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AMERICAN EXPRESS COMPANIES AND
SUBSIDIARIES

Petitioners

v.

OFFICE OF TAX & REVENUE

Respondent

Case No.2020-OTR-00029

2020-OTR-00030

ORDER ON SUMMARY ADJUDICATION

I. Introduction

Petitioner American Express and Subsidiaries (Amex) filed a franchise tax return as a Combined Group in the District of Columbia in 2015, 2016, and 2017. The Combined Group included 22 subsidiaries, two of which are financial institutions.

The Office of Tax and Revenue (OTR) issued Notices of Proposed Assessment alleging deficiencies totaling \$6,264,827 for tax years 2015, 2016, and 2017, contending that Amex improperly modified the apportionment formula for the financial institutions when calculating its tax liability. Amex has filed protests of the proposed assessments with the Office of Administrative Hearings (OAH) ¹

The sole issue in the case is the proper calculation of the payroll factor used in the apportionment formula for one of the financial institutions, Amex Centurion Bank. The parties agree on the numerator of the payroll factor (*i.e.* the compensation paid in the District of Columbia) but disagree about the denominator. Amex contends that the denominator for AMEX Centurion

¹ The OAH Establishment Act gives OAH jurisdiction “over all adjudicated cases of the Office of Tax and Revenue arising from tax protests filed pursuant to §47-4312. DC Official Code § 2-1831.03(b)(4)

Bank's payroll factor is *the total payroll of all 22 members* of the Combined Group, while OTR maintains that is the total *payroll of only the two financial institution members*. The difference in the two approaches accounts for the total alleged deficiency of \$6.3 million.

Amex has filed a motion for Summary Adjudication and OTR has filed a Cross-Motion for Summary Adjudication. For the reasons which follow, Amex's Motion of Summary Adjudication is denied and OTR's Cross-Motion is granted.

II. Summary Adjudication Standard

OAH Rule 2819.1 permits a party to move for summary adjudication of any issue by providing "sufficient evidence of undisputed facts and citation of controlling legal authority." Where OAH Rules do not address a procedural issue, a judge may be guided by District of Columbia Rules of Civil Procedure. OAH Rule 2801.1. Under Superior Court Civil Rule 56, a party is entitled to summary judgment if the evidence in the record shows that there is no genuine issue of material fact and that the party is entitled to judgment as a matter of law. *Weakley v. Burnham Corp.*, 871 A.2d 1167, 1173 (D.C. 2005). A genuine issue of material fact is one where there is sufficient evidence supporting the claimed factual dispute to require a jury or judge to resolve the parties' differing versions of the truth at trial. *Dodek v. CF 16 Corp.*, 537 A.2d 1086, 1092 (D.C. 1988).

III. Facts not in Dispute

Petitioner, American Express Company and Subsidiaries or American Express Combined Group (Amex) consists of 22 members, two of which are financial institutions: American Express Centurion Bank (Amex Centurion Bank) and American Express Bank, FSB (Amex Savings Bank).

AMEX Centurion Bank issues credit and charge cards products which are marketed and sold to consumers, while AMEX Savings Bank issues the credit and charge card products marketed and sold to consumers and small businesses.² Both entities are "financial institutions" as that term is defined in D.C. Code § 47-1810.04(20).³ Because the American Express Combined Group

² Bottieri-August Declaration at ¶ 13. (Petitioner's Motion for Summary Adjudication, Exhibit 1)

³ This is a mixed issue of law and fact, agreed on by the parties.

contains both financial institutions and nonfinancial institutions, the American Express Combined Group is a “Mixed Group.”

American Express filed its original returns for 2015, 2016, and 2017 tax years on October 13, 2016, October 10, 2017, and October 12, 2018, respectively. In these returns, American Express reported a tax liability of \$2,721,347 in the 2015 tax year, \$3,128,532 in the 2016 tax year, and \$3,239,401 in the 2017 tax year. American Express paid the tax liability reported on these returns.

Subsequently, on March 11, 2019, American Express filed amended returns for 2015, 2016, and 2017. Because American Express modified the apportionment formula used, its tax liability was significantly reduced for each of the tax years. In the amended returns, Amex reported a tax liability of \$507,752 in 2015, \$401,075 in 2016, and \$282,675 in 2017.

After the amended returns were filed, OTR conducted an audit of the amended returns. In a notice dated August 10, 2020, OTR advised American Express that it had a “Total Net Deficiency” of \$2,213,095 for Tax Year 2015. OTR issued a single combined notice for tax years 2016 and 2017, also dated August 10, 2020, which was similar to the notice for tax year 2015. It advised American Express that it had a deficiency of \$2,636,957 for tax year 2016 and \$1,414,775 for 2017 for a “Total Net Deficiency” of \$4,051,732 for the two tax years. The total tax OTR claims is owed for the three years is the same as the tax liability reported by Amex in the original returns that it filed for those tax years.

American Express filed its appeal with OAH of both Notices of Proposed Assessment of Tax Deficiency on September 3, 2020. OTR filed a Motion to Dismiss Amex’s appeal on March 29, 2021 for lack of subject matter jurisdiction. OTR contended that OAH lacked jurisdiction to adjudicate this matter because it is an appeal of a refund denial over which the District of Columbia Superior Court has exclusive jurisdiction. The Motion to Dismiss was denied in an Order issued August 24, 2021. 2021 D.C.Off. Adj. Hear. LEXIS 12.

IV. Background

To understand the controversy in this case, it is helpful to first review the three types of apportionment formulas that have been used in the District of Columbia in the past decade, as the

arguments of the parties focus on the significance of the statutes and regulations governing those formulas for the present controversy.

There are two apportionment categories: standard apportionment and special apportionment. Special apportionment applies to certain unique businesses, including financial institutions.

A. District Taxation of Entities Subject to Standard Apportionment

For purposes of state corporate income tax, apportionment is the method of assigning a portion of a multistate corporation's business income to a particular state.⁴ The taxpayer uses the taxing state's apportionment formula to determine the percentage of the business income that is subject to that state's corporate income tax, which is known as the apportionment factor.⁵ The state's corporate tax rate is then applied to the apportioned business income subject to the tax to determine the corporation's tax liability in the state. For example, if a corporation had \$100 in business income and the state's apportionment factor is 10%, then \$10 is subject to the state's corporate income tax.

There have been three widely recognized apportionment formulas used by states: (1) the equally-weighted three-factor formula; (2) the three-factor formula with double-weighted sales (four-factor); and (3) the single sales factor formula. The District has used each of these formulas in the past decade.

Separate Reporting with Three-Factor Formula Prior to 2011, the District used separate reporting, that is, each entity filed its own stand-alone tax return, using the three-factor formula that included property, payroll, and sales factors. §47-1810.02(d). The property factor was calculated as the value of the entity's property in the District *divided by* the value of that entity's total property everywhere. §47-1810.02(e). The payroll factor was calculated as the entity's payroll in the District *divided by* that entity's total payroll everywhere. §47-1810.02(f). The sales factor was calculated as the entity's sales in the District *divided by* total sales everywhere. § 47-1810.02(g).

⁴ See e.g., D.C. Code § 47-1810.02.

⁵ See e.g., § 47-1810.02(d)-(d-2).

Combined Reporting with Four-Factor Formula In 2011, the Council of the District of Columbia changed the reporting method to combined reporting. §47-1805.02a Combined reporting requires multi-state corporations to report together the profits of all of their subsidiaries, even if the subsidiaries are located outside of the state. Combined reporting applies to unitary businesses, which are businesses which have one or more subsidiaries that depend on or contribute to the parent corporation or other subsidiaries and thus constitute a homogenous enterprise.⁶

Also in 2011, the District changed the apportionment formula. The District adopted the three-factor formula with property, payroll, and double weighted sales (“four-factor apportionment formula”).⁷ §47-1810.02(d-1). The property factor for a taxable member of a combined group was calculated as the combined group’s property in the District *divided by* the value of the *combined group’s* total property everywhere. The payroll factor was calculated as the combined group’s payroll in the District *divided by* the combined group’s total payroll everywhere. The sales factor was calculated as the combined group’s sales in the District *divided by* the combined group’s total sales everywhere. §47-1810.04(c)(2).⁸

⁶ *Pioneer Container Corp. v. Beshears*, 684 P. 2d 396, 398-399 (Ks. 1984). The test for a unitary business is whether or not the operation of the portion of the business within the state is dependent on or contributes to the operation of the business outside of the state. *District of Columbia v. Pierce Associates*, 462 A. 2nd 1129 fn. 4 (D.C. 1983).

⁷ The four factor formula, which appears in DC Official Code-47-1810.02 (d-1) states as follows:

- (1) All business income shall be apportioned to the District by multiplying the income by a fraction, the numerator of which is the property factor plus the payroll factor plus the sales factor twice, and the denominator of which is 4.
- (2) This subsection shall be applicable for the tax years beginning after December 31, 2010, and before January 1, 2015.

⁸ DC Official Code-47- 1810.04(c) provides:

Except as provided in paragraph (3), the taxpayers share of the business income apportionable to the District of each combined group of which it is a member shall be the product of the:

- (1) Business income of the combined group, determined under § 47-1810.05; and
- (2) Taxpayer member’s apportionment percentage, determined in accordance with this chapter, including in the property, payroll, and sales factor numerators of the taxpayer’s property, payroll, and sales, respectively, associated with the combined group’s unitary business in the District and including in the denominator the property, payroll, and sales of all members of the combined group, including the taxpayer, which property, payroll, and sales are associated with the combined group’s unitary business wherever located.

Combined Reporting with Single Sales Factor Finally, in 2015 the District retained combined reporting for unitary businesses, but changed from using the four-factor apportionment formula, property, payroll, and double weighted sales, to a single factor apportionment formula that is based exclusively on sales (“single sales factor”). §47-1810.02(d-2). The sales factor is still calculated as the entity’s sales in the District *divided by* the combined group’s total sales everywhere. §47-1810.04(c)(2).

B. The District Taxation of Entities Subject to a Special Apportionment

The District of Columbia, like many states, has a special apportionment formula for financial institutions that differs from its standard apportionment formula.⁹

Financial Institution Apportionment during Separate Reporting Before 2011, when the District was a separate reporting jurisdiction, taxpayers were required to follow the special apportionment rules for financial institutions in 9 DCMR 129.¹⁰ Financial institutions calculated their apportionment factor by adding their gross income (sales) factor to their payroll factor and dividing by 2.

(3) For taxable years beginning after December 31, 2014, the apportionment provisions of § 47-1810.02(d-2) shall apply.

⁹ In 2020, 29 states had special sourcing and apportionment rules for financial institutions. Bloomberg Tax and Accounting, Survey of State Tax Departments, Executive Summary (2020); 2020 Marketing Executive Summary.pdf (Bloomberglp.com).

¹⁰ Allocation and Apportionment Applicable to Financial Institutions (9 DCMR 129)

(1) The District shall impose on a financial institution a franchise tax measured by net income, determined by multiplying the financial institution's base by an apportionment fraction, the numerator of which is the sum of the payroll factor and the gross income factor and the denominator of which is 2 For this purpose the base to which the apportionment fraction is applied shall be the financial institution's net income for that taxable year as defined under Title III of the Act.

(2) The payroll factor is a fraction, the numerator of which is the total amount paid or accrued in the District by the financial institution as compensation and the denominator of which is the total amount paid or accrued everywhere by the financial institution as compensation during the taxable year.

(3) Compensation shall be paid in the District if paid to any employee considered to be located or as having regular presence therein.

(5) The gross income factor is a fraction, the numerator of which is the financial institution's gross income located in the District during the taxable year and the denominator of which is the total gross income of the financial institution during the taxable year

The payroll factor was calculated as a fraction. The financial institution's total payroll in the District *divided by* the total payroll everywhere of the single financial institution that was filing separately.¹¹ Thus, although the denominator for the payroll factor was the total payroll everywhere for the financial institution, it was *only* the payroll of that single financial institution, since under separate reporting, each entity filed a separate stand-alone return. Because combined reporting had not yet been adopted, the financial institution did not include the payroll of non-financial businesses that may have been subsidiaries of the same unitary business.

Financial Institution Apportionment from 2011 to 2014 As discussed above, the District adopted combined reporting in 2011. At the same time., it also adopted a four-factor apportionment (property, payroll, and double weighted sales) as its standard apportionment formula.¹² §47-1810.02(d-1). The property factor for a taxable member of a combined group was calculated as the entity's property in the District *divided by* the value of the combined group's total property everywhere. The treatment of payroll and sales factors were similar. The denominators for those factors were also the value of all of the combined group's payroll and all of the combined group's sales. §47-1810.04(c)(2).

The computation of the special apportionment factor for financial institutions was addressed in a new regulation when combined reporting was adopted in 2011. That regulation, 9 DCMR 164 (Combining Special Apportionment Formulas), provided the method to compute apportionment for combined groups composed of non-financial institutions and financial institutions. Under this regulation, financial institutions still calculated their apportionment formula by using the two-factor formula contained in 9 DCMR 129, but each entity used the combined group's denominators. Thus during this period, the denominator of the payroll factor for

¹¹ 9 DCMR 129.2. Likewise, the sales factor was the financial institution's sales in the District *divided by* the financial institution's total sales everywhere. 9 DCMR 129.5.

¹² DC Official Code §47- 1810.02 (d-1) (apportionment of business Income)

(1) All business income shall be apportioned to the District by multiplying the income by a fraction, the numerator of which is the property factor plus the payroll factor plus the sales factor twice, and the denominator of which is 4.

(2) This subsection shall be applicable for the tax years beginning after December 31, 2010, and before January 1, 2015.

financial institutions included the payroll everywhere of all members of the combined group, including nonfinancial businesses.

The Dispute: the Formula for Financial Institutions after Single Sales Factor Adopted As discussed above, the use of the four-factor apportionment formula was short-lived as the District adopted the single sales factor formula for non-financial institutions in 2015.

The dispute in this case centers on how to calculate the payroll factor for financial institutions after the single sales factor formula was adopted. The parties are in agreement that the sales factor for the non-financial institutions in the combined group is calculated by dividing the sales of all the non-financial members in the combined group in the District of Columbia by the sales of the same members everywhere. They also agree on how the numerator of the financial institutions in the group should be calculated. They differ only on the calculation of the denominator of the payroll factor.

Amex takes the position that the denominator includes the payroll of all members of the combined group, both financial and non-financial, which is the method that was used to calculate the payroll denominator in the period from 2011 to 2014. OTR maintains once the single sales factor formula was adopted as the standard apportionment formula in 2015, and payroll was dropped as a factor for non-financial members of the combined group, calculation of the payroll denominator for a financial institution included only the nationwide payroll of the financial institution members.

OTR has published an administrative guidance that reflects this position. It appears in an example of a combined reporting schedule provided by OTR to show taxpayers how to mix groups with different apportionment formulas when preparing a District of Columbia tax return for a combined group. (Schedule F of District of Columbia tax return Form D-20). That example of an apportionment factor computation for a mixed group follows.

2015 DC Combined Reporting Schedule 2 Apportionment Factors Computation

World Wide Year _____ of 10 Year Election

Water's Edge

Name of Designated Agent:		Tax Year Ending:					
Taxpayer Identification Number (FEIN/SSN)							
Type of Entity: Fill in the respective columns if you are a Corporation, Unincorporated Business, Financial Institution or Non-Nexus Member.					(Non-Nexus)	(Financial Institution)	(Financial Institution)
Fiscalized: Y/N		N	Y	N	N	N	N
Description	Combined Group Report	Designated Agent	Member 1	Member 2	Member 3	Member 4	Member 5
Payroll Factor Computation							
1	District payroll: (total compensation paid or accrued).	\$719,400	\$0	\$0	\$0	\$219,400	\$500,000
2	Everywhere payroll: (total compensation paid or accrued).	\$3,743,000	\$0	\$0	\$0	\$1,743,000	\$2,000,000
3	Total payroll - District (total compensation paid or accrued).	\$719,400	\$0	\$0	\$0	\$219,400	\$500,000
4	Total payroll - everywhere (total compensation paid or accrued).	\$3,743,000	\$0	\$0	\$0	\$3,743,000	\$3,743,000
5	District payroll factor. <i>Line 3 divided by Line 4.</i>	19.2199%	0.0000%	0.0000%	0.0000%	5.8616%	13.3583%
Sales Factor Computation							
6	District sales.	\$10,075,000	\$2,960,000	\$1,505,000	\$0	\$2,610,000	\$3,000,000
7	Everywhere sales.	\$37,555,000	\$11,145,000	\$7,410,000	\$2,100,000	\$7,600,000	\$4,500,000
8	Total sales - District. <i>Line 6</i>	\$10,075,000	\$2,960,000	\$1,505,000	\$0	\$2,610,000	\$3,000,000
9	Total sales - everywhere. <i>Line 7.</i>	\$37,555,000	\$37,555,000	\$37,555,000	\$37,555,000	\$37,555,000	\$37,555,000
10	District single sales factor. <i>Line 8 divided by Line 9.</i>	26.8273%	7.8818%	4.0075%	0.0000%	6.9498%	7.9883%
11	Total percent. <i>Add Lines 5 and 10.</i>		7.8818%	4.0075%	0.0000%	0.0000%	12.8114%
12	Divider <i>for Financial institutions only.*</i>		1	1	1	1	2
13	DISTRICT APPORTIONMENT FACTOR. <i>Line 11 by Line 12 for Financial institutions only.</i>	28.9682%	7.8818%	4.0075%	0.0000%	0.0000%	6.4057%

* Financial institutions will use payroll & sales factor receipts (gross income) only and they will divide by 2. If there are less than two factors divide by one.

Take the total of the apportionment factors from the combined group report above and enter them on the appropriate lines and columns of schedule F of the D-20 / D30.

As shown by this chart, only financial institutions still used a payroll factor after the single sale factor formula was adopted in 2015. The financial members of the combined group have two factors: sales and payroll. Non-financial institutions use only one factor, a sales factor. The denominator of the sales factor for the combined group is the sales of both the financial and non-financial institutions everywhere. (Line 9)

Reflecting OTR's position, the denominator for the financial institutions consists only of the payroll of the financial institutions in the group. (Line 4 for Member 4 and 5). No payroll data is shown for the non-financial members (Member 1,2, and 3), as payroll is no longer used to calculate a payroll factor for non-financial members.

If this chart was changed to reflect Amex's position, payroll for non-financial members would be entered on Line 4 for Members 1, 2, and 3 in this example. Payroll for all five members

of the Combined Group would then be added together to derive the denominator for the financial institutions in the group. The payroll data for non-financial member of the group would not be used for any other calculation since only sales data is relevant to calculating their apportionment percentage.

V. Contentions of the Parties

Amex first contends that the position it advocates - inclusion of the payroll of all of the members of the combined group in the payroll denominator for the financial institution members of the group - is dictated by the plain language of the applicable statutes and regulations. Secondly, Amex maintains that the excluding the payroll of approximately twenty non-financial members of its combined group from Amex Centurion Bank's payroll factor violates the basic principle of combined reporting and radically distorts the amount of Amex Centurion's Bank income during the three years at issue, causing a degree of distortion that is impermissible under the U.S Constitution. These contentions, and OTR's arguments in opposition, will be discussed in turn.

A. The "Plain Language" of Statutes and Regulation

The Combined Reporting Statute In support of its plain language argument, Amex first cites the District's Combined Reporting statute, D.C. Official Code §47-1810.04(c). It provides:

(c) Except as provided in paragraph (3), the taxpayers share of the business income apportionable to the District of each combined group of which it is a member shall be the product of the:

(1) Business income of the combined group, and

(2) Taxpayer member's apportionment percentage, determined in accordance with this chapter, including in the property, payroll, and sales factor numerators of the taxpayer's property, payroll, and sales, respectively, associated with the combined group's unitary business in the District and including in the denominator the property, payroll, and sales of all members of the combined group, including the taxpayer, which property, payroll, and sales are associated with the combined group's unitary business wherever located. [Emphasis Added

(3) For taxable years beginning after December 31, 2014, the apportionment provisions of §47-1810.02(d-2) shall apply.¹³

¹³ D.C Official Code §47-1810.02(d-2) states:

(1) All business income shall be apportioned to the District by multiplying the income by the sales factor.

Amex maintains that the highlighted language, which prescribed how the apportionment percentage denominator was calculated from 2011 to 2014 when the District used a four factor formula, mandates that the payroll denominator for financial institutions include the payroll of all members of the group, even after the District stopped using the four factor formula. It argues that the adoption of the single sales factor in 2015 did not change the requirement that the denominator of any factor used to calculate the apportionment percentage for a member of the combined group include the relevant component (i.e. payroll, property, or sales) of all members of the combined group wherever located.

This is a logical stretch. Amex is extracting a piece of a formula no longer in effect and arguing that the extracted piece dictates what the components of the formula that replaced it must contain.

The Regulation on Combined Reporting for Mixed Groups In support of its position, Amex next cites a regulation addressing combined reporting for mixed combined groups, that include both financial and non-financial entities. That regulation, 9 DCMR 164.1, states in relevant part as follows:

Combined groups which include some members which are required to use the four (4)-factor apportionment formula and other members which are required to use a special apportionment method are subject to apportionment as described below:

(a) Combined group members who use the four (4)-factor formula and those that use special apportionment methods for purposes of allocation and apportionment shall prepare a federal consolidated pro forma return consisting of all combined group members,...

(b) Each member shall separately compute its District apportionment factor numerators, determine its District apportionment factor based on the group's denominators, and then apply its factors to the group's business income or loss subject to apportionment to arrive at net income or loss apportioned to the District; [Emphasis Added]

(2) This subsection shall be applicable for the tax years beginning after December 31, 2014.

In the accompanying chart, provided as an example for financial institutions, (9 DCMR 164.2) the payroll factor denominator for financial institution is calculated as the sum of the payroll in all states of all members of the combined group including the non-financial institutions.

In its opposition, OTR acknowledges that the above regulation, 9 DCMR 164, specifies that the denominator of the payroll factor for financial institutions include the payroll of both the financial and non-financial institutions, the position that Amex advocates. However, OTR maintains once the District adopted the single sales factor formula for non-financial institutions, the regulation was no longer in effect since it specifically contemplated that non-financial institutions use the four-factor formula as it applied to “[c]ombined groups which include some members which are required to use the *four (4)-factor apportionment formula* and other members which are required to use a special apportionment method. ” And since combined groups with members required to use the four-factor apportionment formula ceased to exist after the transition to the single sales factor in 2015, the regulation became irrelevant to apportionment calculations for mixed groups. In addition, OTR notes that the regulation was made obsolete by D.C. Official Code §47-1810.02(d-2), the statute that changed the District’s apportionment formula from a four factor formula to a single sales factor formula in 2015.

OTR maintains that its published guidance, the chart that appears above, was adopted to show taxpayers how to treat financial members in a mixed group once non-financial members no longer used a payroll factor, reflecting its determination that the special apportionment rules in 29 DCMR 129 would still apply to financial institutions in a combined group, but that the financial institution’s payroll factor would use a denominator consisting of only financial institutions in the combined group because the non-financial members of the group no longer used a payroll factor.

Discussion The “plain language” of the Combined Reporting Statute (D.C. Official Code §47-1810.04(c) or the Mixed Group Combined Reporting Regulation. (9 DCMR 164) does not resolve the issue of whether the payroll denominator for financial institutions consists of the payroll of all members of the combined group or only the payroll of the financial members, as Amex contends. Neither of these provisions directly address the issue. Both address the method for calculating the apportionment percentage using the four-factor formula, a formula no longer in use. Thus these provisions do not answer the question of how the payroll factor for financial

members of a combined group should be calculated after the transition to single sales factor formula.

That question is directly answered, however, by OTR's administration guidance, the Apportionment Factor Computation Chart (Schedule 2). That chart clearly shows how the payroll factor of the financial institution in a mixed combined group is to be calculated. As shown by the chart, the denominator of the payroll factor for the financial institution includes only the nationwide payroll of the financial institutions in the combined group and not the payroll of non-financial members.

Under the standard of review enunciated by the District of Columbia Court of Appeals, an agency's interpretations of the statutes and regulations it administers are owed great deference unless the agency's interpretation is plainly wrong or incompatible with the statutory purposes. *Tesfaramarian v. District of Columbia Dep't of Consumer & Regulatory Affairs*, 645 A. 2nd 1105, 1108 (D.C. 1994; *District of Columbia Office of Human Rights v. District of Columbia Dep't of Corr.*, 40 A.3d 917, 923 (D.C. 2012). (deference should be accorded agency's "interpretation of the statute and regulations it is charged by the legislature to administer, unless its interpretation is unreasonable or is inconsistent with the statutory language or purpose).

Here, no inconsistency with any statute or regulation has been demonstrated. In fact, OTR's administrative guidance answers a question left unanswered when the four-factor formula was abandoned, making the explanation in 9 DCMR 164 on how determine an apportionment percentage for a mixed group obsolete. Because 9 DCMR 164 was not amended to reflect the single sales factor, OTR's administrative guidance was published to show how to combine financial and non-financial institutions after the single sale factor formula was adopted. Even if there are reasonable alternative interpretations, the Office of Administrative Hearings, like Courts, must give deference to an agency's interpretation that is not plainly wrong or inconsistent with the legislative purpose. *District of Columbia Dep't of the Environment v. E. Capitol Exxon*, 64 A.3d 878, 879 (D.C. 2013). Accordingly, Amex's claim that the apportionment methodology in OTR's administrative guidance contravenes applicable District of Columbia statutes and regulations is rejected.

B. Claim of Constitutionally Impermissible Distortion

Amex next argues that if OTR's interpretation is found to be a permissible interpretation under District of Columbia law, the alternative interpretation it advocates should nevertheless be adopted because OTR's interpretation radically distorts the amount of Amex Centurion's Bank income during the three years at issue, causing a degree of distortion that is impermissible under the U.S Constitution.

Under the Constitution, each state in which a multistate taxpayer conducts business is entitled tax a fair share of the business's income using a reasonable apportionment methodology. To satisfy the Due Process and Commerce Clauses, state taxation on interstate commerce must be apportioned in a manner that reasonably approximates the relationship between a taxpayer's income attributed to a state and the taxpayer's business activity in the state. *Underwood v. Chamberlain* 254 U.S. 113, 119 (1920).

When reviewing challenges to apportionment formulas, the Supreme Court has recognized that "...States have wide latitude in the selection of apportionment formulas" *Morman v Bair* 437 U.S. 267, 274 (1978). A formula-based assessment that is "reasonably related to the activities conducted within the taxing State will only be disturbed when the taxpayer has proved by clear and cogent evidence that the income attributed to the State is in out of all appropriate proportion to the business transacted ...in that State" *Id.* (internal citations and quotes omitted). The Court has found that the application of a formula to a taxpayer violated due process only when the taxpayer demonstrated that a formula produced a tax on a percentage of its income that vastly exceeded the percentage of its income generated in the state. *Hans Rees Sons v. North Carolina* 283 U.S. 123 (1931) (formula that produced a tax on 83% of the taxpayer's income when only 17% of that income had its source in the State invalidated under the due process clause.)

In this case, Amex has attempted to demonstrate constitutionally impermissible distortion by comparing the size of the payroll factor when the denominator is the total payroll of all members of the Combined Group to the size of the payroll factor when the denominator is limited to the payroll of the two financial members. Amex provides this example: in 2015, Amex Centurion Bank's payroll in the District of Columbia was \$453,154. In that year, the payroll for all members of the Combined Group in 50 states was \$2,846,480,306, while the payroll for the two financial members of the Combined Group (Amex Centurion Bank and Amex Savings Bank) was

\$72,484,759. When the District of Columbia payroll for Amex Centurion in 2015 is divided by payroll for all members of the combined group, the resulting payroll factor is 0.000159198. When American Centurion Bank's payroll in the District is divided by the two financial members' payroll in the 50 states, the payroll factor is increased to 0.006251714. Given that the payroll factor makes up half of Amex Centurion Bank's apportionment percentage, Amex claims that OTR's methodology results in a nearly twenty-fold increase in Amex Centurion Bank's apportionment percentage for 2015.

This example focuses on the wrong metric for determining distortion. When assessing whether a state's apportionment formula ran afoul of the Constitution, the Supreme Court has examined *whether the formula produced a tax on a percentage of a multistate taxpayer's income that is out of all appropriate proportion to the business transacted in the state*. Amex analysis simply shows that computing the financial institution formula as it advocates produces a lower tax than OTR's method. Amex has presented no evidence, however, showing that the District's apportionment formula produces a tax on a percentage of its income that is out of all proportion with the business transacted in the District of Columbia and the income that that business generates.¹⁴ Such might be the case, for example, if Amex provided evidence showing that the District's formula resulted in taxation of 20% of its business income although transactions in the District of Columbia accounted for only 5% of its income.

Instead, Amex has simply shown that the apportionment formula it advocates results in a lower apportionment percentage for American Centurion Bank than the percentage that results from the formula used by OTR. To establish constitutionally impermissible distortion, Amex would have to prove "by clear and cogent evidence that the income attributed to the State is in or out of all

¹⁴ In 2015, Amex Centurion Bank's payroll in the District of Columbia was \$453,154. The District has a population of approximately 700,000 and has about 20 million visitors annually. It is therefore likely that the payroll required to support business transacted by Amex in the District of Columbia greatly exceeds a payroll of \$450,000 and that most of the payroll expense needed to support District of Columbia business is paid to employees working in other jurisdictions.

As a result, the numerator of the payroll factor (payroll paid in the District of Columbia) is probably small in light of the business transacted. A smaller numerator results in a smaller apportionment percentage. This could explain why OTR's method of calculating the payroll factor for a financial institution may not result in a tax out of proportion with business transacted in the District of Columbia, even though it may have produced, for example, a nearly twenty-fold increase in Amex Centurion Bank's apportionment percentage in 2015.

appropriate proportion to the business transacted ...in that State. Amex has not done so and its claim of constitutionally impermissible distortion has therefore not been established.

VI. Order

It is therefore this 19th day of April, 2022:

ORDERED, that Amex's Motion for Summary Adjudication is **DENIED** and OTR's Cross-Motion for Summary Adjudication is **GRANTED**. Amex's protests of the Notices of Proposed Assessment for Tax Years 2015, 2016, and 2017 are dismissed and the Notices of Proposed Assessment are **AFFIRMED**.

ORDERED, that the appeal and reconsideration rights of any party aggrieved by this Order appear below.

/s/ Mary Masulla

Mary Masulla
Administrative Law Judge

APPEAL RIGHTS

After an administrative law judge has issued a Final Order, a party may ask the judge to change the Final Order and may ask the District of Columbia Court of Appeals to change the Final Order. There are important time limitations described below for doing so.

COVID-19 NOTICE: The deadlines described below may be temporarily suspended or extended due to the COVID-19 pandemic. For up-to-date information about any changes to these deadlines, please visit the Office of Administrative Hearings website at <https://oah.dc.gov> and the D.C. Court of Appeals website at <https://www.dccourts.gov/court-of-appeals>.

HOW TO REQUEST THE ADMINISTRATIVE LAW JUDGE TO CHANGE THE FINAL ORDER

Under certain limited circumstances and within certain time limits, a party may file a written request with the Office of Administrative Hearings (OAH) asking the administrative law judge to change a final order. OAH Rule 2828 explains the circumstances under which such a request may be made. Rule 2828 and other OAH rules are available at <https://oah.dc.gov> and at OAH's office. Rule 2828 states that a request to change a final order "shall state whether an appeal [to the District of Columbia Court of Appeals] has been filed. If an appeal has been filed, OAH has no jurisdiction to decide" the request unless the Court of Appeals has remanded the case to OAH for that purpose.

A request to change a final order does not affect the party's obligation to comply with the final order and to pay any fine or penalty. If a request to change a final order is received at OAH **within 10 calendar days** of the date the Final Order was filed (**15 calendar days** if OAH mailed the final order to you), the period for filing an appeal with the District of Columbia Court of Appeals does not begin to run until the Administrative Law Judge rules on the request. **A request for a change in a final order will not be considered if it is received at OAH more than 120 calendar days of the date the Final Order was filed (125 calendar days if OAH mailed the Final Order to you).**

HOW TO APPEAL THE FINAL ORDER TO THE DISTRICT OF COLUMBIA COURT OF APPEALS

Pursuant to D.C. Official Code § 2-1831.16(c)-(e), any party suffering a legal wrong or adversely affected or aggrieved by this Order may seek judicial review by filing a Petition for Review and six copies with the District of Columbia Court of Appeals at the following address:

Clerk
District of Columbia Court of Appeals
430 E Street, NW, Room 115
Washington, DC 20001

The Petition for Review (and required copies) may be mailed or delivered to the Court of Appeals, and must be received there within 30 calendar days of the mailing date of this Order, pursuant to D.C. App. R. 15(a)(2). There is a \$100 fee for filing a Petition for Review. Persons who are unable to pay the filing fee may file a motion and affidavit to proceed without the payment of the fee when they file the Petition for Review. Information on petitions for review can be found in Title III of the Court of Appeals' Rules, which are available from the Clerk of the Court of Appeals, or at <https://www.dccourts.gov/court-of-appeals>.

Certificate of Service:

By E-mail

Kiara Rankin, Principal
Ernst & Young LLP
1401 McKinney Street, Suite 2400
Houston, TX 77010
Email: kiara.rankin@ey.com

D.C. Office of Tax and Revenue
1101 Fourth Street, SW, Room 7576
Washington, DC 20024
OTRLitigation@dc.gov.

Attn: [Aaishah.hashmi](mailto:Aaishah.hashmi@dc.gov)
Aaishah.hashmi@dc.gov

I hereby certify that on April 19, 2022, this document was served upon the parties named on this page at the address(es) and by the means stated.

/s/ Starr Gantt
Clerk / Deputy Clerk

