# MULTISTATE TAX COMMISSION

## Twentieth Annual Report

## 1986 - 1987

For the fiscal year of
July 1, 1986 - June 30, 1987

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# The Multistate Tax Commission: An Introduction and Overview

The Multistate Tax Commission is an organization of states created for the purpose of bringing some order to the state taxation of multistate businesses. Recognizing both the confusion to taxpayers and the dangers of federal preemption created by the then-current plethora of state laws and practices, the Multistate Tax Compact was developed in 1966 as a means by which to develop alternative approaches. Activated in 1967, the Commission has nineteen members, including the District of Columbia; another ten states have been granted associate membership at their request.

The purposes of the Commission are stated in the Compact: to facilitate proper determination of state and local tax liability of multistate taxpayers, to promote uniformity or compatibility of tax systems, to facilitate taxpayer convenience and compliance, and to avoid duplicative taxation. The Commission acts as a resource to those ends through research and publication, seminars, litigation, and the conducting of a joint audit program, and through representation of member state interests in Washington, D.C.

States join the Commission by enacting the Multistate Tax Compact, which incorporates the Uniform Division of Income for Tax Purposes Act (UDITPA). This act provides ground rules for apportioning income of multistate businesses to all states in which the taxpayer does business. All business income is apportioned according to a formula which takes into account the in-state payroll, property, and sales of a corporation as fractions of its total payroll, property, and sales; these fractions are then averaged and the result is the percentage of a taxpayer's total income which is apportioned to that state for tax purposes. Non-business income (such as that from passive investments) is allocated to the state in which the corporate domicile is located. This simple approach (though occasionally complex in application) was designed to ensure that there would be no double taxation and no undertaxation of corporate income were all states to enact the law. To avoid double sales taxation, the Compact also includes a uniform credit provision to prevent a transaction from being taxed twice.

When a state joins the Commission, the director of its tax agency becomes that state's representative on the Commission. The full Commission meets annually, normally in July of each year; between meetings, the Commission's affairs are supervised by an Executive Committee consisting of the officers of the Commission (Chairman, Vice-Chairman, and Treasurer), and four members elected by the full Commission. Past Chairmen serve as ex officio members. The operations of the Commission are carried out by a staff headed by the Executive Director. The administrative and legal staffs are located at the headquarters office in Boulder, Colorado (soon to be relocated to Washington, D.C.); the Commission also maintains audit offices in Chicago, Houston, and New York City, and has a representative in Washington, D.C. Commission operations are funded by administrative dues (apportioned according to tax revenues) and audit fees from the member states.

## The Joint Audit Program

The Commission differs from other interstate and tax organizations in that it serves as an operating arm of member states through the joint audit program. Member states pool their resources to select candidates for corporation income, sales and use, franchise and gross receipts tax audits. The MTC audit staff members perform these audits just as though they were part of a state's own audit staff, forwarding their findings and recommendations to the member states for assessment and collection at the completion of the audit. A single MTC audit takes the place of separate and duplicative audits by member states, and provides obvious economies of scale to the states. At the same time, it relieves the taxpayer of the burden of multiple audits. The MTC provides businesses with a forum through which to seek resolution of inconsistencies in the state tax rules which become apparent during a joint audit.

Aside from its economies of scale and its financial benefits—in fiscal 1986-87 the member states received approximately $20 in suggested tax assessments for each dollar invested in the program—the audit program serves the Commission's goals in other ways as well. States learn of any inconsistent reporting to different states by multistate taxpayers. In cases in which settlements of disputes are negotiated, the states' bargaining power is improved by their joining together; by the same token, corporate taxpayers sometimes find it less burdensome to negotiate with one representative than with numerous individual state tax agencies. Finally, states gain a tool for determining how well the theoretical compatibility of their tax laws works on a day-to-day basis.

The program is a supplement to, and not a replacement for, the audit activities of the member states. But it can offer a significant addition for a smaller state, and can provide useful support to a larger one. States maintain control of the program through selection of the audit candidates; they make the decision as to whether or not to participate in a given audit and as to whether and how to act upon the audit results. The Audit Committee and its oversight subcommittee, consisting of the audit and compliance directors of member state tax agencies, guide the program and ensure that it is responsive to member state needs.

## Legal Assistance

The taxation of interstate businesses is a complex legal specialty, and state revenue counsel and assistant attorneys general, spread thin over many kinds of cases, face great difficulty in trying to keep up with the myriad of developments within their own states as well as in trying to keep track of how other states may have confronted similar issues. The MTC maintains a staff of two lawyers whose fulltime specialty is the state taxation of multistate business activity. The legal staff provides information in response to state requests, does research on multistate issues, acts as a legal resource for the audit program, and is generally available to assist states in any way possible. MTC legal personnel have been involved directly in cases ranging from district courts to the U.S. Supreme Court, occasionally with the MTC as a litigant, but more commonly with the MTC as an *amicus curiae*. Part of that assistance takes the form of seminars for both state officials and the general tax community. MTC legal staff also frequently participate as speakers and discussants in tax meetings nationally.

## Uniformity

In order to relieve businesses of the problems of compliance with fifty-one different tax laws, the Commission is charged in the Compact with the promotion of uniformity or compatibility in tax laws. To achieve that end, the Commission has a Committee on Uniformity which studies problems and recommends possible solutions. One approach that the Commission has taken is to develop, through a formal hearing process, model uniform regulations for consideration and adoption by states. To date, the Commission has adopted model regulations interpreting the allocation and apportionment sections of the UDITPA provisions of the Compact; it has also adopted regulations for specialized industries to which the standard three-factor formula does not fairly apply. Regulations promulgated to date cover railroads, airlines, trucking and contractors for corporate income tax purposes and recordkeeping for sales and use tax purposes. In addition, the Commission has developed a uniform sales and use tax exemption certificate which is widely used. The Commission has also adopted a useful statement concerning the members' interpretation of Public Law 86-272 (see Appendix F). Finally, the Commission has promoted uniform agreements for the exchange of information among the states relating to sales and use and income taxes.

The pursuit of uniformity is important not only as a means of easing the taxpayers' burden of compliance and the administrators' burden of enforcing compliance, but as a means of demonstrating that the states, working together through the Commission, can develop solutions to these problems without federal preemption. If the Federal Government were to begin to restrict the ability of the states to administer their own tax laws, it could set precedents for future interventions which would undermine the very nature of the federal system.

## Federal Policy Issues

The Commission has always strongly opposed restrictive federal legislation in matters of state taxation; such intervention contravenes the very purpose of a federal system of government. Though the Commission is perhaps best known for its defense of the states' right to use worldwide combination in the income tax area, it is important to note that this was so not only because many of the member states preferred that method, but also because all member states felt that the federal government should not, as a matter of principle, dictate to the states how they should exercise their constitutional right to tax. While several states have moved away from worldwide combination—partly as a result of their participation with the Commission in the President's Working Group on Unitary Taxation—the Commission remains firmly opposed to any federal restriction on worldwide combination, or on any other constitutional method of taxation which a state chooses to adopt.

To monitor federal developments and provide information on state views to Congress and the Executive Branch, the Commission is represented in Washington, D.C. by the firm of Rosapepe, Powers and Spanos.

The Commission is not merely committed to opposition to federal restriction, however; by its actions in the joint audit program, the work of the Uniformity Committee, the development of model laws and regulations, and the work of its educational programs and publications, the Commission aims to demonstrate that it is possible to address the problems of multistate taxation in a cooperative manner and thereby alleviate some of the problems which gave rise to the requests for federal restriction in the first instance. John Shannon, the Executive Director of the U.S. Advisory Commission on Intergovernmental Relations, has referred to the 1980s as the age of "do-it-yourself federalism". It is a matter of considerable pride to the member states that, in

# REPORT OF THE EXECUTIVE DIRECTOR

It has been traditional for the Report of the Executive Director to review the highlights of the immediate past fiscal year's operation of the Commission. However, some departure from that practice is demanded by certain recent events that will have a far-reaching impact on the future of the Commission. In May of 1987, the Commission members and staff endured one and one-half days of a rigorous goals and objectives planning session held in Denver. From that session, a consensus regarding several organizational goals was reached. Among the goals to be pursued over the next two to three year period were the following:

1. Expansion of membership through exploring of different membership options.
2. Improvement of relationships with other state tax organizations such as NATA.
3. Re-examination of the Commission's organizational structure.
4. Advancement of procedural uniformity with regard to areas such as filing dates, extended dates, interest computations, domestic disclosure spreadsheets, and the like.
5. Computerization of the MTC Joint Audit Program.
6. Development of a Centrally-Assessed Property Tax Project.

In September, the Commission formally adopted a motion to move its Executive office to the Washington, D.C. area in order to more effectively pursue certain of the goals decided upon at its May meeting. The decision to move was not an easy one to make; and it is one that necessarily results in disruption and dislocation of the current administrative staff. The term "painful" is accurate in many respects to describe the decision and its effect upon staff members. While the pessimist may perceive that pain as symptomatic of an injury, the optimist will liken it to that associated with an acceleration of growth and development.

While the pessimist may view the Commission's move as jumping without a parachute from a "mile-high" precipice, the optimist will liken the Commission's decision to that of following one of several possible forks at one of the many crossroads that we all personally or professionally meet along the way. The direction along the particular fork that the Commission now takes is an exciting and challenging one; and the successful response to that challenge remains in the hands of the Tax Administrators of the member states. These are the best of times for the optimists among us.

# MAJOR TAX POLICY ISSUES ADDRESSED BY THE COMMISSION STATES

**Income Tax**

This past year has seen continued action on behalf of the worldwide combination states to move to a water's edge approach as suggested by Option Two of the Report of the President's Working Group on Unitary Taxation. While some progress in the area of Section 482 training has been experienced, little evidence of additional federal assistance to the states has been forthcoming from Treasury. In any event, the states have certainly lived up to the spirit of the Working Group effort, with only Alaska now remaining as a worldwide state; and it faces no business pressure to do otherwise, given its unique tax base.

What once was to be a federally-required filing of a "domestic disclosure spreadsheet" has now become a requirement of certain states. The states of California, Idaho, Montana, and North Dakota will require the filing of such a spreadsheet as an incident to their withdrawal from requiring worldwide combination. In an effort to reduce the taxpayer's administrative burden of filing the spreadsheets, these states have been working together to arrive at a common disclosure form that will be acceptable to all of the states. The principal goal shared by the states is to require the disclosure of only that amount of information that is consistent with the intent under the new statutes, without undue imposition on the taxpayer.

The ghost of the bill introduced by Senator Pete Wilson (R-Calif), S.1974, has appeared in the form of Rep. Frenzel's H.R.2940. That apparition, too, should disappear, as the states have substantially accomplished voluntarily what they suggested to the Working Group's Option Two. In light of the states' voluntary withdrawal from the legally acceptable worldwide concept that was approved by the United States Supreme Court in the *Container* case, the promotion of federal intervention at this time would be improper and undesirable. As discussed further below, the Commission states have expended a great amount of energy through the workings of the Uniformity Committee on several key income tax issues during the past year. While those issues do not receive nearly the public attention that the worldwide combination issues do, they have a significant impact on the administration of the states' corporate income taxes.

**Sales Tax**

The Commission's support for the Congressional effort to obtain reversal of the *National Bellas Hess* decision, which currently limits the states' power to require direct marketers to collect the states' use taxes, is now in full gear. Bills introduced by Representatives Brooks (D-Texas) (H.R.1891) and Dorgan (D-ND) (H.R.1242) and Senators Cochran (R-Miss) (S.1099) and Burdick (D-ND) (S.639) have been heard in the respective subcommittees. Joint testimony in support of the Senate bills was provided by Hal Hansen, Chairman of the MTC and John Baldwin, President of NATA. Rep. Dorgan's bill has been favorably marked up and voted out of subcommittee to the House Ways and Means Committee. As amended in subcommittee, H.R.1242 contains all of the substantive provisions of Rep. Brooks' H.R.1891 that was drafted by NATA.

**Taxation of Centrally-Assessed Properties**

The adverse decision in *Burlington Northern Railroad Co. v. Oklahoma Tax Comm'n.*, ___ U.S. ___, 95 L.Ed.2d 404 (1987) has prompted the states to increase the coordination of their efforts with respect to the property taxation of centrally-assessed properties. Initially, this coordinated effort will focus on the transportation industries that have received special Congressional protection; and it will be facilitated by MTC staff. The involvement of the MTC in this effort will depend, in large part, on the willingness and ability of the affected state and local governments to contribute funding and in-kind resources. The contemplated MTC special project would address problems with regard to the taxation of centrally-assessed properties, such as railroads, airlines, trucking and telecommunications companies and public utilities that operate interstate.

**Uniformity**

One of the principal purposes of the Multistate Tax Commission that is established by the Multistate Tax Compact is the promotion of "uniformity or compatibility in significant components" of state tax systems. The Commission's Uniformity Committee has worked diligently this past year to push this gargantuan effort forward. Under the Chairmanship of Philip Aldape, Bureau Chief, Income and Inheritance Tax for the State of Idaho, much progress has been achieved.

Several studies and recommendations are at various levels of development before the Uniformity Committee. On the Committee agenda are recommendations to advance uniformity with respect to a diverse range of state income and sales/use tax issues. Among them are recommendations affecting the following subjects:

1. The treatment of intangible drilling costs and royalties in the property factor of the apportionment formula.
2. Formulae for apportionment of business income derived from the financial and broadcasting industries.
3. The definition of terminology regarding canned and customized computer software.
4. The deductibility of foreign taxes.
5. The taxation of master limited partnerships.
6. The treatment of diverse businesses with regard to whether they are combinable.
7. Issues of a procedural nature, such as dates for tax return filing or extension, the effect of I.R.S. Revenue Agent Reports on the scope of adjustments for state tax returns, statutes of limitation and the like.
8. Clarification of the dock sale concept.
9. Treatment of income or loss derived from the sale of partnership interests.
10. Various sales/use tax issues that lend themselves to a uniform approach.

The Uniformity Committee has also prepared the agenda regarding the states' review for possible revision of current regulations or creation of new regulations for certain portions of the Uniform Division of Income for Tax Purposes Act. This agenda has been derived from earlier MTC surveys of the states regarding the operation of UDITPA. A review of the items listed below makes evident the fact that several years will be necessary to complete this effort. The issues that have been determined by the Uniformity Committee to be most pressing are:

1. Sales Factor Issues.
   a. Receipts from intangibles such as patents, copyrights, bonds, stocks and sales of stocks.
   b. Sales of services: the all or nothing "greater proportion" rule.
   c. Dock sales clarification.
   d. Attribution of sales of mobile/moveable property.
   e. Throw-out versus throw-back rule for non-jurisdictional sales.
   f. Refinement of rental versus service rules.

g. Review of Art.IV.16.(b): "not taxable in the state of the purchaser" concept in relation to P.L. 86-272 and sales to foreign countries.

2. Property Factor Issues.
   a. Government-owned property.
   b. Mobile/moveable property.
   c. Throw-out rule for certain types of property, e.g., satellites, undersea cables, air transportation property.
3. Payroll Factor Issues.
   a. Treatment of payments to independent contractors.
   b. Modification of "Base of operations" and "place where service is directed" concepts.
4. General Apportionment or Base Issues.
   a. Reflection of dividend payor's factors in recipient's sales factor.
   b. Factors to use in installment sales situation.
   c. Factor and business/non-business issues in deferred income situations, e.g., like-kind exchanges, involuntary conversions, etc.
   d. Treatment of long-term construction contracts.
   e. Partnership distribution of business and non-business income.
   f. Assignment of income from sale of partnership interest.
   g. Business/non-business income treatment of interest and dividends.
   h. Amendment of UDITPA's Section 18 relief provision with regard to nature of showing that has to be made to obtain adjustment.
   i. Net operating loss rules for apportioning corporations.
   j. Combination.
      1) Definition of unitary business.
      2) Uniform unity of ownership rules.
      3) Treatment of diverse business operations.
      4) Uniform rules regarding mechanics of combination.
      5) Allocation of interest expense.
      6) Deferred intercompany transactions (including factor and business/non-business character).
      7) Water's edge limitation and spreadsheet requirements.

## JOINT AUDIT PROGRAM

The Commission's Joint Audit Program has continued its development as an extension of and a supplement to audit programs operated by the states themselves. This year's effort, directed by the Audit Oversight Subcommittee and the full Audit Committee and chaired by Jeff Miller, Chief of the Montana Corporate Tax Bureau, resulted in measurable improvement of the Joint Audit Program's reporting procedures and direction. Non-member states can now join the Joint Audit Program either as full Commission members or on a contractual basis for a limited number of years. Benefits are measured not only in terms of revenue production but in terms of the opportunity for states to exchange ideas and information with respect to specific taxpayers and to audit policy in general.

The State of Nebraska has joined the MTC Joint Audit Program on a contractual basis for a two-year period. Nebraska now participates in other programs of the Commission as well. Its addition to the Program enhances the resources upon which the MTC can rely.

The Executive Committee and the Audit Committee continued their support for the Program by approving a plan to provide the Commission's auditors with access to a number of lap-top and desk-top computers over the next two years. Increased audit productivity at reduced cost is anticipated.

This year's audit production exceeded $22,000,000 in recommended assessments. This figure, which includes negotiated settlements of more than $3,900,000 obtained by the legal staff, exceeds the Program's past four years' average cost/benefit ratio of nearly $20 returned for every $1 invested in the Program. The improvements initiated through the efforts of the Audit Committee are now coupled with the continuing commitment to excellence held by the Commission's audit staff. That staff is directed by Audit Managers Bob Milligan, Mort Kotkin and Jerry Birk. They have continually demonstrated loyalty and support of the Commission's efforts; and they form a solid basis for the future growth and continued success of the Joint Audit Program.

## LEGAL ASSISTANCE AND LITIGATION

The legal staff continued to concentrate on providing assistance to the MTC audit staff, as well as to the Executive, Audit and Uniformity Committees of the Commission. In addition, staff counsel presented speeches throughout the country at meetings of tax professionals; conducted surveys of states' tax practices; and published articles in the MTC Review and elsewhere in furthering the goals of the Commission. In addition, MTC counsel have provided their resources in the development of regulations dealing with such areas as the treatment of intangible drilling costs, royalties, definitions for computer software, dock sales treatment, and apportionment issues concerning the financial and broadcasting industries, to cite a few examples.

On several occasions, direct consulting was provided to state legal and audit staffs in cases dealing with taxation of interstate enterprises. This assistance has even taken the form of drafting a model response to protests arising from an MTC audit. On other occasions, the MTC legal staff has prepared and filed *amicus curiae* briefs in various courts around the country.

The special projects of the Commission, e.g., the *National Bellas Hess* Project in which twenty-nine states participate, and the newly initiated Centrally-Assessed Property Tax Project, have been developed and supported by MTC legal counsel. Legal counsel have successfully negotiated multistate settlements of both income and sales/use tax liability, through the *National Bellas Hess* Project and otherwise amounting to payments in excess of $2,800,000.00 to the state participants during the year.

As reflected by the foregoing synopsis, it was a most productive year for the Commission in many respects. Much has been accomplished; and much more remains to be done. The Commission's priorities for future efforts have been brought into clear focus and are within its reach. The next two to three years will provide it with an opportunity to obtain increased coordination with other organizations as well as to continue its varied contributions to the most challenging areas of state taxation.

# Staff Members

### Acting Executive Director/Deputy General Counsel

Alan H. Friedman's legal experience over some twenty years has included positions as legal counsel with the U.S. Justice Department, the U.S. Senate, and the Colorado Attorney General's Office. As First Assistant Attorney General, he supervised the legal representation of Colorado's Governor, Secretary of State, Treasurer and, finally, Department of Revenue of which he last served as Deputy Director. He is a graduate of the University of California at Berkeley and of Boalt Hall Law School at that University.

### General Counsel

Eugene F. Corrigan became the Commission's General Counsel in February, 1985 after having served for sixteen years as its Executive Director. His prior experience included three years as a Sears, Roebuck tax attorney and ten years with the Illinois Department of Revenue, in the Chicago office of which he last served as Chief Counsel. During the mid-sixties, he was also a partner in the Chicago law firm of Stradford, Lafontant, Fisher and Corrigan. He is a graduate of Princeton University and of John Marshall Law School of Chicago. He is a Past Chairman of the Urban State and Local Government Law Section of the American Bar Association.

### Program Coordinator

Clela A. Rorex joined the MTC in 1981. She holds a Bachelor of Arts Degree and a Master's Degree in Public Administration from the University of Colorado. Her previous experience includes service as: the publicly elected Clerk and Recorder of Boulder County; acting general manager of the Colorado Music Festival; business manager for the Sacramento Civic Theatre; insurance and financial counselor; manager of the Visiting Scientists Program of the Joint Institute for Laboratory Astrophysics at the University of Colorado; and management representative at the U.S. Naval Exchange at Guantanamo Bay. She also wrote and published the first edition of the Colorado Legislative Almanac.

## Audit Managers

**Chicago/Houston**: Robert Milligan was a corporate accountant for nearly ten years. He was the Tax Manager of two different corporations prior to joining the Michigan Department of Revenue as an auditor in 1961. There, he audited for Income, Sales and Use, Franchise, Intangibles, Business Activities and other taxes until 1977, when he joined the staff of MTC.

**New York**: Gerald Birk and Morton Kotkin have served as Income Tax Audit Manager and Sales Tax Audit Manager, respectively, since February, 1986. Gerald Birk has been with the Commission for five years. Before joining the MTC in 1981, he had been an auditor and audit supervisor with the New York office of the California Franchise Tax Board for eight years. A native of Brooklyn, New York, he graduated from Long Island University in 1973 with a Bachelor of Science Degree in Accounting. Morton Kotkin has served with the Commission as a Senior Auditor, Eastern Regional Manager and Senior Review Auditor. Before joining the MTC in 1974, he had been an auditor and field audit supervisor with the New York office of the California State Board of Equalization for twelve years, performing and supervising sales, use, property and cigarette tax audits of California's largest out-of-state taxpayers. Also a native of Brooklyn, he graduated from New York University in 1961 with a Bachelor of Science Degree in Accounting.

## Consultants

William D. Dexter has served the MTC in an Of Counsel capacity since July 1983 when he retired as General Counsel, a position which he had held since 1975. He had been an Assistant Attorney General for the Washington Department of Revenue from 1969 to 1975. He had previously served for many years as the Assistant Attorney General in charge of revenue litigation for the State of Michigan.

James Rosapepe has served as Legislative and Media Consultant for the MTC since 1977. He is a partner in the firm of Rosapepe, Powers and Spanos in Washington, D.C.

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Ken Capek *(Alternate)*
Chief of Audit
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Olympia, WA 98504
(206)753-3320

1 The Executive Secretary of the Board of Equalization represents California in MTC fiscal years beginning in odd-numbered calendar years; the Executive Officer of the Franchise Tax Board represents California in MTC fiscal years beginning in even-numbered calendar years.

2 MTC Chairman 1979-1980

3 MTC Chairman 1984-1985

4 MTC Chairman 1985-1986

5 MTC Chairman 1986-1987

# Tax Administrators Associate Member States *

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Department of Revenue
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**Arizona**
C. Hos Hoskins
Director
Department of Revenue
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1600 W. Monroe
Phoenix, AZ 85007
(602)255-3572

**Georgia**
Marcus E. Collins, Sr.
Commissioner
Department of Revenue
410 Trinity-Washington Bldg.
Atlanta, GA 30334
(404)656-4016

**Louisiana**
Shirley McNamara
Secretary
Dept. of Revenue & Taxation
PO Box 201
Baton Rouge, LA 70821
(504)925-7680

**Maryland**
Louis L. Goldstein
Comptroller of the Treasury
Goldstein Treasury Building
PO Box 466
Annapolis, MD 21404
(301)974-3801

**Massachusetts**
Stephen W. Kidder
Commissioner
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**New Jersey**
John R. Baldwin
Director
Division of Taxation
Department of Treasury
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(609)292-5185

**Ohio**
Joanne Limbach
Tax Commissioner
Department of Taxation
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Columbus, OH 43216
(614)466-2166

**Pennsylvania**
Barton A. Fields
Acting Secretary of Revenue
Department of Revenue
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Harrisburg, PA 17127
(717)783-3680

**Tennessee**
Dudley W. Taylor
Commissioner
Department of Revenue
Andrew Jackson State Office Bldg., Rm. 927
Nashville, TN 37242
(615)741-2461

*The Commission has made provisions for association membership in bylaw 13 as follows:
13. Association Membership
(a) Associate membership in the Compact may be granted, by a majority vote of the Commission members, to those States which have not effectively enacted the Compact but which have through legislative enactment made effective adoption of the Compact dependent upon a subsequent condition or have, through their Governor or through a statutorily established State agency, requested associate membership.
(b) Representatives of such associate members shall not be entitled to vote or to hold a Commission office but shall otherwise have all the rights of Commission members.

Associate membership is extended especially for states that wish to assist or participate in the discussions and activities of the Commission, even though they have not enacted the Compact. This serves two purposes: (1) it permits and encourages states that feel that they lack knowledge about the Commission to become familiar with it through meeting with the members, and (2) it gives the Commission an opportunity to seek the active participation and additional influence of states which are willing to assist in a joint effort in the field of taxation while they consider or work for enactment of the compact to become full members.

# Tax Administrators Non-Member States

**Connecticut**
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Commissioner
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**Delaware**
Robert W. Chastant
Director of Revenue
Department of Finance
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820 N. French Street
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**Florida**
Randy Miller
Executive Director
Florida Dept. of Revenue
102 Carlton Building
Tallahassee, FL 32399-0100
(904)488-5050

**Illinois**
Roger D. Sweet
Director
Illinois Dept. of Revenue
PO Box 3681
Springfield, IL 62708
(217)785-2602

**Indiana**
M.F. Renner
Commissioner of Revenue
Indiana Dept. of Revenue
202 State Office Building
Indianapolis, IN 46204
(317)232-2101

**Iowa**
Gerald D. Bair
Director
Iowa Dept. of Revenue & Finance
Hoover State Office Bldg.
Des Moines, IA 50319
(515)281-3204

**Kentucky**
Gary W. Gillis
Secretary
Revenue Cabinet
Capital Annex
Frankfort, KY 40620
(502)564-3226

**Maine**
Anthony J. Neves
State Tax Assessor
Bureau of Taxation
State Office Building
Augusta, ME 04333
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**Mississippi**
C.A. Marx
Chairman
Tax Commission
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**Nebraska**
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**Nevada**
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**New Hampshire**
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**New York**
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**North Carolina**
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**Virginia**

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**West Virginia**

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**Wisconsin**

Karen A. Case
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**Wyoming**

Shirley Wittler
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# Multistate Tax Commission

# Report of Certified Public Accounts

*Balance Sheet*

Executive Committee
Multistate Tax Commission
Boulder, Colorado

We have examined the balance sheet of Multistate Tax Commission as of June 30, 1987 and 1986, and the related statements of revenues and expenses, and changes in fund balance and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of Multistate Tax Commission at June 30, 1987 and 1986, and the results of its operations, and changes in fund balance, and changes in financial position for the years then ended in conformity with generally accepted accounting principles applied on a consistent basis.

Rhode, Scripter & Associates

August 19, 1987

MULTISTATE TAX COMMISSION

## BALANCE SHEET
June 30, 1987 and 1986

### ASSETS

| | 1987 | 1986 |
|---|---|---|
| CURRENT ASSETS | | |
| Cash (including certificates of deposit of $450,000 and $544,533 in 1987 and 1986 respectively) | $ 837,141 | $ 629,922 |
| Accounts receivable--members | 155,293 | 32,400 |
| Accrued interest receivable | 9,444 | 8,408 |
| Receivable from termination of pension plan--Note 2 | --- | 299,523 |
| Investments | 253,689 | --- |
| Prepaid insurance | 6,723 | --- |
| TOTAL CURRENT ASSETS | 1,262,290 | 970,253 |
| PROPERTY AND EQUIPMENT--Note 3 | | |
| Office furniture and equipment | 254,113 | 242,003 |
| Leasehold improvements | 2,235 | 2,235 |
| | 256,348 | 244,238 |
| Less: Accumulated depreciation and amortization | 177,152 | 144,006 |
| TOTAL PROPERTY AND EQUIPMENT | 79,196 | 100,232 |
| OTHER ASSETS | | |
| Expense account advances | 3,250 | 4,500 |
| Deposits | 3,081 | 2,696 |
| TOTAL OTHER ASSETS | 6,331 | 7,196 |
| TOTAL ASSETS | $1,347,817 | $1,077,681 |

Exhibit A

## LIABILITIES AND FUND BALANCE

| | 1987 | 1986 |
|---|---|---|
| CURRENT LIABILITIES | | |
| Accounts payable | $ 34,478 | $ 10,675 |
| Accrued vacation pay | 83,043 | 80,866 |
| Payroll taxes payable | 2,259 | 14,475 |
| Deferred assessments and audit reimbursements | 280,120 | --- |
| Current portion of long-term debt | 11,494 | 10,624 |
| Accrued pension plan contributions | 9,691 | --- |
| TOTAL CURRENT LIABILITIES........................ | 421,085 | 116,640 |
| LONG-TERM DEBT | | |
| Note payable--Note 3 | 38,556 | 49,180 |
| Less: Current portion | 11,494 | 10,624 |
| TOTAL LONG-TERM DEBT............................. | 27,062 | 38,556 |
| TOTAL LIABILITIES ............................... | 448,147 | 155,196 |
| COMMITMENTS AND CONTINGENCIES--Note 4 | | |
| FUND BALANCE | | |
| Unappropriated | 482,532 | 804,769 |
| Appropriated--Note 6 | 277,444 | 20,672 |
| Restricted--Note 7 | 139,694 | 97,044 |
| TOTAL FUND BALANCE............................... | 899,670 | 922,485 |
| TOTAL LIABILITIES AND FUND BALANCE............... | $1,347,817 | $1,077,681 |

See accompanying notes to financial statements.

Exhibit B

MULTISTATE TAX COMMISSION

STATEMENT OF REVENUES AND EXPENSES
AND STATEMENT OF CHANGES IN FUND BALANCE
For the years ended June 30, 1987 and 1986

| | UNAPPROPRIATED FUNDS | |
|---|---|---|
| | 1987 | 1986 |
| REVENUES: | | |
| Assessments | $1,656,415 | $1,689,415 |
| Interest | 54,510 | 64,298 |
| Other revenue: | | |
| Legal administrative | 25,551 | 25,000 |
| Miscellaneous | 75 | 2,112 |
| TOTAL REVENUES | 1,736,551 | 1,780,825 |
| EXPENSES: | | |
| Accounting | 8,000 | 8,634 |
| Bonds and insurance | 6,488 | 5,281 |
| Conferences | 7,432 | 12,595 |
| Consulting fees | 110,868 | 112,450 |
| Depreciation and amortization | 41,031 | 52,720 |
| Employee benefits | 95,076 | 96,063 |
| Interest expense | 3,506 | 3,922 |
| Legal and legal support | --- | 2,088 |
| Miscellaneous | 6,363 | 12,501 |
| Office supplies | 11,489 | 12,241 |
| Pension plan and retirement provision | 176,856 | 90,922 |
| Postage | 10,059 | 9,779 |
| Printing and duplicating | 6,673 | 17,522 |
| Publications | 16,931 | 12,809 |
| Rent | 109,336 | 98,937 |
| Repairs and maintenance | 15,682 | 10,565 |
| Salaries | 1,078,154 | 1,070,692 |
| Telephone | 24,297 | 27,894 |
| Travel | 75,507 | 73,072 |
| Utilities | --- | 1,195 |
| TOTAL EXPENSES | 1,803,748 | 1,731,883 |
| EXCESS (DEFICIENCY) OF REVENUE OVER EXPENSES BEFORE EXTRAORDINARY ITEM | (67,197) | 48,942 |
| Extraordinary Item - Gain on termination of pension plan--Note 2 | --- | 230,425 |
| EXCESS (DEFICIENCY) OF REVENUE OVER EXPENSES | (67,197) | 279,367 |
| FUND BALANCE--Beginning of Year | 804,769 | 525,402 |
| Transfer to Appropriated Funds--Note 6 | (255,040) | --- |
| FUND BALANCE--End of Year | $ 482,532 | $ 804,769 |

See accompanying notes to financial statements.

Exhibit C

MULTISTATE TAX COMMISSION

STATEMENT OF REVENUES AND EXPENSES
AND STATEMENT OF CHANGES IN FUND BALANCE
For the years ended June 30, 1987 and 1986

| | APPROPRIATED FUNDS--Note 6 | | | |
|---|---|---|---|---|
| | Publications and Seminars | Review Subscriptions | Terminated Pension Plan | Total |
| FUND BALANCE--June 30, 1985 ... | $ 18,001 | $ --- | $ --- | $ 18,001 |
| REVENUES | 6,876 | 10,887 | --- | 17,763 |
| EXPENSES | (7,260) | (7,832) | --- | (15,092) |
| EXCESS (DEFICIENCY) OF REVENUES OVER EXPENSES ............. | (384) | 3,055 | --- | 2,671 |
| FUND BALANCE--June 30, 1986 | 17,617 | 3,055 | --- | 20,672 |
| REVENUES | 31,571 | 10,237 | | 41,808 |
| EXPENSES | (33,621) | (6,455) | --- | (40,076) |
| EXCESS (DEFICIENCY) OF REVENUES OVER EXPENSES ............. | (2,050) | 3,782 | --- | 1,732 |
| TRANSFER FROM UNAPPROPRIATED FUND--Note 6 | --- | --- | 255,040 | 255,040 |
| FUND BALANCE--June 30, 1987 ... | $ 15,567 | $ 6,837 | $ 255,040 | $ 277,444 |

See accompanying notes to financial statements.

MULTISTATE TAX COMMISSION

STATEMENT OF REVENUES AND EXPENSES
AND STATEMENT OF CHANGES IN FUND BALANCE
For the years ended June 30, 1987 and 1986

| | RESTRICTED FUNDS--Note 7 | |
|---|---|---|
| | 1987 | 1986 |
| REVENUES: | | |
| Contributions | $ 82,747 | $ 97,520 |
| EXPENSES: | | |
| Conferences | 600 | --- |
| Employee benefits | 640 | --- |
| Miscellaneous | 814 | --- |
| Office supplies | 870 | --- |
| Pension plan and retirement benefits | 1,251 | --- |
| Postage | 1,259 | --- |
| Printing and duplicating | 595 | --- |
| Rent | 4,686 | --- |
| Salaries | 25,878 | --- |
| Telephone | 1,300 | --- |
| Travel | 2,204 | 476 |
| TOTAL EXPENSES | 40,097 | 476 |
| EXCESS OF REVENUES OVER EXPENSES | 42,650 | 97,044 |
| FUND BALANCE--Beginning of Year | 97,044 | --- |
| FUND BALANCE--End of Year | $ 139,694 | $ 97,044 |

See accompanying notes to financial statements.

Exhibit E

MULTISTATE TAX COMMISSION

STATEMENT OF CHANGES IN FINANCIAL POSITION
For the years ended June 30, 1987 and 1986

| | 1987 | 1986 |
|---|---|---|
| WORKING CAPITAL PROVIDED BY: | | |
| Operations: | | |
| Excess (deficiency) of revenue over expenses before extraordinary item | $ (22,815) | $148,657 |
| Add: Charges not requiring the use of working capital: | | |
| Depreciation and amortization | 41,031 | 52,720 |
| Working Capital provided by operations before extraordinary item | 18,216 | 201,377 |
| Extraordinary Item | --- | 230,425 |
| Working Capital provided by operations | 18,216 | 431,802 |
| Decrease in expense account advances | 1,250 | --- |
| Decrease in prepaid pension costs | --- | 69,098 |
| TOTAL PROVIDED .................................... | 19,466 | 500,900 |
| WORKING CAPITAL APPLIED TO: | | |
| Purchase of property and equipment | 19,995 | 6,512 |
| Increase in expense account advances | --- | 800 |
| Increase in deposits | 385 | --- |
| Payment and reclassification of long-term debt | 11,494 | 10,641 |
| TOTAL APPLIED ..................................... | 31,874 | 17,953 |
| INCREASE (DECREASE) IN WORKING CAPITAL ..................... | $ (12,408) | $482,947 |
| CHANGES IN WORKING CAPITAL COMPONENTS | | |
| Increase (decrease) in current assets: | | |
| Cash | $ 207,219 | $278,488 |
| Accounts receivable--members | 122,893 | (56,645) |
| Accounts receivabe--other | (8) | (83,272) |
| Accrued interest receivable | 1,044 | 8,400 |
| Receivable from termination of pension plan | (299,523) | 299,523 |
| Investments | 253,689 | --- |
| Prepaid insurance | 6,723 | --- |
| | 292,037 | 446,494 |
| Decrease (increase) in current liabilities: | | |
| Accounts payable | (23,803) | 33,472 |
| Accrued vacation pay | (2,177) | 633 |
| Payroll taxes payable | 12,216 | (1,697) |
| Deferred assessments and audit reimbursements | (280,120) | 5,656 |
| Current portion of long-term debt | (870) | (1,611) |
| Accrued pension plan contributions | (9,691) | --- |
| | (304,445) | 36,453 |
| INCREASE (DECREASE) IN WORKING CAPITAL ..................... | $ (12,408) | $482,947 |

See accompanying notes to financial statements.

MULTISTATE TAX COMMISSION

NOTES TO FINANCIAL STATEMENTS
June 30, 1987

## NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Multistate Tax Commission was organized in 1967. It was established under the Multistate Tax Compact, which by its terms, became effective August 4, 1967. The basic objective of the "Compact" and, accordingly, the Commission is to provide solutions and additional facilities for dealing with state taxing problems related to multistate business.

### Method of Accounting

The Commission follows the accrual method of accounting whereby assessment revenue is recognized in the fiscal year of assessment, contributions for specific purposes are recognized as income during the year of receipt, other revenue is recognized as it is earned and expenses are recognized as they are incurred.

### Property and Equipment

All property and equipment is stated at cost and depreciated using straight-line and accelerated methods over the estimated useful lives of the assets which range from 3 to 8 years.

### Restricted Funds

Funds whose use is restricted to a specific use or purpose by outside agencies or persons are included in restricted funds. Restricted funds are deemed to be earned and reported as revenues when the Organization has received them and expenses are recognized as they are incurred.

## NOTE 2 - PENSION PLAN

The Commission had a defined benefit pension plan covering substantially all of its employees. The total pension expense for the year ended June 30, 1986 was $90,922. The Commission's policy is to fund pension costs as accrued. The actuarial value of the plan's assets as of June 30, 1986 was $1,235,696, which exceeded the lump sum benefits payable of $936,173 by $299,523. Because $69,098 had previously been recognized as a prepaid pension cost, the extraordinary gain on the termination of the defined benefit pension plan was $230,425 for the year ended June 30, 1986. The entire amount of the overpayment will be refunded to the Commission. Effective June 30, 1986, the Commission terminated the defined benefit pension plan and adopted a defined contribution plan to be funded at a rate of twelve percent of each vested individual's annual salary. The total pension expense relating to the defined contribution plan for the year ended June 30, 1987 was $176,856.

## NOTE 3 - NOTE PAYABLE

Note payable at June 30, 1987 was as follows:

| | Current | Long-Term | Total |
|---|---|---|---|
| Manufacturer--7.9% installment note, collateralized by related equipment, payable in monthly installments of $1,177.47, including interest, with final payment due July, 1990. | $ 11,494 | $ 27,062 | $ 38,556 |

The minimum scheduled note payments remaining at June 30, 1987 are as follows:

| Fiscal Year Ended | |
|---|---|
| 1988 | $ 14,130 |
| 1989 | 14,130 |
| 1990 | 14,130 |
| 1991 | 1,176 |
| Total note payments | 43,566 |
| Interest included in payments | ( 5,101) |
| TOTAL | $ 38,465 |

## NOTE 4 - COMMITMENTS

The Commission rents its primary office facilities in Boulder, Colorado, and other office facilities in New York and Illinois under lease agreements with terms expiring on various dates through September 30, 1991. These leases provide for the following minimum annual rentals exclusive of utility charges and certain escalation charges:

| Fiscal Year Ended | Minimum Annual Rental |
|---|---|
| June 30, 1988 | $104,499 |
| June 30, 1989 | 88,642 |
| June 30, 1990 | 53,050 |
| June 30, 1991 | 49,724 |
| June 30, 1992 | 12,431 |
| Subsequent years | --- |
| TOTAL | $308,346 |

The leases include certain escalation charges based on various factors including wage index, utility, operating and property tax increases from a base year. Rent expense for the year ended June 30, 1987 and 1986 was $114,022 and $98,937, respectively.

NOTE 5 - INCOME TAXES

In the opinion of legal counsel, the Commission is exempt from Federal income taxes as well as from other Federal taxes as an organization of a group of States or as an instrumentality of those States. Therefore, no provision has been made in the financial statements for Federal income taxes.

NOTE 6 - APPROPRIATED FUND BALANCE

In 1981, the Executive Committee of the Multistate Tax Commission established a revolving fund financed through the net income from publications and seminars to be used to promote additional seminars and publications of additional works.

During the year ended June 30, 1986, the Executive Committee set up the review subscription revolving funds. The net proceeds from the review subscriptions are to be used to cover future printing and postage costs of the publication.

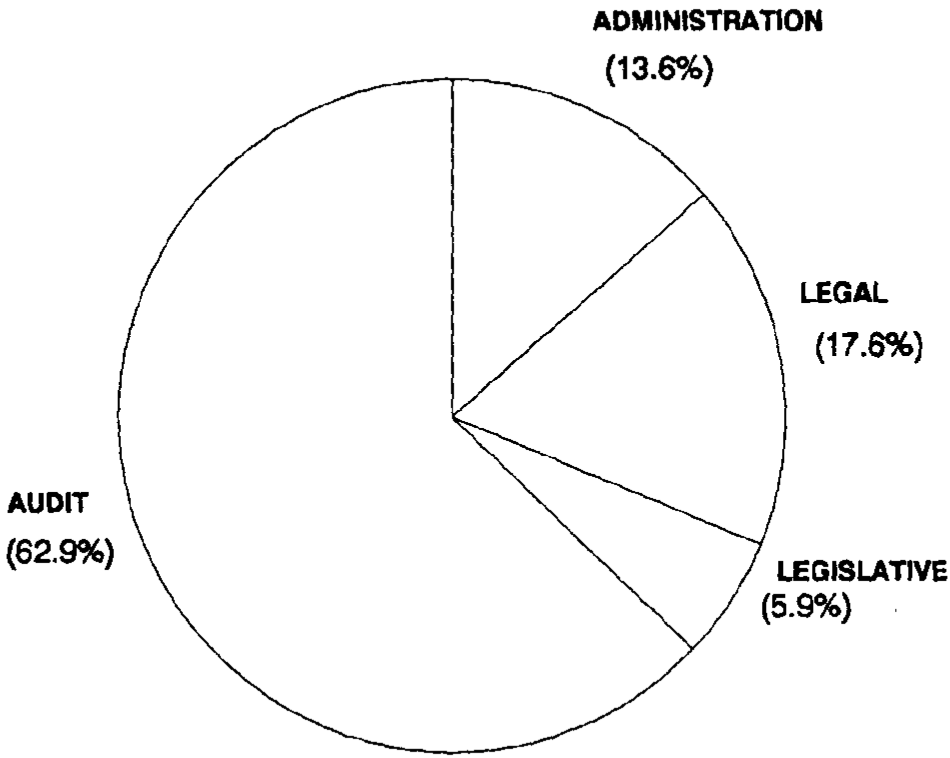
During the year ended June 30, 1987, the Executive Committee determined that the proceeds from the over funding of the pension plan would be set aside to be used to provide funds for moving the administrative office to Washington, D.C. Therefore, $255,040 has been appropriated for this purpose.

NOTE 7 - RESTRICTED FUND BALANCE

During the year ended June 30, 1986 the Executive Committee set up the National Bellas Hess Fund and solicited contributions on its behalf. The contributions received are restricted for this program and are to be used to support education, lobbying and legal expenses related to the National Bellas Hess case.

# MTC EXPENSES

## 1986/87



# Adoption of MTC Regulations

| State | Allocation & Apportionment Formally | Allocation & Apportionment Informally | Airline Formally | Airline Informally | Contractor Formally | Contractor Informally | Railroad Formally | Railroad Informally |
|---|---|---|---|---|---|---|---|---|
| Alabama | No | No | No | No | No | No | No | No |
| Alaska | Yes | | No | No | No | No | No | No |
| Arizona | Yes | | No | No | No | No | No | No |
| Arkansas | Partially | | No | No | No | No | Yes[1] | |
| California | Yes | | No | No | Yes | | Yes[2] | |
| Colorado | Yes | | No | No | Yes[2] | | Yes | |
| Connecticut | No | No | No | No | No | No | No | No |
| Delaware | No | No | No | No | No | No | No | No |
| Dist. of Columbia | No | Partially | No | No | No | No | No | No |
| Florida | No | Yes[3] | No | No | No | No | No | No |
| Georgia | No | No | No | No | No | No | No | No |
| Hawaii | No | No | No | No | No | No | N/A | N/A |
| Idaho | Yes | | Yes | | Yes | | Yes | |
| Illinois | Partially | | No | No | No | No | No | No |
| Indiana | No | Yes | No | No | No | No | No | No |
| Iowa | No | No | No | No | No | No | No | No |
| Kansas | Yes | | No | Yes | No | No | No | No |
| Kentucky | No | No | No | No | No | No | No | No |
| Louisiana | No | No | No | No | No | No | No | No |
| Maine | No | No | No | No | No | No | No | No |
| Maryland[4] | No | No | No | No | No | No | No | No |
| Massachusetts | No | No | No | No | No | No | No | No |
| Michigan | No | Yes | No | No | No | No | No | No |
| Minnesota[5] | Partially | | No | No | No | No | Yes | |
| Mississippi | No | No | No | No | No | No | No | No |
| Missouri | Yes | | No | Yes | Yes | | No | Yes |
| Montana | Yes | | No | Yes | No | Yes | No | Yes |
| Nebraska[6] | Yes | | Yes | | No | No | No | No |
| New Hampshire | No[7] | No | No | No | No | No | No | No |
| New Jersey | No | No | No | No | No | No | No | No |
| New Mexico | Yes | | No | Yes | No | Yes | No | Yes |
| New York | No | No | No | No | No | No | No | No |
| North Carolina | No | No | No | No | No | No | No | No |
| North Dakota | Yes | | Yes | | No | Yes | Yes | |
| Ohio | No | No | No | No | No | No | No | No |
| Oklahoma | No | No | No | No | No | No | No | No |
| Oregon | Yes | | Yes | | Yes | | Yes | |
| Pennsylvania | No | No | No | No | No | No | No | No |
| Rhode Island | No | No | No | No | No | No | No | No |
| South Carolina | No | No | No | No | No | No | No | No |
| Tennessee | No | No | No | No | No | No | No | No |
| Utah | Yes | | No | No | Yes | | No | No |
| Vermont | No | No | No | No | No | No | No | No |
| Virginia | No | No | No | No | No | No | No | No |
| West Virginia | No | No | No | No | No | No | No | No |
| Wisconsin | No | No | No | No | No | No | No | No |

| Railroad | | Trucking | | P.L. 86-272 Guidelines | |
|---|---|---|---|---|---|
| nally | Informally | Formally | Informally | Formally | Informally |
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| Yes[1] | | No | No | Yes | |
| Yes[2] | | No | No | Yes | |
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| No | No | No | No | Yes[8] | No |
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| No | Yes | No | No | Yes | |
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| No | No | No | No | No | No |
| Yes | | No[9] | No | Yes | |
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| Yes | | No | No | Yes | |
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| No | No | No | No | No | No |
| No | No | No | No | No | No |
| No | No | No | No | Yes | |

Notes

1 Substantially same. See Arkansas Reg. 1-84-2004.
2 Substantially same.
3 Florida double weights sales factor.
4 But Maryland's treatment is generally similar to MTC treatment.
5 Minnesota weights sales factor at 70%.
6 Nebraska is moving toward 100% sales factor.
7 By statute, non-unitary dividends are exempt; all else is apportionable.
8 Rev. 304.01(d)
9 In-process; formal adoption expected as of 12/31/87.

# Appendix A
## Multistate Tax Commission
## Construction Contractor Regulation

*Adopted July 10, 1980*

Reg.IV.18.(d). *Special Regulation: Construction Contractors.*

The following special rules are established in respect to the apportionment of income of long-term constructions contractors:

(1) *In General.* When a taxpayer elects to use the percentage of completion method of accounting, or the completed contract method of accounting for long-term contracts (construction contracts covering a period in excess of one year from the date of execution of the contract to the date on which the contract is finally completed and accepted), and has income from sources both within and without this state from a trade or business, the amount of business income derived from such long-term contracts from sources within this state shall be determined pursuant to this regulation. In such cases, the first step is to determine which portion of the taxpayer's income constitutes "business income" and which portion constitutes "nonbusiness income" under Article IV.1 and Reg. IV.1 thereunder. Nonbusiness income is directly allocated to specific states pursuant to the provisions of Article IV.5 to .8, inclusive. Business income is apportioned among the states in which the business is conducted pursuant to the property, payroll, and sales apportionment factors set forth in this regulation. The sum of (1) the items of nonbusiness income directly allocated to this state and (2) the amount of business income attributable to this state constitutes the amount of the taxpayer's entire net income which is subject to tax by this state.

(2) *Business and Nonbusiness Income.* For definitions, rules and examples for determining business and nonbusiness income, see Reg. IV.1.

(3) *Methods of Accounting and Year of Inclusion.* For general rules of accounting, definitions and methods of accounting for long-term construction contracts see [each state adopting this Regulation should insert here reference to its laws and regulations relating in general to accounting methods of reporting income from long-term contracts. This Regulation assumes that the law of the adopting states permits the taxpayer to elect either the percentage of completion or completed contract method. If not, the Regulation will have to be modified to conform to an adopting state's accounting method for long-term construction contracts.]

(4) *Apportionment of Business Income.*

(i) *In General.* Business income is apportioned to this state by a three-factor formula consisting of property, payroll and sales regardless of the method of accounting for long-term contracts elected by the taxpayer. The total of the property, payroll and sales percentages is divided by three to determine the apportionment percentage. The apportionment percentage is then applied to business income to determine the amount apportioned to this state.

(ii) *Percentage of Completion Method.* Under this method of accounting for long-term contracts, the amount to be included each year as business income from each contract is the amount by which the gross contract price which corresponds to the percentage of the entire contract which has been completed during the income year exceeds all expenditures made during the income year in connection with the contract. In so doing, account must be taken of the material and supplies on hand at the beginning and end of the income year for use in each such contract.

**Example**: A taxpayer using the percentage of completion method of accounting for long-term contracts, entered into a long-term contract to build a structure for $9,000,000. The contract allowed three years for completion and, as of the end of the second income year, the taxpayer's books of account, kept on the accrual method, disclosed the following:

| | Receipts | Expenditures |
|---|---|---|
| End of 1st income year | $2,500,000 | $2,400,000 |
| End of 2nd income year | 4,500,000 | 4,100,000 |
| Totals | $7,000,000 | $6,500,000 |

In computing the above expenditures, consideration was given to material and supplies on hand at the beginning and end of each income year. It was estimated that the contract was 30% completed at the end of the first income year and 80% completed at the end of the second income year. The amount to be included as business income for the first income year is $300,000 (30% of $9,000,000 or $2,700,000 less expenditures of $2,400,000 equals $300,000). The amount to be included as business income for the second income year is $400,000 (50% of $9,000,000 or $4,500,000 less expenditures of $4,100,000 equals $400,000).

(iii) Completed Contract Method. Under this method of accounting business income derived from long-term contracts is reported for the income year in which the contract is finally completed and accepted. Therefore, a special computation is required to compute the amount of business income attributable to this state from each completed contract (see subdivision (5) of this regulation). Thus, all receipts and expenditures applicable to such contracts whether complete or incomplete as of the end of the income year are excluded from business income derived from other sources, as for example, short-term contracts, interest, rents, royalties, etc., which is apportioned by the regular three-factor formula of property, payroll and sales.

(iv) *Property Factor.* In general the numerator and denominator of the property factor shall be determined as set forth in Article IV.10 to .12, inclusive, and Reg. IV.10 to .12, inclusive. However, the following special rules are also applicable:

(A) The average value of the taxpayer's cost (including materials and labor of construction in progress, to the extent that such costs exceed progress billings (accrued or received, depending on whether the taxpayer is on the accrual or cash basis for keeping its accounts) shall be included in the denominator of the property factor. The value of any such construction costs attributable to construction projects in this state shall be included in the numerator of the property factor.

**Example 1**: Taxpayer commenced a long-term construction project in this state as of the beginning of a given year. By the end of its second income year, its equity in the costs of production to be reflected in the numerator and denominator of its property factor for such year is computed as follows:

| | 1st Year | | 2nd Year | |
|---|---|---|---|---|
| | Beginning | Ending | Beginning | Ending |
| Construction Costs | 0 | $1,000,000 | | |
| Progress billings | | 600,000 | | |
| Balance 12/31 - (1/1) | | $400,000 | $400,000 | |
| Construction Costs - Total from beginning of project | | | | $5,000,000 |
| Progress billings - Total from beginning of project | | | | 4,000,000 |
| Balance 12/31 | | | | 1,000,000 |
| Balance beginning of Year | | | | 400,000 |
| Total | | | | $1,400,000 |
| Average (1/2) - Value used in property factor | | | | $700,000 |

Note: It may be necessary to use monthly averages if yearly averages do not properly reflect the average value of the taxpayer's equity; see Article IV.12 and Reg. IV.12.

**Example 2**: Same facts as in example 1, except that progress billings exceeded construction costs. No value for the taxpayer's equity in the construction project is shown in the property factor.

(B) Rent paid for the use of equipment directly attributable to a particular construction project is included in the property factor at eight times the net annual rental rate even though such rental expense maybe capitalized into the cost of construction.

(C) The property factor is computed in the same manner for all long-term contract methods of accounting and is computed for each income year even though under the completed contract method of accounting, business income is computed separately (see paragraph (5) below).

(v) *Payroll Factor*. In general the numerator and denominator of the payroll factor shall be determined as set forth in Article IV.13 and .14 and Reg. IV.13 and .14. However, the following special rules are also applicable:

(A) Compensation paid employees which is attributable to a particular construction project is included in the payroll factor even though capitalized into the cost of construction.

(B) Compensation paid employees who in the aggregate perform most of their services in a state to which their employer does not report them for unemployment tax purposes, shall nevertheless be attributed to the state in which the services are performed.

**Example**: A taxpayer engaged in a long-term contract in state X sends several key employees to that state to supervise the project. The taxpayer, for unemployment tax purposes, reports these employees to state Y where the main office is maintained and where the employees reside. For payroll factor purposes and in accordance with Article IV.14 and Reg. IV.14 thereunder, the compensation is assigned to the numerator of state X.

(C) The payroll factor is computed in the same manner for all long-term contract methods of accounting and is computed for each income year even though, under the completed contract method of accounting, business income is computed separately (see paragraph (5) below).

(vi) *Sales Factor*. In general, the numerator and denominator of the sales factor shall be determined as set forth in Article IV.15-.17, inclusive, and Reg. IV.15-.17, inclusive. However, the following special rules are also applicable:

(A) Gross receipts derived from the performance of a contract are attributable to this state if the construction project is located in this state. If the construction project is located partly within and partly without this state, the gross receipts attributable to this state are based upon the ratio which construction costs for the project in this state incurred during the income year bear to the total of construction costs for the entire project during the income year, or upon any other method, such as engineering cost estimates, which will provide a reasonable apportionment.

**Example 1**: A construction project was undertaken in this state by a calendar year taxpayer which had elected one of the long-term contract methods of accounting. The following gross receipts (progress billings) were derived from the contract during the three income years that the contract was in progress.

| | 1st Year | 2nd Year | 3rd Year |
|---|---|---|---|
| Gross Receipts | $1,000,000 | $4,000,000 | $3,000,000 |

The gross receipts to be reflected in both the numerator and denominator of the sales factor for each of the three years are the amounts shown.

**Example 2**: A taxpayer contracts to build a dam on a river at a point which lies half within this state and half within state X. During the taxpayer's first income year, construction costs in this state were $2,000,000. Total construction costs for the project during the income year were $3,000,000. Gross receipts (progress billings) for the year were $2,400,000. Accordingly, gross receipts of $1,600,000 ($2,000,000/$3,000,000 x $2,400,000) are included in the numerator of the sales factor.

(B) If the percentage of completion method is used, the sales factor includes only that portion of the gross contract price which corresponds to the percentage of the entire contract which was completed during the income year.

**Example 3:** A taxpayer which had elected the percentage of completion method of accounting entered into a long-term construction contract. At the end of its current income year (the second since starting the project), it estimated that the project was 30% completed. The bid price for the project was $9,000,000 and it had received $2,500,000 from progress billings as of the end of its current income year. The amount of gross receipts to be included in the sales factor for the current income year is $2,700,000 (30% of $9,000,000), regardless of whether the taxpayer uses the accrual method or the case method of accounting for receipts and disbursements.

(C) If the completed contract method of accounting is used, the sales factor includes the portion of the gross receipts (progress billings) received or accrued, whichever is applicable, during the income year attributable to each contract.

**Example 4:** A taxpayer which had elected the completed contract method of accounting entered into a long-term construction contract. By the end of its current income year (the second since starting the project), it had billed and had accrued on its books a total of $5,000,000 of which $2,000,000 had accrued in the first year in which the contract was undertaken and $3,000,000 had accrued in the current (second) year. The amount of gross receipts to be included in the sales factor for the current income year is $3,000,000.

**Example 5**: Same facts as in Example 4 except that the taxpayer keeps its books on the cash basis and, as of the end of its current income year, had received only $2,500,000 of the $3,000,000 billed during the current year. The amount of gross receipts to be included in the sales factor for the current income year is $2,500,000.

(D) The sales factor, except as noted above in subparagraphs (B) and (C), is computed in the same manner, regardless of which long-term method of accounting the taxpayer has elected, and is computed for each income year even though, under the completed contract method of accounting, business income is computed separately.

(vii) *Apportionment Percentage.* The total of the property, payroll and sales percentages is divided by three to determine the apportionment percentage. The apportionment percentage is then applied to business income to establish the amount apportioned to this state.

(5) *Completed Contract Method - Special Computation.* The completed contract method of accounting requires that the reporting of income (or loss) be deferred until the year in which the construction project is completed or accepted. Accordingly, a separate computation is made for each such contract completed during the income year, regardless of whether the project is located within or without this state, in order to determine the amount of income which is attributable to sources within this state. The amount of income from each contract completed during the income year apportioned to this state plus other business income apportioned to this

state by the regular three-factor formula such as interest income, rents, royalties, income from short-term contracts, etc. plus all nonbusiness income allocated to this state is the measure of tax for the income year.

The amount of income (or loss) from each contract which is derived from sources within this state using the completed contract method of accounting is computed as follows:

(i) In the income year in which the contract is completed, the income (or loss) therefrom is determined.

(ii) The income (or loss) determined at (i) above is apportioned to this state by the following method:

(A) A fraction is determined for each year during which the contract was in progress. The numerator is the amount of construction costs paid or accrued in each year during which the contract was in progress and the denominator is the total of all such construction costs for the project.

(B) Each percentage determined in (A) is multiplied by the apportionment formula percentage for that particular year as determined in subparagraph (4)(vii) of this regulation above.

(C) The percentages determined at (B) for each year during which the contract was in progress are totaled. The amount of total income (or loss) from the contract determined at subparagraph (5)(i) of this regulation is multiplied by the total percentage. The resulting income (or loss) is the amount of business income from such contract derived from sources within this state.

**Example 1:** A taxpayer using the completed contract method of accounting for long-term contracts is engaged in three long-term contracts; Contract L in this state, Contract M in state X and Contract N in state Y. In addition, it has other business income (less expenses) during the income year 1972 from interest, rents and short-term contracts amounting to $500,000, and nonbusiness income allocable to this state of $8,000. During 1972, it completed Contract M in state X at a profit of $900,000. Contracts L and N in this state and state Y, respectively, were not completed during the income year. The apportionment percentages of the taxpayer as determined in subparagraph (4)(vii) of this regulation and the percentages of contract costs as determined in subparagraph (5)(ii) above for each year during which Contract M in state X was in progress are as follows:

| | 1970 | 1971 | 1972 |
|---|---|---|---|
| Apportionment % | 30% | 20% | 40% |
| % of Construction Costs of Contract M each year to total construction costs - (100%) | 20% | 50% | 30% |

The corporation's net income subject to tax in this state for 1972 is computed as follows:

| | |
|---|---|
| Business Income | $500,000 |
| Apportion 40% to this state | $200,000 |
| Add: Income from Contract M* | $252,000 |
| Total business income derived from sources within this state | 452,000 |
| Add: Nonbusiness income allocated to this state | 8,000 |
| Net income subject to tax | $460,000 |

*Income from Contract M apportioned to this state:

| | 1970 | 1971 | 1972 | Total |
|---|---|---|---|---|
| Apportionment % | 30% | 20% | 40% | |
| % of Construction Costs | 20% | 50% | 30% | 100% |
| Product | 6% | 10% | 12% | 28% |

28% of $900,000 = $252,000.

**Example 2:** Same facts as in example 1 except that Contract L was started in 1972 in this state, the first year in which the taxpayer was subject to tax in this state. Contract L in this state and Contract N in state Y are incomplete in 1972.

The corporation's net income subject to tax in this state for 1972 is computed as follows:

| | |
|---|---|
| Business income | $500,000 |
| Apportion 40% to this state | $200,000 |
| Add: Income from Contract M* | 108,000 |
| Total business income derived from sources within this state | $308,000 |
| Add: Nonbusiness income allocated to this state | 8,000 |
| Net income subject to tax | $316,000 |

*Income from Contract M apportioned to this state:

| | 1970 | 1971 | 1972 | Total |
|---|---|---|---|---|
| Apportionment % | 0 | 0 | 40% | |
| Costs | 20% | 50% | 30% | 100% |
| Product | 0 | 0 | 12% | 12% |

12% of $900,000 = $108,000.

**Note:** Only 12% is used to determine the income derived from sources within this state since the corporation was not subject to tax in this state prior to 1972.

**Example 3:** Same facts as in example 1 except that the figures relate to Contract L in this state and 1972 is the first year the corporation was taxable in another state (see Article IV.2 and .3 and Reg. IV.2(b)(1) and .3. Contracts M and N in states X and Y were started in 1972 and are incomplete.

The corporation's net income subject to tax in this state for 1972 is computed as follows:

| | |
|---|---|
| Business income | $500,000 |
| | |
| Apportion 40% to this state | $200,000 |
| Add: Income from Contract L* | 738,000 |
| Total business income derived from sources within this state | $938,000 |
| Add: Nonbusiness income allocated to this state | 8,000 |
| Net income subject to tax | $946,000 |

*Income from Contract L apportioned to this state:

| | 1970 | 1971 | 1972 | Total |
|---|---|---|---|---|
| Apportionment % | 100% | 100% | 40% | |
| % of Construction Costs | 20% | 50% | 12% | 82% |

82% of $900,000 = $738,000.

(6) *Computation for Year of Withdrawal, Dissolution or Cessation of Business - Completed Contract Method.* Use of the completed contract method of accounting for long-term contracts requires that income derived from sources within this state from incomplete contracts in progress outside this state on the date of withdrawal, dissolution or cessation of business in this state be included in the measure of tax for the taxable year during which the corporation withdraws, dissolves or ceases doing business in this state.

The amount of income (or loss) from each such contract to be apportioned to this state by the apportionment method set forth in subparagraph (5)(ii) of this regulation shall be determined as if the percentage of completion method of accounting were used for all such contracts on the date of withdrawal, dissolution or cessation of business. The amount of business income (or loss) for each such contract shall be the amount by which the gross contract price from each such contract which corresponds to the percentage of the entire contract which has been completed from the commencement thereof to the date of withdrawal, dissolution or cessation of business exceeds all expenditures made during such period in connection with each such contract. In so doing, one must take into account the material and supplies on hand at the beginning and end of the income year for use in each such contract.

**Example:** A construction contractor qualified to do business in this state had elected the completed contract method of accounting for long-term contracts. It was engaged in two long-term contracts. Contract L in this state was started in 1971 and completed at a profit of $900,000 on 12/16/73. The taxpayer withdrew on 12/31/73. Contract M in state X was started in 1972 and was incomplete on 12/31/73. The apportionment percentages of the taxpayer, as determined at subdivision (4) of this regulation, and percentages of construction costs, as determined in subparagraph (5)(ii) of this regulation, for each year during which Contract M in state X was in progress are as follows:

| | 1971 | 1972 | 1973 | Total |
|---|---|---|---|---|
| Apportionment % | 30% | 20% | 40% | |
| % of Construction Costs: | | | | |
| Contract L, this state | 20% | 50% | 30% | 100% |
| Contract M, state X | 0 | 10% | 25% | 35% |

The corporation had other business income (net of expenses) of $500,000 during 1972 and $300,000 during 1973. The gross contract price of Contract M (state X) was $1,000,000, and it was estimated to be 35% completed on 12/31/73. Total expenditures to date for Contract M (state X) were $300,000 for the period ended 12/31/73.

The measure of tax for the taxable year ended 12/31/73 is computed as follows:

| | Taxable Year 1973 | |
|---|---|---|
| | Income Year 1972 | Income Year 1973 |
| Business income | $500,000 | $300,000 |
| Apportionment % to this state | 20% | 40% |
| Amount apportioned to this state | $100,000 | $120,000 |
| Add: Income from contracts: | | |
| L* (this state) | | $252,000 |
| M** (state X) | | 6,000 |
| Total business income derived from sources within this state | $100,000 | $378,000 |

*Income from Contract L apportioned to this state:

| | 1971 | 1972 | 1973 | Total |
|---|---|---|---|---|
| Apportionment % | 30% | 20% | 40% | |
| % of Construction Costs | 20% | 50% | 30% | 100% |
| Product | 6% | 10% | 12% | 28% |

28% of $900,000 = $252,000.

**Income from Contract M apportioned to this state:

| | 1971 | 1972 | 1973 | Total |
|---|---|---|---|---|
| Apportionment % | 0 | 20% | 40% | |
| % of Construction Costs | 0 | 10% | 25% | 35% |
| Product | 0 | 2% | 10% | 12% |

12% of \$50,000† = \$6,000.

†Computation of apportionable income from Contract M based on percentage of completion method:

| | |
|---|---|
| Total Contract Price | \$1,000,000 |
| Estimated to be 35% completed | \$350,000 |
| Less: total expenditures to date | 300,000 |
| Apportionable income | \$50,000 |

# Appendix B
## Multistate Tax Commission
## Railroad Regulation

*Adopted July 16, 1981*

Reg. IV.18.(f). Special Rules: Railroads.

The following special rules are established in respect to railroads:

(1) *In general*. Where a railroad 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 this regulation. In such cases, the first step is to determine what portion of the railroad's income constitutes "business" income and which portion constitutes "nonbusiness" income under Article IV.1 and Regulation IV.1 thereunder. Nonbusiness income is directly allocable to specific states pursuant to the provisions of Article IV.5 to .8, inclusive. Business income is apportioned among the states in which the business is conducted pursuant to the property, payroll and sales apportionment factors set forth in this regulation. The sum of (1) the items of nonbusiness income directly allocated to this state and (2) the amount of business income attributable to this state constitutes the amount of the taxpayer's entire net income which is subject to tax by this state.

(2) *Business and Nonbusiness Income*. For definitions, rules and examples for determining business and nonbusiness income, see Reg. IV.1.

(3) *Apportionment of Business Income*.

(i) *In General*. The property factor shall be determined in accordance with Reg. IV.10.-.12., inclusive, the payroll factor in accordance with Reg. IV.13., and the sales factor in accordance with Reg. IV.14.-.17, inclusive, except as modified in this regulation.

(ii) *The Property Factor*.

A. *Property Valuation*. Owned property shall be valued at its original cost and property rented from others shall be valued at eight (8) times the net annual rental rate in accordance with Article IV.11. and Reg. IV.11. Railroad cars owned and operated by other railroads and temporarily used by the taxpayer in its business and for which a per diem or mileage charge is made are not included in the property factor as rented property. Railroad cars owned and operated by the taxpayer and temporarily used by other railroads in their business and for which a per diem charge is made by the taxpayer are included in the property factor of the taxpayer.

B. *General Definitions*. The following definitions are applicable to the numerator and denominator of the property factor:

1. "Original cost" is deemed to be the basis of the property for federal income tax purposes (prior to any federal income tax adjustments except for subsequent capital additions, improvements thereto or partial dispositions); or, if the property has no such basis, the valuation of such property for Interstate Commerce Commission purposes. If the original cost of property is unascertainable under the foregoing valuation standards, the property is included

in the property factor at its fair market value as of the date of acquisition by the taxpayer (Reg. IV.11.(a)).

2. "Rent" does not include the per diem and mileage charges paid by the taxpayer for the temporary use of railroad cars owned or operated by another railroad.

3. The "value" of owned real and tangible personal property shall mean its original cost. (See Article IV.11 and Reg. IV.11(a).)

4. "Average value" of property means the amount determined by averaging the values at the beginning and ending of the income tax year, but the [insert here the appropriate title of the administrative agency] may require the averaging of monthly values during the income year or such averaging as necessary to effect properly the average value of the railroad's property. (See Article IV.12. and Reg. IV.12.)

5. The "value" of rented real and tangible personal property means the product of eight (8) times the net annual rental rate. (See Article IV.11. and Reg. IV.11(b).)

6. "Net annual rental rate" means the annual rental rate paid by the taxpayer less any annual rental rate received by the taxpayer from subrentals.

7. "Property used during the income year" includes property which is available for use in the taxpayer's trade or business during the income year.

8. A "locomotive-mile" is the movement of a locomotive (a self-propelled unit of equipment designed solely for moving other equipment) a distance of one mile under its own power.

9. A "car-mile" is a movement of a unit of car equipment a distance of one mile.

C. *The Denominator and Numerator of the Property Factor.* The denominator of the property factor shall be the average value of all of the taxpayer's real and tangible personal property owned or rented and used during the income year. The numerator of the property factor shall be the average value of the taxpayer's real and tangible personal property owned or rented and used in this state during the income year.

In determining the numerator of the property factor, all property except mobile or movable property such as passenger cars, freight cars, locomotives and freight containers which are located within and without this state during the income year shall be included in the numerator of the property factor in accordance with Article IV.10.-.12., inclusive, and Regulation IV.10.-.12, inclusive.

Mobile or movable property such as passenger cars, freight cars, locomotives and freight containers which are located within and without this state during the income year shall be included in the numerator of the property factor in the ratio which "locomotive-miles" and "car-miles" in the state bear to the total everywhere.

(iii) *The Payroll Factor.* The denominator of the payroll factor is the total compensation paid everywhere by the taxpayer during the income year for the production of business income. (See Article IV.13.-14. and Reg. IV.13.-.14.) The numerator of the payroll factor is the total amount paid in this state during the income year by the taxpayer for compensation. With respect to all personnel except enginemen and trainmen performing services on interstate trains, compensation paid to such employees shall be included in the numerator as provided in Article IV.13.-.14 and Reg. IV.13.-.14.

With respect to enginemen and trainmen performing services on interstate trains, compensation paid to such employees shall be included in the numerator of the payroll factor in the ratio which their services performed in this state bear to their services performed everywhere. Compensation for services performed in this state should be deemed to be the compensation reported or required to be reported by such employees for determination of their income tax liability to this state.

(iv) *The Sales (Revenue) Factor.*

A. *In General.* All revenue derived from transactions and activities in the regular course of the trade or business of the taxpayer which produces business income, except per diem and mileage charges which are collected by the taxpayer, is included in the denominator of the revenue factor. (See Article IV.1. and Reg. IV.1.)

The numerator of the revenue factor is the total revenue of the taxpayer in this state during the income year. The total revenue of the taxpayer in this state during the income year, other than revenue from hauling freight, passengers, mail and express, shall be attributable to this state in accordance with Article IV.15.-.17. and Regulation IV.15.-.17.

B. *Numerator of Sales (Revenue) Factor From Freight, Mail and Express.* The total revenue of the taxpayer in this state during the income year for the numerator of the revenue factor from hauling freight, mail and express shall be attributable to this state as follows:

1. All receipts from shipments which both originate and terminate within this state; and

2. That portion of the receipts from each movement or shipment passing through, into, or out of this state is determined by the ratio which the miles traveled by such movement or shipment in this state bear to the total miles traveled by such movement or shipment from point of origin to destination.

C. *Numerator of Sales (Revenue) Factor from Passengers.* The numerator of the sales (revenue) factor shall include:

1. All receipts from the transportation of passengers (including mail and express handled in passenger service) which both originate and terminate within this state; and

2. That portion of the receipts from the transportation of interstate passengers (including mail and express handled in passenger service) determined by the ratio which revenue passenger miles in this state bear to the total everywhere.

# Appendix C
## Multistate Tax Commission
## Airline Regulation

*Adopted July 14, 1983*

Reg. IV.18.(e). *Special Rules: Airlines.*

The following special rules are established with respect to airlines:

(1) *In General.* Where an airline has income from sources both within and without this state, the amount of business income from sources within this state, the amount of business income from sources within this state shall be determined pursuant to Article IV. of the Multistate Tax Compact except as modified by this regulation.

(2) *Apportionment of Business Income.*

(i) *General Definitions.*

The following definitions are applicable to the terms used in the apportionment factor descriptions.

A. "Value" of owned real and tangible personal property shall mean its original cost. (See Article IV.11. and Regulation IV.11(a).)

B. "Cost of aircraft by type" means the average original cost or value of aircraft by type which are ready for flight.

C. "Original cost" means the initial federal tax basis of the property plus the value of capital improvements to such property, except that, for this purpose, it shall be assumed that Safe Harbor Leases are not true leases and do not affect the original initial federal tax basis of the property. (See Regulation IV.11(a).)

D. "Average value" of the property means the amount determined by averaging the values at the beginning and ending of the income year, but the [insert here the appropriate title of the administrative agency] may require the averaging of monthly values during the income year if such averaging is necessary to reflect properly the average value of the airline's property. (See Article IV.12. and Regulation IV.12.)

E. The "value" of rented real and tangible personal property means the product of eight (8) times the net annual rental rate. (See Article IV.11. and Regulation IV.11(b).)

F. "Net annual rental rate" means the annual rental rate paid by the taxpayer.

G. "Property used during the income year" includes property which is available for use in the taxpayer's trade or business during the income year.

H. "Aircraft ready for flight" means aircraft owned or acquired through rental or lease (but not interchange) which are in the possession of the taxpayer and are available for service on the taxpayer routes.

I. "Revenue service" means the use of aircraft ready for flight for the production of revenue.

J. "Transportation revenue" means revenue earned by transporting passengers, freight and mail as well as revenue earned from liquor sales, pet crate rentals, etc.

K. "Departures" means, for purposes of these regulations, all takeoffs, whether they be regularly scheduled or charter flights, that occur during revenue service.

(ii) *Property Factor*

A. *Property valuation*. Owned aircraft shall be valued at its original cost and rented aircraft shall be valued at eight (8) times the net annual rental rate in accordance with Article IV.11. and Regulation IV.11. The use of the taxpayer's owned or rented aircraft in an interchange program with another air carrier will not constitute a rental of such aircraft by the airlines to the other participating airline. Such aircraft shall be accounted for in the property factor of the owner. Parts and other expendables, including parts for use in contract overhaul work, will be valued at cost.

B. *The denominator and numerator of the property factor*. The denominator of the property factor shall be the average value of all of the taxpayer's real and tangible personal property owned or rented and used during the income year. The numerator of the property factor shall be the average value of the taxpayer's real and tangible personal property owned or rented and used in this state during the income year.

In determining the numerator of the property factor, all property except aircraft ready for flight shall be included in the numerator of the property factor in accordance with Article IV.10.-12, inclusive. Aircraft ready for flight shall be included in the numerator of the property factor in the ratio calculated as follows:

Departures of aircraft from locations in this state weighted as to the cost and value of aircraft by type compared to total departures similarly weighted.

(iii) *The Payroll Factor*

The denominator of the payroll factor is the total compensation paid everywhere by the taxpayer during the income year. (See Article IV.13.-.14.) The numerator of the payroll factor is the total amount paid in this state during the income year by the taxpayer for compensation. With respect to non-flight personnel, compensation paid to such employees shall be included in the numerator as provided in Article IV.13-.14. With respect to flight personnel (the air crew aboard an aircraft assisting in the operations of the aircraft or the welfare of passengers while in the air), compensation paid to such employees shall be included in the ratio of departures of aircraft from locations in this state, weighted as to the cost and value of aircraft by type compared to total departures similarly weighted, multiplied by the total flight personnel compensation.

(iv) *Sales (Transportation Revenue) Factor.*

The transportation revenue derived from transactions and activities in the regular course of the trade or business of the taxpayer and miscellaneous sales of merchandise, etc., are included in the denominator of the revenue factor. (See Article IV.1. and Regulation IV.1.) Passive income items such as interest, rental income, dividends, etc., will not be included in the denominator nor will the proceeds or net gains or losses from the sale of aircraft be included. The numerator of the revenue factor is the total revenue of the taxpayer in this state during the income year. The total revenue of the taxpayer in this state during the income year is the result of the following calculation:

The ratio of departures of aircraft in this state weighted as to the cost and value of aircraft by type, as compared to total departures similarly weighted multiplied by the total transportation revenue. The product of this calculation is to be added to any non-flight revenues directly attributable to this state.

(3) *Records*. The taxpayer must maintain the records necessary to arrive at departures by type of aircraft as used in these regulations. Such records are to be subject to review by the respective state taxing authorities or their agents.

## EXAMPLES OF THE MANNER IN WHICH THE MULTISTATE TAX COMMISSION AIRLINE REGULATION WOULD APPLY TO SPECIFIC FACT SITUATIONS

**Example 1:** Assume the following facts for an airline for a tax year:

1. It has ten 747s ready for flight and in revenue service at an average cost per unit of $40,000,000 for none of the aircraft. It rents the tenth 747 from another airline for $9,000,000 per year. At eight times rents, the latter is valued at $72,000,000 for apportionment purposes. The total 747 valuation is, therefore, $432,000,000 for property factor denominator purposes.
2. It has twenty 727s ready for flight in revenue service at an average cost per unit of $20,000,000. The total 727 valuation is, therefore, $400,000,000 for property factor denominator purposes.
3. It has nonflight tangible property (n.t.p.) valued at an original cost of $200,000,000.
4. It has the following annual payroll:

| | |
|---|---|
| Flight personnel | $ 60,000,000 |
| Nonflight personnel (n.p.) | 40,000,000 |
| Total | $100,000,000 |

5. From its operations, it has total receipts of $50,000,000, business net income of $1,000,000, and no nonbusiness income.
6. It has the following within state X:

a. 10% of its 747 flight departures (.10 x $432,000,000) $43,200,000
b. 20% of its 727 flight departures (.20 x $400,000,000) $80,000,000
c. 5% of its n.t.p. (.05 x $200,000,000) $10,000,000
d. 15% of its n.p. payroll (.15 x $40,000,000) $6,000,000

7. State X has a corporate tax rate of 10%.

The airline's tax liability to state X would be determined as follows:

Property Factor:

$$\frac{43{,}200{,}000\ (747s) + 80{,}000{,}000\ (727s) + 10{,}000{,}000\ (n.t.p.)}{432{,}000{,}000 + 400{,}000{,}000 + 200{,}000{,}000} = \frac{133{,}200{,}000}{1{,}032{,}000{,}000} = .1291$$

**Sales Factor:**

$$\frac{43{,}200{,}000\ (747s) + 80{,}000{,}000\ (727s)}{432{,}000{,}000 + 400{,}000{,}000} = \frac{123{,}200{,}000}{832{,}000{,}000} = .1481$$

**Payroll Factor:**

$$\frac{6{,}000{,}000\ (n.p.) + 8{,}880{,}000\ (.148 \times 60{,}000{,}000)(flight)}{100{,}000{,}000} = \frac{14{,}880{,}000}{100{,}000{,}000} = .1488$$

Average ratio: (.1291 + .1481 + .1488)/3 = .4260/3 = .1420

Taxable Income in State X: .1420 x $1,000,000 = $142,000

Tax Liability to State X: .10 x $142,000 = $14,200

Example 2: Same facts except that paragraphs 6 and 7 are changed to read:

6. It has the following within state Y:

| | |
|---|---|
| a. 6% of its 747 flight departures (.06 x $432,000,000) | $25,920,000 |
| b. 31% of its 727 flight departures (.31 x $400,000,000) | $124,000,000 |
| c. 3% of its n.t.p. (.03 x $200,000,000) | $6,000,000 |
| d. 7% of its n.p. payroll (.07 x $40,000,000) | $2,800,000 |

7. State X has a corporate tax rate of 6.5%.

The airline's tax liability to state Y would be determined as follows:

**Property Factor:**

$$\frac{25{,}920{,}000\ (747s)\ +124{,}000{,}000\ (727s)\ +\ 6{,}000{,}000\ (n.t.p.)}{432{,}000{,}000\ +400{,}000{,}000\ +\ 200{,}000{,}000} = \frac{155{,}920{,}000}{1{,}032{,}000{,}000} = .1511$$

**Sales Factor:**

$$\frac{25{,}920{,}000\ (747s)\ +124{,}000{,}000\ (727s)}{432{,}000{,}000\ +400{,}000{,}000} = \frac{149{,}920{,}000}{832{,}000{,}000} = .1802$$

**Payroll Factor:**

$$\frac{2{,}800{,}000\ (n.p.) +\ 10{,}812{,}000\ (.1802 \times 60{,}000{,}000)(flight)}{40{,}000{,}000\ +\ 60{,}000{,}000} + \frac{13{,}612{,}000}{100{,}000{,}000} = .1361$$

Average ratio: (.1511 + .1802 + .1361)/3 = .4674/3 = .1558

Taxable Income in State Y: .1558 x $1,000,000 = $155,800

Tax Liability to State Y: .65 x $155,800 = $10,127

# Appendix D
## Multistate Tax Commission
## Recordkeeping Regulation for Sales and Use Tax Purposes
### *Adopted July 11, 1986*

Reg. VII.1. *Recordkeeping a Sales and Use Tax Transaction*

(1) *In General.* Every retailer [**seller**] [**vendor**] [**person**] doing business in this state or storing, using, or otherwise consuming in this state tangible personal property purchased from a retailer [**and every lessor and lessee of tangible personal property for use in this state**] shall keep complete and adequate records as may be necessary for the Executive Director [**Department**] [**Commissioner**] [**Commission**] [**Board**] to determine the amount of sales and use tax for the payment and collection of which that retailer [**seller**] [**vendor**] [**person**] [**and lessor and lessee**] is liable under [**cite relevant sales and use tax section**]. Unless the Executive Director [**Department**] [**Commissioner**] [**Commission**] [**Board**] authorizes an alternative method of recordkeeping in writing, these records shall show:

a. Gross receipts from sales, or rental payments from leases, of tangible personal property (including any services that are a part of the sale or lease) made in this state, irrespective of whether the retailer [**seller**] [**vendor**] [**person or lessor and lessee**] regards the receipts to be taxable or nontaxable.

b. All deductions allowed by law and claimed in filing the return.

c. Total purchase price of all tangible personal property purchased for sale or consumption [**or lease**] in this state.

These records must include the normal books of account ordinarily maintained by the average prudent businessman engaged in such business, together with all bills, receipts, invoices, cash register tapes, or other documents of original entry supporting the entries in the books of account together with all schedules or working papers used in connection with the preparation of tax returns.

(2) *Microfilm and Microfiche Records.* Records, including general books of account, such as cash books, journals, voucher registers, ledgers and like documents may be microfilmed or microfiched, as long as such microfilmed and microfiched records are authentic, accessible, and readable and the following requirements are fully satisfied:

a. Appropriate facilities are to be provided for preservation of the films or fiche for the periods required and open to examination and the taxpayers must agree to provide transcriptions of any information on microfilm or microfiche which may be required for verification of tax liability.

b. All microfilmed and microfiched data must be indexed, cross-referenced and labeled to show beginning and ending numbers and to show beginning and ending alphabetical listing of documents included, and must be systematically filed to permit ready access.

c. Taxpayer must make available upon request of the Executive Director [**Department**] [**Commissioner**] [**Commission**] [**Board**] a reader/printer in good working order at the examination site for reading, locating and reproducing any record concerning sales and/or use tax liability maintained on microfilm or microfiche.

d. Taxpayer must set forth in writing the procedures governing the establishment of its microfilm or microfiche system and the individuals who are responsible for maintaining and operating the system with appropriate authorization from the Board of Directors, general partner(s), or owner, whichever is applicable.

e. The microfilm or microfiche system must be complete and must be used consistently in the regularly conducted activity of the business.

f. Taxpayer must establish procedures with appropriate documentation so that the original document can be followed through the microfilm or microfiche system.

g. Taxpayer must establish internal procedures for microfilm or microfiche inspection and quality assurance.

h. Taxpayers are responsible for the effective identification, processing, storage, and preservation of microfilm or microfiche, making it readily available for as long as the contents may become material in the administration of any state revenue law.

i. Taxpayer must keep a record identifying by whom the microfilm or microfiche was produced.

j. When displayed on a microfilm or microfiche reader (viewer) or reproduced on paper, the material must exhibit a high degree of legibility and readability. For this purpose, legibility is defined as the quality of a letter or numeral that enables the observer to identify it positively and quickly to the exclusion of all other letters or numerals. Readability is defined as the quality of a group of letters or numerals being recognizable as words or complete numbers.

k. All production of microfilm or microfiche and processing duplication, quality control, storage, identification, and inspection thereof must meet industry standards as set forth by the American National Standards Institute, National Micrographics Association, or National Bureau of Standards.

(3) *Records Prepared By Automated Data Processing Systems (ADP)*. An ADP tax accounting system may be used to provide the records required for the verification of tax liability. Although ADP systems will vary from one taxpayer to another, all such systems must include a method of producing legible and readable records which will provide the necessary information for verifying such tax liability. The following requirements apply to any taxpayer who maintains any such records on an ADP system:

a. **Recorded or Reconstructible Data.** ADP records shall provide an opportunity to trace any transaction back to the original source or forward to a final total. If detailed printouts are not made of transactions at the time when they are processed, the systems must have the ability to reconstruct these transactions.

b. **General and Subsidiary Books of Account**. A general ledger, with source references, shall be written out to coincide with financial reports for tax reporting periods. In cases where subsidiary ledgers are used to support the general ledger accounts, the subsidiary ledgers shall also be written out periodically.

c. **Supporting Documents and Audit Trail**. The audit trail shall be designed so that the details underlying the summary accounting data may be identified and made available to the Executive Director [**Department**] [**Commissioner**] [**Commission**] [**Board**] upon request. The system shall be so designed that supporting documents, such as sales invoices, purchase invoices, credit memoranda, and like documents are readily available.

d. **Program Documentation**. A description of the ADP portion of the accounting system shall be made available. The statements and illustrations as to the scope of operations shall be sufficiently detailed to indicate: (A) the application being performed; (B) the procedures employed in each application (which, for example, might be supported by flow charts, block diagrams or other satisfactory descriptions of the input or output procedures); and (C) the controls used to insure accurate and reliable processing. Important changes, together with their effective dates, shall be noted in order to preserve an accurate chronological record.

e. **Data Storage Media**. Adequate record retention facilities shall be available for storing tapes and printouts, as well as all supporting documents as may be required by law.

(4) *Records Retention*. All records pertaining to transactions involving sales or use tax liability shall be preserved for a period of not less than [ ] years.

(5) *Examination of Records*. All of the foregoing records shall be made available for examination on request by the Executive Director **[Department]** **[Commissioner]** **[Commission]** **[Board]** or his **[its]** authorized representatives.

(6) *Failure of the Taxpayer to Maintain and Disclose Complete and Adequate Records*. Upon failure by the taxpayer, without reasonable cause, to substantially comply with the requirements of this regulation, the Executive Director **[Department]** **[Commissioner]** **[Commission]** **[Board]** shall:

a. Impose and not abate or reduce in amount any penalty as may be authorized by law.

b. Enter such other order as may be necessary to obtain compliance with this regulation in the future by any taxpayer found not be in substantial compliance with the requirements of this regulation.

# Appendix E
## Multistate Tax Commission
## Trucking Regulation

*Adopted July 11, 1986*

Reg. IV.18.(g). *Special Rules: Trucking Companies.*

The following special rules are established with respect to trucking companies:

(1) *In General.* As used in this regulation, the term "trucking company" means a motor common carrier, a motor contract carrier, or an express carrier which primarily transports tangible personal property of others by motor vehicle for compensation. Where a trucking company 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 this regulation. In such cases, the first step is to determine what portion of the trucking company's income constitutes "business" income and what portion constitutes "nonbusiness" income under Article IV.1 and Regulation IV.1 thereunder. Nonbusiness income is directly allocable to specific states pursuant to the provisions of Article IV.5 to .8, inclusive. Business income is apportioned among the states in which the business is conducted and pursuant to the property, payroll, and sales apportionment factors set forth in this regulation. The sum of (i) the items of nonbusiness income directly allocated to this state and (ii) the amount of business income attributable to this state constitutes the amount of the taxpayer's entire net income which is subject to tax in this state.

(2) *Business and Nonbusiness Income.* For definitions, rules, and examples for determining business and nonbusiness income, see Regulation IV.1.

(3) *Apportionment of Business Income*

(i) *In General.* The property factor shall be determined in accordance with Regulation IV.10 to .12, inclusive, the payroll factor in accordance with Regulation IV.13 to .14, and the sales factor in accordance with Regulation IV.15 to .17, inclusive, except as modified by this regulation.

(ii) *The Property Factor*

A. *Property Valuation.* Owned property shall be valued at its original cost and property rented from others, including purchased transportation, shall be valued at eight (8) times the net annual rental rate in accordance with Article IV.11 and Regulation IV.11. To the extent that the taxpayer's records reflect a separate charge incurred for the use of purchased transportation attributable to the property so used, such separate charge shall be used in calculating the value of rented property. If such a charge is not separated from that attributable to the compensation paid for the operator of the purchased transportation, the total combined charge shall be reduced by 20% to determine that portion of the charge attributable solely to the value of the rented property. Mobile property, other than purchased transportation, which is owned by other trucking companies and temporarily used by the taxpayer in its business and for which a per diem or mileage charge is made shall not be included in the property factor as rented property. Mobile property which is owned by the taxpayer and temporarily used by other trucking companies in their business and for which a per diem or mileage charge is made by the taxpayer shall be included in the property factor of the taxpayer.

B. *General Definitions*. The following definitions are applicable to the numerator and denominator of the property factor, as well as other apportionment factor descriptions:

1. "Average value" of property means the amount determined by averaging the values at the beginning and end of the income tax year, but the [**insert here the title of the appropriate administrative agency**] may require the averaging of monthly values during the income year or such averaging as is necessary to reflect properly the average value of the trucking company's property. (See Article IV.12 and Regulation IV.12.)

2. "Mobile property" means all motor vehicles, including trailers, engaged directly in the movement of tangible personal property, other than support vehicles used predominantly in a local capacity. Mobile property shall include purchased transportation.

3. A "mobile property mile" is the movement of a unit of mobile property a distance of one mile whether loaded or unloaded.

4. "Original cost" is deemed to be the basis of the property for federal income tax purposes (prior to any federal income tax adjustments, except for subsequent capital additions, improvements thereto, or partial dispositions); or, if the property has no such basis, the valuation of such property for Interstate Commerce Commission purposes. If the original cost of property is unascertainable under the foregoing valuation standards, the property is included in the property factor at its fair market value as of the date of acquisition by the taxpayer. (Regulation IV.11.(a).)

5. "Property used during the course of the income year" includes property which is available for use in the taxpayer's trade or business during the income year.

6. "Purchased transportation" means the taxpayer's use of a motor vehicle owned and operated by another for the purpose of transporting tangible personal property for which a charge, whether based upon a per diem, mileage, or other basis, is incurred.

7. "Temporarily used" means the use of any mobile property owned by another for a period not to exceed a total of 30 days during any income year.

8. The "value" of owned real and tangible personal property means its original cost. (See Article IV.11 and Regulation IV.11.(a).)

9. The "value" of rented real and tangible personal property means the product of eight (8) times the net annual rental rate. (See Article IV.11 and Regulation IV.11.(b).)

C. *The Denominator and Numerator of the Property Factor*. The denominator of the property factor shall be the average value of all of the taxpayer's real and tangible personal property owned or rented and used during the income year. The numerator of the property factor shall be the average value of the taxpayer's real and tangible personal property owned or rented and used in this state during the income year. In the determination of the numerator of the property factor, all property, except mobile property as defined in this regulation, shall be included in the numerator of the property factor in accordance with Article IV.10 to .12, inclusive, and Regulation IV.10 to .12, inclusive.

Mobile property as defined in this regulation, which is located within and without this state during the income year shall be included in the numerator of the property factor in the ratio which mobile property miles in the state bear to the total mobile property miles.

(iii) *The Payroll Factor.* The denominator of the payroll factor is the compensation paid everywhere by the taxpayer during the income year for the production of business income. (See Article IV.13 and .14 and Regulation IV.13 and .14.) The numerator of the payroll factor is the total compensation paid in this state during the income year by the taxpayer. With respect to all personnel, except those performing services within and without this state, compensation paid to such employees shall be included in the numerator as provided in Article IV.13 and .14 and Regulation IV.13 and .14.

With respect to personnel performing services within and without this state, compensation paid to such employees shall be included in the numerator of the payroll factor in the ratio which their services performed in this state bear to their services performed everywhere based on mobile property miles.

(iv) *The Sales (Revenue) Factor*

A. *In General.* All revenue derived from transactions and activities in the regular course of the taxpayer's trade or business which produce business income shall be included in the denominator of the revenue factor. (See Article IV.1 and Regulation IV.1.)

The numerator of the revenue factor is the total revenue of the taxpayer in this state during the income year. The total state revenue of the taxpayer, other than revenue from hauling freight, mail, and express, shall be attributable to this state in accordance with Article IV.15 through .17 and Regulation IV.15 through .17.

B. *Numerator of the Sales (Revenue) Factor From Freight, Mail, and Express.* The total revenue of the taxpayer attributable to this state during the income year from hauling freight, mail, and express shall be:

1. Intrastate: All receipts from any shipment which both originates and terminates within this state; and,

2. Interstate: That portion of the receipts from movements or shipments passing through, into, or out of this state as determined by the ratio which the mobile property miles traveled by such movements or shipments in this state bear to the total mobile property miles traveled by movements or shipments from points of origin to destination.

(4) *Records.* The taxpayer shall maintain the records necessary to identify mobile property and to enumerate by state the mobile property miles traveled by such mobile property as those terms are used in this regulation. Such records are subject to review by **[insert here the title of the appropriate administrative agency]** or its agents.

(5) *De Minimis Nexus Standard.* Notwithstanding any provision contained herein, this Regulation IV.18.(g) shall not apply to require the apportionment of income to this state if the trucking company during the course of the income tax year neither:

a. owns nor rents any real or personal property in this state, except mobile property; nor

b. makes any pick-ups or deliveries within this state; nor

c. travels more than twenty-five thousand mobile property miles within this state; provided that the total mobile property miles traveled within this state during the income tax

**year do not exceed three percent of the total mobile property miles traveled in all states by the trucking company during that period; nor**

**d. makes more than twelve trips into this state.**

# Appendix F

## Multistate Tax Commission

## Public Law 86-272 Guidelines

*Adopted June 21, 1985*

[The Multistate Tax Commission has adopted the following guideline for use by its member states in determining whether a corporation has a taxable nexus within a state's borders for income tax purposes. It adopted this guideline under the title "Information Concerning Practices of Multistate Tax Commission States under Public Law 86-272." It invites all states to adopt this guideline.]

Public Law 86-272, 15 U.S.C. 381-384, (hereafter "P.L. 86-272") restricts a state from imposing a net income tax on income derived within its borders from interstate commerce if the only business activity of the taxpayer within the state consists of the solicitation of orders for sales of tangible personal property, which orders are to be sent outside the state for acceptance or rejection, and, if accepted, are filled by shipment or delivery from a point outside the state. For the purposes of this document, the term "net income tax" shall also include a franchise tax measured by net income. If any sales are made into a state which is precluded by P.L. 86-272 from taxing the income of the seller, such sales remain subject to throwback to the appropriate state which does have jurisdiction to impose its net income tax upon the income derived from those sales.

It is the policy of the state signatories hereto to impose their net income tax, subject to legislative limitations, to the fullest extent constitutionally permissible. Therefore, it is also the policy of those states to construe the provisions of P.L. 86-272 narrowly so as to apply that law to only those limited circumstances clearly and reasonably intended by Congress. The following information reflects the signatory states' current practices with regard to: (1) whether a particular factual circumstance is considered either immune or not immune from taxation by reason of P.L. 86-272; and (2) the jurisdictional standards which will apply to sales made in another signatory state for purposes of applying a throwback rule (if applicable) with respect to such sales.

### I
### NATURE OF PROPERTY BEING SOLD

Only the sale of tangible personal property is afforded immunity under P.L. 86-272; therefore, the leasing, renting, licensing or other disposition of tangible personal property, intangibles or any other type of property is not immune from taxation by reason of P.L. 86-272. The definition of tangible personal property for this purpose is that to be found under each state's respective laws.

## II
## SOLICITATION OF ORDERS

For the in-state activity to be immune, it must be limited solely to solicitation (except for that activity conducted by independent contractors described in Section III below). If there is any other activity unrelated to solicitation, the immunity shall be lost. Examples of activities presently treated by the signatory states (unless otherwise stated as an exception or addition) as either non-immune or immune are as follows:

A. Non-Immune Activities:

The following in-state activities will cause otherwise immune sales to lose their immunity:

1. Making repairs or providing maintenance.
2. Collecting delinquent accounts.
3. Investigating credit worthiness.
4. Installation or supervision of installation.
5. Conducting training courses, seminars or lectures.
6. Providing engineering functions.
7. Handling customer complaints.
8. Approving or accepting orders.
9. Repossessing property.
10. Securing deposits on sales.
11. Picking up or replacing damaged or returned property.
12. Hiring, training, or supervising personnel.
13. Providing shipping information and coordinating deliveries.
14. Maintaining a sample or display room in excess of two weeks (14 days) during the tax year.
15. Carrying samples for sale, exchange or distribution in any manner for consideration or other value.
16. Owning, leasing, maintaining or otherwise using any of the following facilities or property in-state:
    a. Repair shop.
    b. Parts department.
    c. Purchasing office.
    d. Employment office.
    e. Warehouse.
    f. Meeting place for directors, officers, or employees.
    g. Stock of goods.
    h. Telephone answering service.
    i. Mobile stores, *i.e.*, trucks with driver salesmen.
    j. Real property or fixtures of any kind.
17. Consigning tangible personal property to any person, including an independent contractor.
18. Maintaining, by either an in-state or an out-of-state resident employee, of an office or place of business (in-home or otherwise).

19. Conducting any activity in addition to those described in paragraph II.B. below which is not an integral part of the solicitation of orders.

B. Immune Activities:

The following in-state activities will not cause the loss of immunity for otherwise immune sales:

1. Advertising campaigns incidental to missionary activities.
2. Carrying samples only for display or for distribution without charge or other consideration.
3. Owning or furnishing autos to salesmen.
4. Passing inquiries and complaints on to the home office.
5. Incidental and minor advertising, *i.e.*, notice in a newspaper that a salesman will be in town at a certain time.
6. Missionary sales activities.
7. Checking of customers' inventories (for re-order, but not for other purposes).
8. Maintaining a sample or display room for two weeks (14 days) or less during the tax year.
9. Soliciting of sales by an in-state resident employee of the taxpayer; provided the employee maintains no in-state sales office or place of business (in-home or otherwise).

## III
## INDEPENDENT CONTRACTORS

P.L. 86-272 provides immunity to certain in-state activities if conducted by an independent contractor that would not be afforded if performed by the taxpayer directly. Independent contractors may engage in the following limited activities in the state without the taxpayer's loss of immunity:

1. Soliciting sales.
2. Making sales.
3. Maintaining a sales office.

Sales representatives who represent a single principal are not considered to be independent contractors and are subject to the same limitations as employees.

Maintenance of a stock of goods in the state by the independent contractor under consignment or any other type of arrangement with the principal shall remove the immunity.

## IV
## MISCELLANEOUS PRACTICES

A. Interstate Commerce.

The only activity in the state must be in interstate commerce. If there is any other activity (except that described in II.B. or otherwise incidental to solicitation), then the immunity shall be lost.

Requisites are:

1. Approval of the sales *must* be made outside the state (except for sales by independent contractors).
2. Deliveries *must* be made from a point outside the state.

B. Incorporated

The immunity afforded by P.L. 86-272 does not apply to any corporation incorporated within the taxing state.

C. Service vs. Sale

Sales of services are not immune under P.L. 86-272. If a sale consists of a mixture of tangible personal property and services, the immunity shall be lost. Examples of such a mixture are:

1. Photographic development.
2. Fabrication of customer's materials.
3. Installation of equipment.
4. Architectural and engineering services.

# Appendix G
## Multistate Tax Commission
## Public Law 86-272

§381. *Imposition of net income tax.*

(a) *Minimum standards.*

No State, or political subdivision thereof, shall have power to impose, for any taxable year ending after September 14, 1959, a net income tax on the income derived within such State by any person from interstate commerce if the only business activities within such State by or on behalf of such person during such taxable year are either, or both, of the following:

(1) the solicitation of orders by such person, or his representative, in such State for sales of tangible personal property, which orders are sent outside the State for approval or rejection and, if approved, are filled by shipment or delivery from a point outside the State; and

(2) the solicitation or orders by such person, or his representative, in such State in the name of or for the benefit of a prospective customer of such person, if orders by such customer to such person to enable such customer to fill orders resulting from such solicitation are orders described in paragraph (1).

(b) *Domestic corporations; persons domiciled in or residents of a State.*

The provisions of subsection (a) of this section shall not apply to the imposition of a net income tax by any State, or political subdivision thereof, with respect to —

(1) any corporation which is incorporated under the laws of such State; or

(2) any individual who, under the laws of such State, is domiciled in, or a resident of, such State.

(c) *Sales or solicitation of orders for sales by independent contractors.*

For purposes of subsection (a) of this section, a person shall not be considered to have engaged in business activities within a State during any taxable year merely by reason of sales in such State, or the solicitation of orders for sales in such State, of tangible personal property on behalf of such person by one or more independent contractors, or by reason of the maintenance of an office in such State by one or more independent contractors whose activities on behalf of such person in such State consist solely of making sales, or soliciting orders for sales, of tangible personal property.

(d) *Definitions.*

For purposes of this section —

(1) the term "independent contractor" means a commission agent, broker, or other independent contractor who is engaged in selling, or soliciting orders for the sale of, tangible personal property for more than one principal and who holds himself out as such in the regular course of his business activities; and

(2) the term "representative" does not include an independent contractor.

§382. *Assessment of net income taxes; limitations; collection.*

(a) No State, or political subdivision thereof, shall have power to assess, after September 14, 1959, any net income tax which was imposed by such State or political subdivision, as the case may be, for any taxable year ending on or before such date, on the income derived within such State by any person from interstate commerce, if the imposition of such tax for a taxable year ending after such date is prohibited by section 381 of this title.

(b) the provisions of subsection (a) of this section shall not be construed —

(1) to invalidate the collection, on or before September 14, 1959, of any net income tax imposed for a taxable year ending on or before such date, or

(2) to prohibit the collection, after September 14, 1959, of any net income tax which was assessed on or before such date for a taxable year ending on or before such date.

§383. *Definition.*

For purpose of this chapter, the term "net income tax" means any tax imposed on, or measured by, net income.

§384. *Separability of provisions.*

If any provision of this chapter or the application of such provision to any person or circumstance is held invalid, the remainder of this chapter or the application of such provision to persons or circumstances other than those to which it is held invalid, shall not be affected thereby.

# Appendix H
## Multistate Tax Commission
## Compact Enactments

| Member States | Effective Date | Withdrawal Date |
|---|---|---|
| Alaska | July 1, 1970 | |
| Arkansas | January 1, 1968 | |
| California | January 1, 1976 | |
| Colorado | July 1, 1968 | |
| District of Columbia | July 1, 1980 | |
| Florida | August 4, 1967 | June 30, 1976 |
| Hawaii | May 7, 1968 | |
| Idaho | April 10, 1968 | |
| Illinois | August 4, 1967 | August 29, 1975 |
| Indiana | July 1, 1971 | June 30, 1977 |
| Kansas | August 4, 1967 | |
| Michigan | July 1, 1970 | |
| Minnesota | July 1, 1982 | |
| Missouri | October 13, 1967 | |
| Montana | July 1, 1969 | |
| Nebraska | October 23, 1967 | June 30, 1985 |
| Nevada | August 4, 1967 | June 30, 1981 |
| New Mexico | August 4, 1967 | |
| North Dakota | July 1, 1969 | |
| Oregon | September 13, 1967 | |
| South Dakota | July 1, 1967 | |
| Texas | August 4, 1967 | |
| Utah | May 13, 1969 | |
| Washington | August 4, 1967 | |
| West Virginia | July 1, 1980 | June 30, 1985 |
| Wyoming | January 24, 1969 | May 27, 1977 |

| Associate Member States | Effective Date | Withdrawal Date |
|---|---|---|
| Alabama* | October 17, 1967 | |
| Alaska | June 7, 1968 | To Full Member |
| Arizona | June 7, 1968 | |
| Arkansas | October 17, 1967 | To Full Member |
| California | January 23, 1968 | To Full Member |
| Colorado | January 23, 1968 | To Full Member |
| Georgia | June 11, 1971 | |
| Hawaii | January 23, 1968 | To Full Member |
| Idaho | October 17, 1967 | To Full Member |
| Indiana | January 23, 1968 | To Full Member |
| Louisiana | October 27, 1969 | |
| Maryland | July 27, 1970 | |
| Massachusetts | January 23, 1968 | |
| Michigan | November 19, 1968 | To Full Member |
| Minnesota | January 26, 1971 | To Full Member |
| Montana | January 23, 1968 | To Full Member |
| New Jersey | October 14, 1970 | |
| New York | October 27, 1969 | March 9, 1971 |
| North Dakota | January 23, 1968 | To Full Member |
| Ohio | June 11, 1971 | |
| Oklahoma | June 25, 1964 | March 1, 1977 |
| Pennsylvania | January 23, 1968 | |
| South Dakota | October 27, 1969 | To Full Member |
| Tennessee | June 20, 1969 | |
| Utah | January 23, 1968 | To Full Member |
| Virginia | October 27, 1969 | FY 75/76 |
| West Virginia | June 7, 1968 | To Full Member |
| Wyoming | October 17, 1967 | To Full Member |

*Compact enacted in Alabama but not effective unless and until the U.S. Congress enacts legislation specifically giving its consent for the State to enter into this Compact.