



Legal Alert: MTC Executive Committee Advances Significant Part of UDITPA Rewrite

May 9, 2014

On Thursday, May 8, the Multistate Tax Commission's (MTC) Executive Committee (Committee) met in Washington, DC. During the meeting the Committee voted to advance its amendments to the Multistate Tax Compact's (Compact) definition of nonbusiness income, definition of "sales," factor weighting, and the sourcing of service and intangible revenue. The next step in the Compact's amendment process—which is identical to the Uniform Division of Income for Tax Purposes Act (UDITPA)—is a "Bylaw VII" survey by the MTC member states. The Committee essentially embraced the MTC's original proposed amendments and failed to incorporate any of the comments and observations of its Hearing Officer, Professor Richard Pomp.

Additionally, the Committee took split actions on amendments to Section 18, which contains the MTC's alternative apportionment provision. Professor Pomp proposed four changes to Section 18. The Committee, by one vote, moved to a Bylaw VII survey of Professor Pomp's Section 18 proposal barring, in general, the retroactive revocation of alternative apportionment. In two other close votes, the Committee sent the Section 18 proposals regarding the burden of proof and no penalties back to the MTC Uniformity Committee for possible revisions. The Committee did, however, flatly reject the Hearing Officer's Section 18 proposed "unique" and "non-recurring" language that would require regulations where states routinely applied Section 18 to similar facts.

In effect, Bylaw VII surveys are a way for the MTC to portend the adoption of a recommendation by the Committee. A Bylaw VII survey is a poll of the MTC member states regarding whether they would "consider adopting" a draft proposal relating to uniform or compatible tax laws, regulations, or administrative practices—not whether they will, in fact, adopt the proposal. Should a majority of the MTC member states polled report that they would consider adopting the draft proposal, the proposal is referred to the MTC for possible adoption as a uniformity recommendation. In reality, most

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states do not adopt the uniform proposals even if they indicate interest in the Bylaw VII survey.

The primary recommendation to advance to a Bylaw VII survey is the Committee's proposal to change Section 17. Section 17 applies to the sourcing of sales, other than the sale of tangible personal property. The proposal switches the sourcing from the traditional cost of performance method to a market-based sourcing methodology.

Section 9 of the Compact involves factor weighting for purposes of apportioning multistate income. As currently enacted, Section 9 provides for an equally weighted formula consisting of the sum of a taxpayer's property, payroll, and sales factors divided by three. The Committee's recommendation provides for amending the language such that the member states are able to define their own factor weighting fraction, within the recommended definition, as long as the formula uses a double-weighted sales factor.

The proposed revision to Section 1(a) of the Compact replaces the concept of business income with the phrase "apportionable income." The phrase essentially requires the apportionment by looking to a constitutional standard. In addition, the definition—among other revisions—exchanges the language "constitute integral part of" for "is or was related to the operation of," and also removes the word "regular" in describing what income arises from tangible and intangible property in the taxpayer's trade or business.

Lastly, the advancing Section 1(g) amendment changes the definition of "sales" to expressly exclude Treasury and hedging activities. The amendment passed by the Committee is substantially the same as originally proposed by the Uniformity Committee, except the Executive Committee removed language that allowed the receipts from securities dealers to be included.

It is possible that the Bylaw VII survey results may be complete enough so that the full MTC can vote on the amendments during its annual meeting at the end of July. The MTC has yet to fully articulate its intended process for adopting these significant amendments to the Compact, which has not been

amended since adopted by many states in the late 1960s.

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