of television commercials, and to television networks. The provisions of this regulation shall also apply to independent television stations to the extent they are members of a chain of commonly owned stations all of which operate as network affiliates or all of which are unaffiliated with a network but which operate collectively in purchasing properties for telecast or in marketing air time, or which operate as a producer. This regulation applies to income years beginning on and after January 1, 1982.

(b) Definitions.

(1) "Film" means the physical embodiment of a play, story or other literary, commercial, educational or artistic work, as a motion picture, video tape, disc or other similar medium, except that it does not include news or sports films produced for telecast.

"Film" does not include video cassettes or discs intended for home viewing.

(2) Each episode of a series of films produced for television shall constitute a separate film notwithstanding that the series relates to the same principal subject and is produced during one or more television seasons.

(3) "Release date" means the date on which a film is placed in service. A film is placed in service when it is first

telecast or exhibited to the primary audience for which the film was created. Thus, a motion picture theater film is placed in service when it is first publicly exhibited for entertainment purposes and an educational film is placed in service when it is first exhibited for instructional purposes. Each episode of a television series is placed in service when it is first telecast. A film is not placed in service merely because it is completed and therefore in a condition or state of readiness and availability for telecast or exhibition, or merely because it is telecast or exhibited to prospective exhibitors, sponsors, or purchasers, or is shown in a "sneak preview" before a select audience.

(4) A "film" is deemed to be tangible personal property.

(5) "Rent" shall include license fees for the exhibition or telecast of films.

(6) "Tangible personal property" used in the business, whether owned or rented, shall include but is not limited to sets, props, wardrobes, and other similar equipment or property.

(7) A "subscriber" to a subscription television telecaster is the individual residence or other outlet which is the ultimate recipient of the transmission.

(8) "Telecast" means the transmission of an electronic signal by radiowaves or microwaves or by wires, lines, coaxial cables, wave guides or other tangible conduits of communication.

(c) Apportionment of Business Income.

The property, payroll and sales factor of the apportionment formula for Motion Picture and Television Film Producers and Television Networks shall be computed pursuant to Sections 25128 through 25137 of the Revenue and Taxation Code and the regulations adopted pursuant thereto except as provided in this regulation.

(1) Property Factor.

(A) In General.

(i) In the case of rented studios, the net annual rental rate shall include only the amount of the basic or flat rental charge by the studio for the use of a stage and other permanent equipment such as sound recording equipment, etc., except that additional equipment rented from other sources or from the studio not covered in the basic or flat rental charge and used for one week or longer (even though rented on a day-to-day basis) shall be included. Lump-sum net rental payments for a period which encompasses more than a single income year shall be assigned ratably over the rental period.

(ii) The value of films shall--

(I) be the original cost of producing the film as determined for federal income tax purposes, before any adjustment for federal credits which have not been claimed for state purposes, and

(II) include talent salaries.

(iii) The value of a film shall not be included in the property factor until its release date.

(iv) Video cassettes and discs shall be included in the property factor at their inventory cost as shown in the taxpayer's books and records.

(B) Denominator.

(i) All real property and tangible personal property (other than films) whether owned or rented, which is used in the business, shall be included in the denominator.

(ii) Films, other than films the cost of which is expensed for California tax purposes at the time of production, shall be included in the property factor at original cost for twelve years beginning with the release date.

(iii) Films of a topical nature including news or current event programs, sporting events or interview shows, the cost of which is expensed for California tax purposes at the time of production, shall be included in the property factor at original cost for one year beginning with the release date.

(iv) All films, other than those included in the denominator under clause (ii) or (iii) of this subparagraph, shall be aggregated and treated as a single film property which shall be included in the property factor. Such property shall be valued at eight times the gross receipts generated during the income year from theater distribution, network television, television syndication, cable television, subscription television and the marketing of video cassettes and discs through licensing or direct selling, or similar receipts, but in no event in an amount greater than the total original cost of such aggregated film property.

(C) Numerator.

(i) If tangible personal property (other than films) is located or used in this state for part of the income year, its value shall be determined by applying the ratio which the number of days the property is located or used in this state bears to the total number of days such property was owned or rented during the income year.

(ii) The total value of films that are included in the property factor under subparagraph (B) of paragraph (1) of this subsection shall be attributed to this state in the same ratio in which the total California receipts from such films as determined in subparagraphs (A), (B) and (C) of paragraph (3) of this subsection pertaining to the sales factor bears to the total of such receipts everywhere.

(2) Payroll Factor.

(A) In General.

(i) The denominator shall include all compensation paid to employees during the income years, including talent salaries. Residual and profit participation payments constitute compensation paid to employees.

(ii) The amount paid to a corporation for providing the services of an actor or director who is an employee of such corporation or for loaning the services of an actor or director who is under contract with such corporation shall, if substantial, be included in the producer's payroll factor as if the amount paid was compensation paid to an employee of the producer.

(B) Numerator. Compensation of employees engaged in the production of a film on location shall be attributed to the state where the services are or were performed. Compensation of all other employees shall be governed by Regulations 25132 and 25133.

(3) Sales Factor Numerator. The numerator shall include all gross receipts of the taxpayer from sources within this state including the following:

(A) Gross receipts from films in release to theaters and television stations located in this state.

(B) Gross receipts from films in release to or by a television network for network telecast shall be attributed to this state in the ratio that the audience for such network stations (owned and affiliated) located in California bears to the total audience for all such network stations (owned and affiliated) everywhere. The audience shall be determined by rate card values published annually in the Television & Cable Factbook, Vol. I, "Stations Volume," Television Digest, Inc., Washington, D.C., if available, or by other published market surveys, or, if none is available, by population data published by the U.S. Bureau of the Census.

(C) Gross receipts from films in release to subscription television telecasters shall be attributed to this state in the ratio that the subscribers for such telecaster located in California bears to the total subscribers of such telecaster everywhere. If the number of subscribers cannot be determined accurately from records maintained by the taxpayer, the ratio shall be determined on the basis of the applicable year's

statistics on subscribers published in Cable Vision, International Thompson Communications Inc., Denver, Colorado, if available, or by other published market surveys, or, if none is available, by population data published by the U.S. Bureau of the Census for all states in which the telecaster has subscribers.

(D) Receipts from sales and rentals of video cassettes and discs shall be included in the sales factor as provided in Regulations 25135 and 25136.

NOTE: Authority cited: Section 26422, Revenue and Taxation Code. Reference: Section 25137, Revenue and Taxation Code.