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Sent: Wednesday, July 6, 2022 1:34 PM
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Subject: SSF rulemaking [IWOV-IMANAGE.FID1300298]

Phil,

In preparation for our meeting tomorrow, our taxpayer group has been discussing the issue that came up in the meeting with the Commission last week concerning Rule 581. We have a modest suggestion for clarification of what we proposed last week, and I present it at the end of this email. But the meat of the discussion among our group has been over whether special industries were intended to, and should, have the election to be taxed under the new single-sales, market-based regime. We re-examined our position in light of the arguments you presented, and re-affirmed our position that this is the correct position, with the minor modification shown below. Most of the reasons were presented during our meeting:

- An overarching policy consideration, as John Bernasconi pointed out during the meeting, is that we now have a better method of apportioning income. The Commission likes the single-sales, market-based sourcing rules, and we are in a new paradigm that requires administrators and taxpayers alike to re-examine the old ways of apportioning income. If there were doubt about whether a taxpayer should be able to use single-sales, market sourcing, the doubt should be resolved in favor of allowing that option.
- The legislation contemplates that option. The wording is admittedly ambiguous, but was intended to give special industries maximum flexibility to use one of the methods that have been approved for one or more purposes. We believe any rule has to deal with the wording of subsection 10(b) that gives taxpayers "an election to use a special industry regulation."
- An example of that intent toward flexibility is the telecommunications industry, which not only has the option to use a single factor or three factors, but can use market sourcing or cost of performance. Those are essentially the same options that our draft of Rule 581.05 provides. The legislature would logically have intended for the special industries to have that same flexibility.
- You mentioned a concern that subsection (10) is inconsistent with subsection (18), that subsection (18) might be superfluous if a taxpayer can elect out of it, and that the Commission would still have subsection (17) available to countermand a taxpayer election not to use the special industry rule. However, it may be that for most industries, the special industry rules will continue to be the better method, so subsection (18) is still clearly relevant. The provision of subsection (10) that refers to the election to use the special industry rules obviously presupposes that such rules have been adopted, but may not apply in a given case, so subsections (10) and (18) are in harmony. And it would frustrate the ability to make the election if an auditor could assert under subsection (17) that a different method were required, at least if the different method were simply the special industry rule that the taxpayer can opt out of.

As for the minor modification in our draft of the changes in Rule 581.05, first, here is what we proposed last week, with our changes in blue:

a. ~~References in MTC Regulation IV.18.(d) to the computation of the~~ ~~percentage being~~ ~~apportionment~~ ~~the total of the property, payroll and sales percentages divided by three (3), is to be replaced with the total of property, payroll, and two (2) times the sales percentages divided by four (4) as required by Section 63-3027(i), Idaho Code.~~ The default apportionment method in Idaho is sales factor only. Pursuant to section 63-3027(10)(b), Idaho Code, taxpayers subject to special industry regulations as provided in Rule 580 may elect to use the property, payroll, and sales factors, if the special industry regulation applicable to them provides for a property and/or payroll factor or to use solely the sales factor of the special industry rules. If a taxpayer subject to a special industry regulation does not make an election as described in the preceding sentence, then the taxpayer will be subject to the sales factor rules set for in Rules 525-551. See Rule 310 for instructions on making the election.

We think the second blue sentence is a little confusing, because the election referred to "in the preceding sentence" is the election to use the three-factor formula, and is not election to use the special industry rule which is the focus of this sentence. So we suggest a minor change to the wording to clarify that, and to flip the direction of the election so that the default would be to use the special industry rule.

> If a taxpayer otherwise subject to a special industry regulation makes an election not to use that regulation as permitted by Idaho Code section 63-3027(10)(b), then the taxpayer will be subject to the sales factor rules set for in Rules 525-551.

Please pass this email on to the others who will participate in tomorrow's call, and let me know if you have any questions.

Thanks, Rick

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