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VIA FACSIMILE & FEDERAL EXPRESS

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Re: NCCUSL—Project to Revise UDITPA

Dear Mr. Trost:

This letter is being submitted on behalf of General Electric Company. We are writing in response to the meeting that the Revised UDITPA Drafting Committee of the National Conference of Commissioners on Uniform State Laws (NCCUSL) held on May 30 to May 31, 2008 in Chicago. We would like to thank NCCUSL and the Drafting Committee for the opportunity to participate in this project. We have divided our comments into two parts. First, we would like to expand upon some of our comments made at the meeting with regard to establishing standards to be used for determining whether to make changes to UDITPA. Second, we would like to respond directly to the questions raised by President Walters during the Chicago meeting.

Standards for Review and Revision

NCCUSL's project to "revise," or more accurately review and possibly revise, UDITPA undoubtedly is an important undertaking. However, we believe it is critical that before any specific changes to UDITPA are proposed, the Drafting Committee should develop a clearly articulated set of guiding principles, goals or standards by which to evaluate how—or more importantly whether—changes to UDITPA should be made. Drafted over 50 years ago, UDITPA has withstood the test of time and generally has proven to be a workable model. Thus, while a review of UDITPA is not

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necessarily inappropriate, it is imperative that the process not result in change for the sake of change.

This project is difficult and challenging as is the development of workable standards for revising UDITPA. The following are some suggested approaches.

One approach is to revise only those portions of UDITPA that are clearly erroneous—for example, where constitutional violations exist as determined by the courts. While the volume of litigation should not serve as a definitive measure of the need for change, the absence of litigation in a particular area of UDITPA should be a strong indicator that revisions are unnecessary in that area.

Another possible approach is to revise those areas of UDITPA only where there is overwhelming consensus to do so by all stakeholders involved. Since uniformity is one obvious purpose of UDITPA,¹ changes to UDITPA should not be undertaken unless the vast majority of states as well as interested parties in the business community agree that changes to improve uniformity are warranted. If there is no consensus for change at the outset, but revisions are proposed and adopted, it is safe to predict that the new provisions will most likely foster future litigation. Such litigation could lead to disparate court decisions in various states which would defeat rather than promote uniformity.

A third approach would be to focus only on those areas of UDITPA that the original drafters identified as problematic.² However, it should be noted that the original drafters recognized that UDITPA neither was perfect nor intended to address all possible fact patterns or situations, hence the reason for Section 18. To avoid needless tinkering, this approach would limit *review* to those areas that the original drafters conceded were difficult to solve. But, before a *revision* is adopted, it must be clear that the change would create greater certainty and uniformity for states and businesses. Further, it should be accepted that “no change” may be an appropriate alternative to making a revision, since it is not certain in all instances that a revision proposed today would be a better solution than that adopted 50 years ago.

¹ See e.g., UDITPA § 19.

² See William J. Pierce, “The Uniform Division of Income for State Tax Purposes” in 35 *Taxes* 747 (1957); Frank M. Keesling & John S. Warren, “California’s Uniform Division of Income for Tax Purposes Act, Part II,” 15 *UCLA L. Rev.* 653 (1968).

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Response to President Walters

The questions posed by Ms. Walters at the Chicago meeting underscore the importance of focusing upfront on NCCUSL's overall project goals and setting clear standards before delving into any specific changes to UDITPA. Ms. Walters raised the following issues: (1) whether UDITPA is out of date and in need of change, (2) if so, how changes to UDITPA should be achieved, (3) whether federal legislation is needed, (4) if the process must draw lines, whether uniform lines are the best, and (5) how one determines what action should be taken, if not through the NCCUSL process.

1. Is UDITPA out of date and in need of change?

Most, if not all, of UDITPA is not outdated. While not universally adopted or implemented without modification, UDITPA serves as the cornerstone or starting point for most states' assignment of income regimes. As originally conceived, UDITPA was designed to address the "need for a uniform method of division of income for tax purposes among the several taxing jurisdictions."³ By promoting uniformity among the states, UDITPA has achieved, and continues to achieve, one of its most fundamental goals.

It has been argued that UDITPA is in need of change, for example, because it fails to attain what some commentators perceive to be full accountability of a taxpayer's income. In other words, these commentators argue that UDITPA needs to be modified to prevent so-called "nowhere income" from being assigned to a state that does not impose a net income tax. Such an argument is based on, we submit, a misunderstanding of another of UDITPA's basic goals—to develop practical means of ensuring that a taxpayer is not taxed on more than 100 percent of its net income.⁴

The purpose of UDITPA is to avoid "duplicative, over-lapping taxation of business net income by two or more states."⁵ UDITPA was not designed to eliminate the ability of a state to impose or not impose a tax on income properly assigned to that state. Rather, UDITPA was designed to provide for a fair and equitable means of apportioning income to individual states when the taxpayer is engaged in business in more than one state.⁶ UDITPA was never intended to require that 100 percent of a

³ Uniform Division of Income for Tax Purposes Act, Prefatory Note.

⁴ *Id.*

⁵ UDITPA History - Drafts, UDITPA Draft 1957 D
(<http://www.nccusl.org/Update/CommitteeSearchResults.aspx?committee=302>).

⁶ See *Pierce, supra*, at 748.

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taxpayer's income must be subjected to tax in some state. The following comments by the UDITPA drafters in 1957 are clear in this regard:

If State A and State B each levy a net income tax but State C does not impose such a tax, the amount of the corporation's total multi-state business net income apportioned to and taxable by State A and by State B under their respective net income tax laws is exactly the same as it is when all three states levy an income tax. However, the multi-state business net income apportionable to State C by the Uniform Act's apportionment formula is not taxed by State C, because State C does not levy and collect an income tax. Under the Uniform Act neither State A nor State B is permitted to tax any greater amount of the corporation's multi-state business net income even though the income apportioned to State C under the Uniform Act's formula is not actually taxed by State C. In other words, under the Uniform Act all that is required is that all of the business net income from multi-state business operations be subject to income taxation in all of the states in which the multi-state business activities are carried on. It is not necessary that all of these states actually levy and collect a tax upon or measured by net income in order for the apportionment formula of the Uniform Act to apply.⁷

The above example underscores the necessity of examining UDITPA's original underlying goals before proceeding to make any changes. Assertions that UDITPA needs to be changed to address "nowhere income," for example, should be analyzed critically and not simply accepted at face value as justification that UDITPA is in need of reform. All of this illustrates that UDITPA is not necessarily out of date, and therefore, restraint should be taken to avoid making changes that might not meet the objectives of improving UDITPA uniformity.

2. How should changes to UDITPA, if any, be achieved?

UDITPA does not necessarily need to change. This gets back to the issue of setting forth standards for determining whether changes to UDITPA are necessary at all. As

⁷ See UDITPA Draft 1957 D, *supra*, at p.2 (emphasis added); see also Remarks of the Fourteenth Annual Conference of Tax Executives Institute, Inc., French Lick, Indiana, September 30, 1989 by Charles F. Conlon, Executive Secretary, National Association of Tax Administrators ("[C]ontrary to some views, the Act has not been drafted so as to insure that 100 percent of the taxpayer's income will be subjected to tax in some state. This is a fairly common misunderstanding about the Act and, no doubt, this is one reason why some tax men have not been particularly enthusiastic about the proposal.")

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noted above, the standard should not be "change for the sake of change." Instead, the key is whether UDITPA continues to function as a workable approach and whether its provisions align with how and where the taxpayer's income is generated, such that no corporation is subject to tax on more than 100 percent of its income.⁸

3. Is federal legislation needed?

Historically, uniformity of treatment by the states has only been achieved through federal mandates. If the goal is to eliminate tax policy choices in the assignment of income regimes, federal legislation may be required. If the goal is to set forth broad principles concomitant with constitutional standards, federal legislation may not be required.

One of the driving forces which led many states to adopt UDITPA was the real possibility in the mid-1960s of federal legislation in the area of state taxation of income of businesses engaged in interstate commerce. Such legislation was considered a threat to state taxing authority. The prevailing view at the time was that the adoption of UDITPA was the best way to limit the need for federal legislation on the state's ability to fairly assign income among the various states. Since the enactment of Public Law No. 86-272 in 1959, Congress has refrained from enacting legislation in the area of state corporate income tax. In the meantime, UDITPA has served as the foundation for most states' assignment of income regimes. Thus, federal legislation is not an absolute necessity for addressing some of the issues or concerns that have been raised regarding UDITPA.

4. Should uniform lines be drawn?

Uniform lines generally may be the optimal choice. However, assurance of full implementation by all of the states of a singular uniform rule is a difficult objective to achieve. Indeed, during the past decades, many states that adopted UDITPA have modified various provisions of UDITPA to accomplish certain policy objectives. This does not necessarily mean that UDITPA is in need of reform. UDITPA continues to provide a uniform approach or framework for apportioning the income of a multistate business, but it has proven to be sufficiently flexible to accommodate individual states' specific tax policy choices. Uniformity and flexibility are not mutually exclusive concepts, which may account for UDITPA's durability.

⁸ See Pierce, *supra*; see also Transcript of Proceedings in Committee of the Whole, Uniform Division of Income for Tax Purposes Act, July 9, 1957.

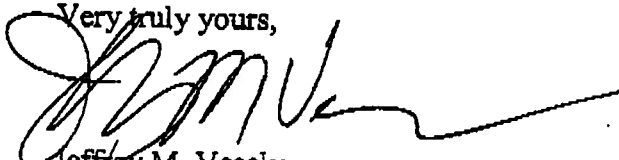
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5. Is the NCCUSL process the best way to proceed?

The NCCUSL process may very well be the best way to proceed. It is just as important, however, that there is not a preconceived notion by any stakeholders that changes to UDITPA are a necessary and absolute outcome of this project. A successful end result of this project could be that, upon review of UDITPA, no changes are required or desirable at this time.

Thank you again for the opportunity to participate in the Chicago meeting and for considering our comments at the meeting and in this submission.

Very truly yours,



Jeffrey M. Vesely

cc: ✓ Martha Lee Walters, President
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