

MEMORANDUM

TO: Committee on Scope & Program

FROM: Charles A. Trost, Chair of Study Committee

DATE: June 8, 2007

RE: *Uniform Division of Income for Tax Purposes Act*

The Study Committee met via teleconference on May 23, 2007, John Sebert and all members of the Committee were on the call except Commissioner Lane Kneedley, who was not available to participate.

After review and discussion of the Report of Stakeholder's Meeting, dated May 11, 2007, the Committee resolved unanimously to recommend to the Committee on Scope and Program that a drafting committee be formed to revise the Uniform Division of Income for Tax Purposes Act in its entirety for the reasons set forth in the attached Report of the Stakeholder's Meeting.

Charles A. Trost

MEMORANDUM

TO: Study Committee to Revise Uniform Division of Income for Tax Purposes Act

FROM: Charles A. Trost

DATE: May 11, 2007

RE: ***Report of the Stakeholders Meeting Considering Revising the Uniform Division of Income for Tax Purposes Act ("UDITPA")***

In a meeting at the ABA Building in Washington, D.C., at 9:30 a.m., on May 4, 2007, members of the Study Committee met with representative stakeholders for a preliminary discussion of the advisability of convening a drafting committee to revise UDITPA. Attending from NCCUSL were Executive Director John Sebert, Study Committee Members Steve Frost and Dale Higer, and Committee Chair Charles Trost. Invited guests attending were: Joe Huddleston and Shirley Sicilian, Executive Director and Legal Counsel of the Multi-State Tax Commission ("MTC"), Harley Duncan, Executive Director of the Federation of Tax Administrators ("FTA"), Doug Lindholm, Executive Director of the Council on State Taxation ("COST"), and Eli Dicker and Shirley Grimmitt, Tax Counsel and State Tax Counsel for Tax Executives Institute ("TEI"). Attending by telephone conference call were: Ben Miller, Fred Craven, and Carl Joseph of the California Franchise Tax Board ("FTB") and Joe Crosby, Legal Counsel for COST.

The meeting was convened as an information gathering open discussion involving highly knowledgeable and committed representatives of the taxpayer community and the tax administrators' community. All invitees are vitally concerned with the issues underlying UDITPA and the laws governing reporting and administering state taxation of corporate income in the context of taxpayers doing business in multiple states.

The questions asked were whether the participants believe that now is the appropriate time for NCCUSL to appoint a draft committee to undertake a review of UDITPA for the purpose of proposing amendments to it, and if so, what should be the scope of the review.

Ben Miller responded first and observed that UDITPA is now 50 years old and that California had been among the first states to adopt it—indeed many of its provisions incorporated much of the then existing California rules for apportionment of income of multistate corporations. He said that in his view, based on 35 years' experience with the FTB, now is the time to review and revise UDITPA.

Joe Huddleston said that while the MTC already had begun drafting a Model Act, it came to the view that it is preferable that NCCUSL take the lead in developing necessary revisions. He acknowledged that while the process will be difficult, that should not be a deterrent to proceeding. He stated that Section 17 dealing with services and intangibles is the area of UDITPA most in need of resolution with promulgation of rules that better address the current economy. Among the 21 regular members and 5 sovereign members of MTC there is substantial interest and unanimous endorsement of the undertaking by NCCUSL of a drafting committee to revise UDITPA. He emphasized that in his view we should not set too high a bar for what would constitute success, observing that it took many years before UDITPA achieved widespread approval.

Doug Lindholm said that he had heard from a great number of the members of COST recognizing that UDITPA needs to be reworked. He said that pragmatically it will be hard to accommodate the views of everyone, because resolution of the various policy issues will impact different industries and different businesses in different ways—there will be winners and losers. He pointed out that not only will this be a problem for taxpayers, but there is also tension among the states—primarily between the market states and the producing states. He suggested an interesting approach would be to look at why states who have not adopted UDITPA have chosen not to and to focus on getting non-MTC states to join the MTC. Doug also touched on federal preemption, observing that from time to time there is interest in seeking federal legislation governing multi-state taxation. He said that as a general proposition COST does not support that approach and prefers the approach of a uniform act that can be submitted to the various states for enactment.

Eli Dicker said that TEI is a very large organization with over 6,000 members representing more than 2,700 businesses. Getting a consensus from them will be impossible, but on the whole having input from TEI into the process can be valuable, particularly as it relates to his members' views as to the process by which state taxes are administered, apart from the particular substantive rules. He pointed out that UDITPA is old and may have reached its useful life. Since all the sections are equally old, it strikes him that the whole Act should be revisited. We should look at all of its provisions, even if the ultimate conclusion is that some sections should remain intact as they are. By doing this we may find there are

areas of concern where there is wide interest in some revisions that will balance out the areas where the outcomes may be more controversial.

Harley Duncan said that the view of FTA is that the Act is 50 years old and needs to be looked at again in its entirety. He observed that while Section 17 particularly requires substantial revisions, the effort should not be confined to only one section or one issue. As it is these issues require resolution—either in the legislatures or in the courts, but piecemeal resolution on a case by case—state by state basis will come short of the uniformity that should be desired. Opening up the drafting and policy consideration process to all viewpoints—bringing everyone concerned into a big tent—will result in a better product in large part because of the perceived fairness of the process. He thinks we ought to do it and lay it out for the states to adopt. But he cautioned, as did Joe Huddleston, that there should be a realistic view of what constitutes success because this process will have a long germination period.

Carl Joseph added that there has been a relatively recent move by states toward a single sales factor which makes resolution of the Section 17 issues exceedingly important since the two concepts go hand in hand.

General discussion followed concerning the advisability of expanding the coverage of UDITPA, what other models might be looked to, and the process. There was unanimous agreement that it will be important to the process, and ultimately to widespread acceptance of the end product, if the first meeting of a drafting committee is confined to discussion of policy issues before any first draft effort is undertaken. The first job of the reporter then should be to identify areas of the Act that might be considered for revision and to create a statement of the issues and threshold policy decisions the revised Act will require.

The meeting adjourned at 11:30 a.m.
