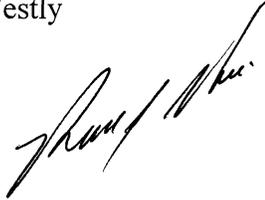


M e m o r a n d u m

To : Honorable John Chiang, Chair
Honorable, Claude Parrish, Vice Chairman
Honorable Betty T. Yee, Acting Board Member
Honorable Bill Leonard
Honorable Steve Westly

Date : August 29, 2005

From : Ramon J. Hirsig
Executive Director



Subject : **Executive Director Report – August 31, 2005**
Report on Multistate Tax Commission and Federation of Tax Administrators

California is currently a member state of both the Multistate Tax Commission (MTC) and the Federation of Tax Administrators (FTA). Attached is background information on both of these agencies as well as an explanation of the provisions of the California Revenue and Taxation Code governing our involvement in MTC.

Under the provisions of Revenue and Taxation Code section 38011, the executive officers of the Franchise Tax Board and the State Board of Equalization alternate as the California member of MTC, the former being the member during MTC's fiscal years beginning in even-numbered years and the latter during MTC's fiscal years beginning in odd-numbered years. The FTB's executive director was California's MTC member for the prior fiscal year of 2004/05. For the current fiscal year, 2005/06, that responsibility has shifted by law to this Board's executive director.

As executive director of the BOE, I have a statutory duty to serve as California's member to MTC this fiscal year. Historically, California's MTC member has consulted with the executive management of the other agency to ensure that he or she can fully represent California's interest at MTC. This practice continues to be worthwhile, so I will consult FTB executive management to discuss MTC matters of interest to the FTB. I will meet with executive management of MTC to gather information relevant to the current and upcoming issues before MTC, and I will also gather information relevant to current and upcoming issues before FTA. I will then report on such matters that may be of interest to you at our Sacramento Board meeting in October. I note that I will not commit California on any substantive issue without first consulting with you. Unless the Board directs otherwise, I will proceed as stated.

RJH:te
Attachment

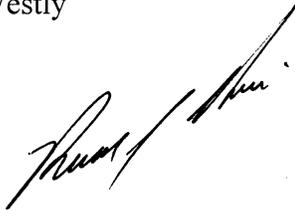
ITEM P1
SUB-ITEM 2
8-31-05

Memorandum

To : Honorable John Chiang, Chair
Honorable, Claude Parrish, Vice Chairman
Honorable Betty T. Yee, Acting Board Member
Honorable Bill Leonard
Honorable Steve Westly

Date : August 29, 2005

From : Ramon J. Hirsig
Executive Director



Subject : **Background and Summary of Board Participation in – Multistate Tax Commission and Federation of Tax Administrators**

This memorandum provides a general discussion of the Multistate Tax Commission (MTC), and some information regarding the Federation of Tax Administrators (FTA), and the Board's past and present relationship with each.

What MTC Is

MTC was created in 1967 pursuant to the Multistate Tax Compact among several of the states. California statutorily enacted the compact (Rev. & Tax. Code, § 38001 et seq.), and became a Compact Member of MTC in 1976. The Compact explains its purpose as follows:

- “1. Facilitate proper determination of State and local tax liability of multistate taxpayers, including the equitable apportionment of tax bases and settlement of apportionment disputes.
- “2. Promote uniformity or compatibility in significant components of tax systems.
- “3. Facilitate taxpayer convenience and compliance in the filing of tax returns and in other phases of tax administration.
- “4. Avoid duplicative taxation.”

(Rev. & Tax. Code, § 38006, art. I.) MTC explains on its website that MTC:

“is a joint agency of state governments established to

- ◆ improve the fairness, efficiency and effectiveness of state tax systems as they apply to interstate and international commerce, and

- ◆ preserve state tax sovereignty.”

What MTC Does

MTC maintains several programs to further its goals. It offers an Alternative Dispute Resolution Program to help resolve multistate disputes between a taxpayer and two or more states. It has a Joint Audit Program that audits businesses for several states at the same time. It has a National Nexus Program that includes a procedure for voluntary disclosure of tax liabilities described on MTC’s web site as follows:

“assists businesses involved in multistate commerce to voluntarily resolve potential state sales/use tax and income/franchise tax liabilities where nexus is the central issue. The National Nexus Program acts as a coordinator through which companies may approach a number of States anonymously and seek resolution of potential liabilities arising from past activities.”

MTC also engages in a number of other activities to further its goal of promoting uniformity and compatibility of tax systems. For example, MTC has created and maintains a Uniform Sales and Use Tax Certificate for use in any of the states that have approved its use (including California). MTC participates in the Streamlined Sales Tax Project (SSTP), conducts surveys, publishes reports on various topics, represents its members’ interests before Congress, and participates in court cases of significant interest to its members. MTC also researches, negotiates, and recommends uniform tax laws and regulations that states may choose to adopt.

Who Participates in MTC

There are several levels of participation in MTC. “Compact Member” is the term MTC uses to describe its member states that have adopted the Multistate Tax Compact. There are currently 21 Compact Members of MTC (20 states plus the District of Columbia). These are the members that govern MTC and its activities. Compact Members also share general MTC costs (now along with Sovereignty Members as explained below) through a formula specified in the Compact.

The next level of participation is called “Sovereignty Membership,” which MTC’s web site describes as joining “in shaping and supporting the Commission’s efforts to preserve state taxing authority and improve multistate tax policy and administration. They will participate in the Commission’s uniformity, federal relations, educational and litigation support activities. Costs conform to the formula in the Compact. Benefits are similar to Compact Membership, but do not require enactment of the Compact.” Such a member pays the same fee it would pay if it were a Compact Member (MTC bylaw 13, subd. (b)1), but without the vote it would have. There are currently five Sovereignty Members of MTC.

Next is “Associate Membership,” which MTC’s web site describes as “States that wish to participate in Commission meetings with an eye to considering broader participation in

Commission activities.... There is no cost for Associate Membership.” There are currently 18 Associate Members of MTC.

Finally, Project Members are states that participate in one (or more) of MTC’s programs without otherwise being members of MTC. There are currently 3 Project Members of MTC.

California’s Participation in MTC

As noted above, California became a Compact Member of MTC in 1976. The Multistate Tax Compact provides that a Compact Member must provide by law for the selection of its representative to MTC. (Rev. & Tax. Code, § 38006, art. VI, subd. 1.(b).) When adopting the Compact, the Legislature also complied with this requirement by adopting Revenue and Taxation Code section 38011, which provides:

“The executive officer of the Franchise Tax Board shall be the member of the Multistate Tax Commission to represent this state for the commission’s fiscal year period beginning in even-numbered calendar years and the executive secretary of the State Board of Equalization shall be such member for the commission’s fiscal year period beginning in odd-numbered calendar years.”

Over the years since California became a Compact Member of MTC, the executive officers of FTB and BOE have worked closely together to ensure that each agency’s interests (i.e., the entire state’s interests) are fully represented in MTC regardless of which executive officer is the official member of MTC.

MTC Dues

The budget as determined by MTC is paid by its members according to the terms of the Compact (now by Sovereignty Members as well as Compact Members). California’s dues are split between FTB and BOE. The dues paid by BOE (i.e., one-half of California’s total) were \$218,610 for fiscal year 2004/05. MTC sends a notice of the dues payable by BOE each year, which we may pay in 12 equal monthly amounts.

Voting

Under the Compact, each member of MTC has one vote. MTC may not act unless a majority of the members are present¹ and the action is approved by a majority of the total number of members. (Rev. & Tax. Code, § 38006, art. VI, subd. 1.(c).) MTC’s bylaws add a second condition for adoption of an action by MTC - the matter must receive not only a majority of the votes of the member states, but the affirmative vote must also represent a majority of the total population of all the member states according to the current United States Statistical Abstract.

¹ For purposes of special MTC meetings other than the annual meeting, the quorum can be satisfied through presence of a member by telephone or other similar technology. (MTC bylaw 5, subd. (a).) A member can also participate by telephone or similar technology during an annual meeting under specific conditions, but not to comprise a quorum; a quorum at the annual meeting requires a majority of members physically present at the meeting. (*Ibid.*)

(MTC bylaw 5, subd. (e).) Thus, California's voting power is about 31 percent of the total possible MTC vote under this provision.

Meetings

MTC holds a number of meetings and conferences. There is an annual meeting of the entire MTC, which is held in July of each year. (Rev. & Tax. Code, § 38006, art. VI, subd. 1.(e); MTC bylaw 4(a).) MTC's executive committee meets four times a year, in many cases in connection with other meetings, such as the annual meeting, or in conjunction with meetings of MTC's various committees. In many cases, work is done via teleconference rather than at in-person meetings. There are also teleconferences for informational purposes and other dialogue. For example, MTC conducts an "Update for the States" teleconference twice per month to brief state tax agencies on the latest news and developments concerning multistate taxation, including congressional developments, and the work of MTC.

BOE's Recent Participation

In 1999, BOE supported legislation to withdraw California from MTC. The legislation was not enacted, and California remains an MTC Compact Member. Since that time, however, the Board has not encouraged or authorized active participation in MTC. The Board was also under budget constraints that limited any travel not absolutely necessary. So, during the last fiscal year that BOE executive director was the California member of MTC (beginning July 1, 2003), the executive director did not cast a vote on behalf of California on MTC actions. My understanding is that FTB has continued to actively participate in MTC matters, and that the FTB executive director, or his designee, did cast votes for California during each fiscal year in which he was the California member of MTC.

In other respects (beyond casting votes), BOE has continued participation. For example, BOE has been participating in the SSTP. Additionally, BOE continues to be a member of the National Nexus Program; thus any retailers who submit voluntary disclosures for California would be forwarded to us.²

Implications

As explained above, because of the weighting by population of votes of MTC's members, California's vote is more than 30 percent of the total vote. Since a majority vote is required to take any action (as opposed to a majority of the members voting, weighted or otherwise), over 50 percent of the weighted vote is required to take an action whether California votes or not. Therefore, if California does not vote, even if all other MTC members do vote, it would take over 70 percent of the vote to carry a motion. In effect, any time California does not vote, the impact is the same as if California were voting no. Abstaining from a vote because we do not have a position

² There is a charge for participation in the National Nexus Program. When California considered withdrawal from MTC, MTC decided to waive the additional fee for the National Nexus Program and allow California to continue to participate without additional charge above our mandatory MTC dues.

is, of course, appropriate. However, simply not participating does not seem consistent with California's adoption of the Multistate Tax Compact making California a Compact Member of MTC. Thus, as long as California is a Compact Member of MTC and pays its dues accordingly, I believe that it is prudent for us to use our voting power so that our state's voice is heard, for or against any proposal of interest to California, as appropriate.

By exercising California's vote, we can help shape MTC's policies and actions. I will bring substantive MTC matters to the Board with my recommendations, to obtain the Board's directions on California's positions on these matters.

FTA

FTA was organized in 1937 to improve the quality of state tax administration by providing services to state tax authorities and administrators. These services include tax research and information exchange, training, and intergovernmental and interstate coordination. FTA also represents the interests of state tax administrators before Congress and other federal policymakers. Unlike MTC, there is no California statute requiring membership in FTA. BOE, FTB, and the Employment Development Department are all members of FTA. BOE's portion of dues for fiscal year 2004/05 was \$30,567.

In the last two years, budgetary constraints on travel and enrollment costs have tended to limit BOE's staff involvement in FTA, with most activity focused on attending FTA's motor fuels tax section's annual and regional meetings, uniformity meetings, and FTA-sponsored motor fuels training. Ongoing federal funds for these programs have been used to cover travel and participation expenses. Before the budgetary constraints, BOE had been more active in FTA matters, sending staff representatives to FTA meetings, conferences, committees, workshops, and training in the areas of sales and use tax, investigations, fuel and various excise taxes, compliance, enforcement, uniformity, research and statistics, and technology services.

FTA and MTC

FTA and MTC often have similar interests and goals, and have worked together when appropriate. While MTC's stated purpose of furthering uniformity requires that it research and develop new policy in the form of proposed uniformity measures, FTA is not totally absent from that field. For example, both FTA and MTC work with the states on the SSTP, and it includes many uniformity provisions. While FTA is heavily involved in offering training for its members, MTC also offers some training for its members. Nevertheless, while it may seem that both FTA and MTC cover the same areas, that is the result of similarity of interests, that is, providing services and representing their member states. However, the different focus of each organization results in little actual overlap, and to the extent that each organization has found it efficient to pool their resources to further their shared goals, they have done so, such as for the SSTP.

cc: Ms. Audrey Noda
Mr. Neil Shah
Ms. Sylvia Tang
Ms. Barbara Alby
Ms. Marcy Jo Mandel