REQUEST LETTER

December 13, 2006

NAME
ADDRESS
PHONE
EMAIL

Dear TP REPRESENTATIVE,

We are requesting a ruling from the Utah State Tax Commission as to the application of Utah's corporate franchise tax apportionment rules to financial institution doing business in Utah. Please find attached a Memorandum in Support of Ruling Request, which provides relevant facts, sets forth the issue upon which we are requesting that the Commission rule, and a detailed analysis of applicable laws, regulations and other guidance in support of what we believe to be the correct conclusion. We are submitting this ruling request on a "no-name basis, subject to receipt of a favorable ruling.

It is our understanding that this request will be assigned to a Commission reviewer. Once it has been assigned, we ask that the reviewer contract me at ###### or my colleague, 2ND NAME, at ######, so that we can discuss the procedures, any concerns and timing for obtaining the rule.

Your attention to this matter is greatly appreciated.

Sincerely,

NAME

Memorandum In Support of Ruling Request

September 7, 2005

I. Facts:

The applicant is organized in a parent-subsidiary structure (hereafter referred to as "Parent," "Subsidiary" and, collectively, "Taxpayers"). Subsidiary is a financial services business that does business in Utah and also has several employees in States X and Y. Subsidiary issues credit cards to individuals who reside in every state in the United States plus the District of Columbia. Subsidiary's number of credit card holders in a given state ranges from a maximum of approximately ###### to a minimum of approximately ######.

Subsidiary earns: (1) interest income and fees, such as late fees, cash advance fees, return check fees, over-limit fees, pay-by-phone fees and annual fees from its credit card holders (collectively, "Credit Card Income");[1] (2) interchange fees ("Interchange Fees") from banks that contract with merchants where the banks agree to pay Subsidiary (i.e., the issuer) a fee based on credit card charges made by Subsidiary's credit card holders; and (3) interest from installment loans made to individuals for the purchase of personal property ("Loan Interest").

Parent does business in multiple states. Parent services credit cards issued by Subsidiary and unrelated third parties. As part of its credit card serving function, Parent is required to register as a debt collector in all 50 States, which, in turn, requires Parent to register to do business in all such states. In addition, Parent files tax returns in many of the states in which it is registered.

It is assumed for purposes of this ruling request that:

1. Taxpayers are corporations for federal income and Utah corporation franchise tax purposes.

2. Taxpayers are members of a unitary group pursuant to Title 59, Chapter 7 of the Utah Code Annotated ("Code" or the" Code") and file as such for Utah franchise tax purposes.

3. Subsidiary is a "financial institution" pursuant to R865-6F-32.A.8 of the Utah Administrative Code {"regulation") and is "commercially domiciled" in Utah pursuant to regulation R865-6F-32.A.3. Other than the employees located in States X and Y, Subsidiary does not have property (other than credit card holders or re-possessed property) or employees in any other state.

4. Parent is not a "financial institution" pursuant to the above-referenced provision and does not, for Utah franchise tax purposes, have taxable nexus with Utah.

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[1] Please refer to the "Definitions" attachment

5. The Credit Card Income, Interchange Fees and Loan Interest are business income for purposes of regulation R865-6F-32.B.2.

II. Issue:

For Utah Corporation franchise tax apportionment purposes, what portion of Subsidiary's receipts from Credit Card Income, Interchange Fees and Loan Interest should be included in the numerator of Taxpayers' receipts factor (i.e., sourced to Utah?

III. Law and Analysis:

In general, where a taxpayer engages in business in Utah and other states, there are allocation and apportionment rules that apply to the taxpayer's taxable income base. Code section 59-7-303(1) provides that taxpayers having income from business activities taxable both within and without Utah must allocate and apportion their income according to Title 59, Chapter 7, Part 3 of the Code. For this purpose, Code section 59-7-305(2) provides that a taxpayer is taxable in another state if "that state has jurisdiction to subject the taxpayer to a net income tax regardless of whether, in fact, the state does to does not."[2]

Taxable income is allocated or apportioned depending on the type of income involved. In this regard, taxable income is bifurcated between "business income" and "non-business income." Code section 59-7-302(1) provides that business income is "income arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, management, and disposition of the property constitutes integral parts of the taxpayer's regular trade or business operations." Code section 59-7-302(4) provides that non-business income is all income other than business income.

In general, business income is subject to apportionment and non-business income is subject to separate set of allocation rules.[3] Code section 59-7-311 provides that business income must be apportioned to Utah by multiplying the income by a fraction, the numerator of which is the property factor plus the payroll factor plus the sales factor, and the denominator of which is three.[4]

For purposes of the apportionment formula, Code section 59-7-317 provides that the "sales factor" is a fraction, the numerator of which is the taxpayer's total sales in Utah, and the denominator of which is the taxpayer's total sales everywhere. In this context, Code section 59-7-302(5) provides that "sales" means all gross receipts of the taxpayer not allocated under

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[2] The term "state" includes any state of the United States and the District of Columbia. Code section 59-7-302(6).

[3] This ruling request is concerned only with business income. Accordingly, the allocation of non-business income is not addressed.

[4] For tax years beginning on or after January 1, 2006, taxpayers may elect of double-weight the sales factor. See UT HB 78, section 1, which amends Code section 59-7-311 to provide for the elections.

Sections 59-7-306 through 59-7-310 (which apply to non-business income).

A taxpayer's gross receipts are sourced to Utah (or not) depending on the type of activity in which a taxpayer is engaged. Gross receipts for sales other than sales of tangible personal property (i.e., receipts for services performed) generally are sourced based on the "cost of performance rule. Code section 59-7-319 provides that such receipts are sourced to Utah if the income-producing activity is performed in Utah, or the income-producing activity is performed both in and outside Utah and a greater proportion of the income-producing activity is performed in Utah than in any other state, based on costs of performance. Thus, under the cost of performance rule, a service provider that performed services with and without the State would source all of its gross receipts to Utah for apportionment purposes to the extent the greater portion of its income producing activities (based on cost) takes place in Utah.

There are, however, special allocation and apportionment rules for the financial services industry that apply in lieu of the foregoing general apportionment rules. Regulation R865-6F-32B.1 provides that a financial institution (as defined in regulation R865-6F-32A.8) whose business activity is "taxable" within the without Utah must allocate and apportion its net income as provided in regulation R865-6F-32B. As with the general rule cited above, regulation R865-6F-32A.20(b) provides that "taxable" means another state has the jurisdiction to subject the taxpayer to taxes regardless of whether the state actually imposes such taxes.

As with the general apportionment rules, regulation R865-6F-32B.2 provides that business income of a financial institution is apportioned pursuant to a formula consisting of the same three factors cited above – receipts, property and payroll.[5] These factor rules, however, are specific to activities performed by financial providers, several of which are relevant to this ruling request.

First, regulation R865-6F-32.C.7 provides that receipts from "credit card receivables," which include "interest and fees or penalties in the nature of interest from credit card receivables and receipts from fees charged to card holders, such as annual fees" are sourced to the billing address of the cardholer.[6] Thus, if a cardholder's billing address is not in Utah, the numerator of the receipts factor would not include the credit card receipts from such cardholder.

Second, regulation R865-6F-32C.9 provides that "credit card issuer's reimbursement fees" are sourced to Utah by multiplying the amount of such fees by a fraction, the numerator of which is the amount of credit card receivables sourced to Utah and the denominator of which

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[5] At the time of this writing, the Utah Tax Commission has not, to our knowledge, promulgated amended regulations to take into account the double-weighted sales factor election.

[6] For purposes of these rules, "credit card" means a credit, travel or entertainment card. Regulation R865-6F-32A.5.

is total amount of credit card receivables. Pursuant to R865-6F-32.A.6, credit card issuer's reimbursement fees are the fees a taxpayer receives from a merchant bank because one of the persons to whom the taxpayer has issued a credit card has charged merchandise of services to the credit card.

Third, regulation R865-6F-32.C.5 provides that "interest from loans not secured by real property" includes interest and fees or penalties in the nature of interest from borrowers located in Utah. A "loan" for this purpose means any extension of credit resulting from direct negotiations between a taxpayer and its customer. Thus, as with credit card receivables, if a borrower's address is not in Utah, the numerator of the receipts factor would not include interest receipts from such borrower.

The foregoing rules do not necessarily apply to all members of a combined group of corporations. Regulation R865-6F-32.4 provides that where a unitary group of corporations filing a combined report consists of financial institutions and non-financial institutions, the special apportionment rules, described above, apply on to the financial institutions. The remainder of the corporations in the group (assuming they are not in another special industry) would use the general allocation and apportionment rules.

In summary, the apportionment rules generally permit a financial institution doing business within and without Utah to source receipts from credit card receivables, credit car issuer's reimbursement fees and interest form loans not secured by real property to the billing address of the credit card holders. There is, however, an exception to these "customer sourcing" rules where the financial institution is commercially domiciled in Utah but where it is not taxable in other states.

Regulation R865-6F-32.C.15(a) provides that "all receipts assigned ... to a state in which the taxpayer is not taxable shall be included in the numerator of the receipts factor if the taxpayer's commercial domicile is in this state" (hereafter referred to as the "throwback rule").[7] For this purpose regulation R865-6F-32A.20 provides , in part, that "taxable" means" another state has the jurisdiction to subject the taxpayer to taxes regardless of whether that state actually imposes those taxes."

The regulations provide for two exceptions to the throwback rule. Presumably, these exceptions are intended to incorporate the "Finnigan" rule. As briefly discussed below, the Finnigan rule originated from a line of California cases that addressed the application of California's throwback rule in the context of a unitary group or corporations.

In *Appeal of Finnigan,*[8] two corporations, one with California nexus, one without, filed a

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[7] For this purpose, regulation section R865-6F-32.A.3 provides that "commercial domicile" means the principal place from which the trade or business of the taxpayer is directed or managed.

[8] Cal State Bd. Of Equiliz., August 28, 1988, Dkt. No. 88-SBE-022, *on reh'g*, Jan 24, 1990 (referred to as

unitary return. The corporation without nexus sold goods to customers located in states in which it was not subject to tax; however, the unitary affiliate was subject to tax in such states. At issue was whether California's throwback rule would apply since the selling corporation was not subject to tax in the destination states. The tax tribunal determined that the throwback rule would not apply because, although the seller was not subject to tax in the destination states, its unitary affiliate was taxable. The tribunal thus viewed the unitary group as one taxpayer for purposes of applying the throwback rule.
With the foregoing principal in mind, regulation R865-6F-32.C.15(b) provides the following two exceptions to the throwback rule:

1. If a unitary group includes one or more financial institution, and if any member of the unitary group is subject to the taxing jurisdiction of this state, the receipts of each financial institution in the unitary group shall be included in the numerator of this state's receipts factor as provided in C.1. through C.14. [which include the customer sourcing rules noted above] rather than being attributed to the commercial domicile of the financial institution as provided in C.15.a).
2. If a unitary group includes one or more financial institutions whose commercial domicile is in this state, and if any member of the unitary group is taxable in another state under section 59-7-305, the receipts of each financial institution in the unitary group that would be included in the numerator of the other state's receipts factor under C.1. through C.14 [which include the customer sourcing rules noted above] may not be included in the numerator of this state's receipts factor.

The first exception (1) presumably is directed at a financial institution within a Utah unitary group that is commercially domiciled outside of Utah (it would not otherwise make sense, when read in the context of the second exception). Employing the *Finnigan* principle, it provides that even though a non-commercially domiciled financial institution does not have nexus with Utah, as long as a unitary affiliate does, such financial institution may not throw its receipts back to its commercial domicile; rather, it should continue to source based on the regular sourcing rules (which include customer sourcing in C1. to C.14.). This ensures, for example, that if the financial institution had credit card holders residing in Utah, income earned from such persons would be included in the unitary group's Utah numerator.

The second exception (2), which is directed at a financial institution that is commercially domiciled in Utah, virtually encapsulates the basic facts and premise of *Finnigan.* It provides that, to the extent a unitary affiliate (of a financial institution that is commercially domiciled in Utah) is "taxable" in another state, the throwback rule does not apply to such financial institution. Code section 59-7-305 provides that a taxpayer is taxable in another state if "that state has jurisdiction to subject the taxpayer to a net income tax regardless of

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Finnigan I and Finnigan II). CF, There also is the *Joyce* rule, which is another line of California cases that came to the opposite conclusion of *Finnigan* (i.e., a unitary affiliate that has nexus with a state will not impact a selling corporation that does not have nexus).

whether, in fact, the state does or does not."

It is the second exception that is applicable for purposes of this ruling request. In this regard, the throwback rule would not apply to a financial institution that is commercially domiciled in Utah where, at least, a unitary affiliate is registered to do business in every state (and, thus, "taxable" in other states and, where necessary, filing tax returns in such states)[9] and where the financial institution has credit card holders in every state. Accordingly, such financial institution would be subject to the receipts sourcing rules contained in regulation section R865-6F-32.C.1. through C.14, which include customer sourcing for credit card receivables, interchange fees and interest from loans not secured by real property.

IV. Ruling Requested

Based on the foregoing, Taxpayers' income would be subject to apportionment because Subsidiary is doing business in Utah and is subject to tax in other states (and, though not critical is filing a return in States X and Y), as is Parent. The apportionment rules applicable to financial institutions would apply to Taxpayers because Subsidiary is a financial institution that is commercially domiciled in Utah within the meaning of regulation section R865-6F-32.A.8 and R865-6F-32.A.3. For this purpose, the Credit Card Income earned by Subsidiary is a "credit card receivable" because such income consists of interest and penalties and fees from credit cards issued by Subsidiary; the Interchange Fee is a "credit card issuer's reimbursement fee" because it is a fee earned by Subsidiary with respect to charges made by its cardholders to merchants who contract with other banks for reimbursements; and the Loan Interest is "interest from loans not secured by real property." Utah's throwback rule does not apply to Subsidiary because Subsidiary is "taxable" in those states in which cardholders reside (it also files returns in certain states) and Parent, its unitary affiliate, is "taxable" in all states in which it is registered both as a debt collector and to do business (and files tax returns therein) (i.e., Taxpayers are taxable in all 50 states plus the District of Columbia).

Accordingly:

1. Only Credit Card Income collected from cardholders with billing addresses in Utah must be included in the numerator of Taxpayers' receipts factor;
2. Only a *pro rata* portion of Interchange Fees, based on a ratio of Taxpayers' Credit Card Income sourced to Utah over Taxpayers' total Credit Card Income, must be included in the numerator of Taxpayers' receipts factor; and
3. Only Loan Interest received from borrowers located in Utah must be included in the numerator of Taxpayers' receipts factor.

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[9]The vast majority of the states require taxpayers that are merely registered to do business in such states to file a return.

DEFINITIONS

Annual Fee – Annual or monthly fees that are assessed to the credit card accounts that are either open or closed with a balance. The fee amount varies depending on the pricing strategy offered to the cardholder.

Cash Advance Fee – A fee is assessed if a cardholder chooses to withdraw cash against his/her credit account. This fee is calculated as a percentage of the transaction or as a flat minimum, whichever is greater.

Return Check Fee – A fee is assessed when a cardholder's payment is returned unpaid by their financial institution.

Over-limit Fee – A fee is assessed when a cardholder's account balance exceeds his/her credit limit.

Pay-by Phone Fee – This fee is assessed to a cardholder for the ability to make a payment to his/her credit card account over the telephone.

06-027

December 13, 2006

TP REPRESENTATIVE

COMPANY Request for a Ruling

Dear TP REPRESENTATIVE,

We previously requesting a ruling from the Utah Tax Commission as to the application of Utah's corporate franchise tax apportionment rules on behalf of a client, which is a financial institution doing business in Utah. We submitted the ruling request on a "no-name basis," subject to receipt of a letter confirming the conclusions reached in our request. In a letter dated July 26, 2006, the Commission, in fact, issued such a ruling (published on the Commission's Web site as 05-001).

We now seek on behalf of our client, COMPANY, to move forward with a "named" ruling that COMPANY may fully rely upon in filing its Utah corporation franchise tax returns. In this regard, please find attached a slightly amended version of our original ruling request, which accounts for the name of our client and other minor detail, none of which are material to our request. Our original no-name ruling request, the Commission's response, and the memorandum in support of the named ruling request are attached for your reference as Appendices, A,B and C respectfully.

We respectfully request that the named ruling be issued at the Commission's earliest convenience. Please call me at PHONE if you have any questions.

Your attention to this matter is greatly appreciated.

Sincerely,

2ND NAME for NAME

Attachments
Copy to 3RD NAME (COMPANY)
4TH NAME (2ND)
5TH NAME (3RD COMPANY)

MEMORANDUM IN SUPPORT OF RULING REQUEST FOR COMPANY BANK CORPORATION

I. FACTS

COMPANY is headquartered at ADDRESS. COMPANY was founded in 1997, is a top-50 issuer of Visa® cards and is an authorized issuer of MasterCard® cards. COMPANY also provides finance options to Marine and RV Dealers throughout the country, helping to facilitate boat and RV purchases for consumers. COMPANY has over 555,000 cardholders, which, on a per state basis, range from approximately 110,000 to 1,200. COMPANY specializes in credit programs that assist consumers looking to establish or rebuild their credit rating. COMPANY is FDIC insured and offers Certificates of Deposit with a variety of rates and terms.

2ND COMPANY, which wholly owns COMPANY, is a holding company headquartered at ADDRESS. 2ND COMPANY also wholly owns 4TH COMPANY, which does business at the foregoing address and in CITY, STATE. 4TH COMPANY manages and services credit and debit cards issued by COMPANY and unrelated third parties for which it earns a servicing fee.10 As part of its credit card servicing function, 4TH COMPANY is required to register as a debt collector in all 50 States, which, in turn, requires 4TH COMPANY to register to do business in all such states.

COMPANY earns the following types of income: (1) interest income and fees, such as late fees, cash advance fees, return check fees, over-limit fees, pay-by-phone fees and annual fees from its credit card holders (collectively, "Credit Card Income,,);11 (2) interchange fees ("Interchange Fees") from banks that contract with merchants where the banks agree to pay COMPANY (i.e., the issuer) a fee based on credit card charges made by COMPANY'S credit card holders; and (3) interest from installment loans made to individuals for the purchase of personal property ("Loan Interest").

It is assumed for purposes of this ruling request that:

1. COMPANY and 2ND COMPANY are corporations for federal income and Utah corporation franchise tax purposes.

2. 4TH COMPANY is a single member LLC ("SMLLC"), which is disregarded for federal income tax purposes.

3. Given that 4TH COMPANY is disregarded for federal income tax purposes, it is likewise disregarded for all relevant state and local tax purposes, such that 4TH COMPANY'S

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[10] COMPANY also has several employees working at the above-referenced CITY address.

[11] Please refer to the "Definitions" attachment.

activities are deemed to be the activities of 2ND COMPANY for income/ franchise tax purposes.[12]

4. 2ND COMPANY is not protected under Public Law 86-272.

5. COMPANY and 2ND COMPANY (collectively, "Taxpayers") are members of a unitary group pursuant to Title 59, Chapter 7 of the Utah Code Annotated ("Code" or the "Code") and file as such for Utah franchise tax purposes.

6. COMPANY is a "financial institution" pursuant to R865-6F-32.A.8 of the Utah Administrative Code ("regulation") and is "commercially domiciled" in Utah pursuant to regulation R865-6F-32.A.3. Other than the employees located in STATE, COMPANY does not have property (other than credit card holders or re- possessed property) or employees in any other state.

7. Neither 2ND COMPANYnor 4TH COMPANY is a "financial institution" pursuant to the above-referenced provision and do not, for Utah franchise tax purposes, have taxable nexus with Utah.

8. The Credit Card Income, Interchange Fees and Loan Interest are business income for purposes of regulation R865-6F-32.B.2.

9. COMPANY is filing income/ franchise tax returns in the following states: 3RD STATE, 8TH STATE, 4TH STATE, 2ND STATE, 5TH STATE and 6TH STATE.

10. 2ND COMPANY/ file income/ franchise tax returns in all jurisdictions except 7TH STATE, 9TH STATE, 10TH STATE and 11TH STATE.

II. ISSUE

For Utah corporation franchise tax apportionment purposes, what portion of COMPANY'S receipts from Credit Card Income, Interchange Fees and Loan Interest should be included in the numerator of Taxpayers' receipts factor (i.e., sourced to Utah)?

III. LAW AND ANALYSIS

In general, where a taxpayer engages in business in Utah and other states, there are allocation and apportionment rules that apply to the taxpayer's taxable income base. Code section 59-7-303(1) provides that taxpayers having income from business activities taxable both within and without Utah must allocate and apportion their income according to Title 59, Chapter 7, Part 3 of the Code. For this purpose, Code section 59-7-305(2) provides that a taxpayer is taxable in another

[12] It is understood that a few jurisdiction, such as 12TH STATE, impose taxes in SMLLCs that are disregarded.

state if "that state has jurisdiction to subject the taxpayer to a net income tax regardless of whether, in fact, the state does or does not."[13]

Taxable income is allocated or apportioned depending on the type of income involved. In this regard, taxable income is bifurcated between "business income" and "non-business income." Code section 59-7-302(1) provides that business income is "income arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, management, and disposition of the property constitutes integral parts of the taxpayer's regular trade or business operations." Code section 59-7 -302(4) provides that non-business income is all income other than business income.

In general, business income is subject to apportionment and non-business income is subject to a separate set of allocation rules.14 Code section 59-7-311 provides that business income must be apportioned to Utah by multiplying the income by a fraction, the numerator of which is the property factor plus the payroll factor plus the sales factor, and the denominator of which is three.15 For purposes of the apportionment formula, Code section 59-7-317 provides that the "sales factor" is a fraction, the numerator of which is the taxpayer's total sales in Utah, and the denominator of which is the taxpayer's total sales everywhere. In this context, Code section 59-7-302(5) provides that "sales" means all gross receipts of the taxpayer not allocated under Sections 59-7-306 through 59-7-310 (which apply to non-business income).

A taxpayer's gross receipts are sourced to Utah (or not) depending on the type of activity in which a taxpayer is engaged. Gross receipts for sales other than sales of tangible personal property (i.e., receipts for services performed) generally are sourced based on the "cost of performance" rule. Code section 59-7-319 provides that such receipts are sourced to Utah if the income-producing activity is performed in Utah, or the income-producing activity is performed both in and outside Utah and a greater proportion of the income-producing activity is performed in Utah than in any other state, based on costs of performance. Thus, under the cost of performance rule, a service provider that performed services with and without the State would source all of its gross receipts to Utah for apportionment purposes to the extent the greater portion of its income producing activities (based on cost) takes place in Utah.

There are, however, special allocation and apportionment rules for the financial services industry that apply in lieu of the foregoing general apportionment rules. Regulation R865-6F-32.B.1 provides that a financial institution (as defined in regulation R865-6F-32.A.8) whose business activity is "taxable" within and without Utah must allocate and apportion its net income as provided in regulation R865-6F-32.B. As with the general rule cited above, regulation R865-6F-32.A.20(b) provides that "taxable" means another state has the jurisdiction to subject the taxpayer to taxes regardless of whether the state actually imposes such taxes.

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[13] The term "state" includes any state of the United States and the District of Columbia. Code section 59-302(6).

[14] This ruling request is concerned with business income. Accordingly, the allocation of non-business income is not addressed.

[15] For tax years beginning on or after January 1, 2006, taxpayers may elect to double-weight the sales factor. See UT HB 78, section 1, which amends Code section 59-7-311 to provide for the election.

As with the general apportionment rules, regulation R865-6F-32.B.2 provides that business income of a financial institution is apportioned pursuant to a formula consisting of the same three factors cited above - receipts, property and payroll.[16] These factor rules, however, are specific to activities performed by financial service providers, several of which are relevant to this ruling request.

First, regulation R865-6F-32.C.7 provides that receipts from "credit card receivables," which include "interest and fees or penalties in the nature of interest from credit card receivables and receipts from fees charged to card holders, such as annual fees" are sourced to the billing address of the cardholder.[17] Thus, if a cardholder's billing address is not in Utah, the numerator of the receipts factor would not include the credit card receipts from such cardholder.

Second, regulation R865-6F-32.C.9 provides that "credit card issuer's reimbursement fees" are sourced to Utah by multiplying the amount of such fees by a fraction, the numerator and denominator of which are the same for those of credit card receivables set forth above. Pursuant to R865-6F-32.A.6, credit card issuer's reimbursement fees are the fees a taxpayer receives from a merchant bank because one of the persons to whom the taxpayer has issued a credit card has charged merchandise or services to the credit card.

Third, regulation R865-6F-32.C.5 provides that "interest from loans not secured by real property" includes interest and fees or penalties in the nature of interest from borrowers located in Utah. A "loan" for this purpose means any extension of credit resulting from direct negotiations between a taxpayer and its customer. Thus, as with credit card receivables, if a borrower's address is not in Utah, the numerator of the receipts factor would not include interest receipts from such borrower.

The foregoing rules do not necessarily apply to all members of a combined group of corporations. Regulation R865-6F-32.4 provides that where a unitary group of corporations filing a combined report consists of financial institutions and non-financial institutions, the special apportionment rules, described above, apply only to the financial institutions. The remainder of the corporations in the group (assuming they are not in another special industry) would use the general allocation and apportionment rules.

In summary, the apportionment rules generally permit a financial institution doing business within and without Utah to source receipts from credit card receivables, credit card issuer's reimbursement fees and interest from loans not secured by real property to the billing address of the credit card holders. There is, however, an exception to these "customer sourcing" rules where the financial institution is commercially domiciled in Utah but where it is not taxable in other states.

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[16] At the time of this writing, the Utah Tax Commission has not, to our knowledge, promulgated amended regulations to take into account the double-weighted sales factor election.

[17] For purposes of these rules, “credit card” means a credit, travel or entertainment card. Regulation R865-6F-32.A.5.

Regulation R865-6F-32.C.15(a) provides that "all receipts assigned... to a state in which the taxpayer is not taxable shall be included in the numerator of the receipts factor if the taxpayer's commercial domicile is in this state" (hereafter referred to as the "throwback rule").[18] For this purpose, regulation R865-6F-32.A.20 provides, in part, that "taxable" means "another state has the jurisdiction to subject the taxpayer to taxes regardless of whether that state actually imposes those taxes."

The regulations provide for two exceptions to the throwback rule. Presumably, these exceptions are intended to incorporate the "Finnigan" rule. As briefly discussed below, the *Finnigan* rule originated from a line of California cases that addressed the application of California's throwback rule in the context of a unitary group of corporations.

In *Appeal of Finnigan,*[19] two corporations, one with California nexus, one without, filed a unitary return. The corporation without nexus sold goods to customers located in states in which it was not subject to tax; however, the unitary affiliate was subject to tax in such states. At issue was whether California's throwback rule would apply since the selling corporation was not subject to tax in the destination states. The tax tribunal determined that the throwback rule would not apply because, although the seller was not subject to tax in the destination states, its unitary affiliate was taxable. The tribunal thus viewed the unitary group as one taxpayer for purposes of applying the throwback rule.

With the foregoing principal in mind, regulation R865-6F-32.C.15(b) provides the following two exceptions to the throwback rule:

> (1) If a unitary group includes one or more financial institutions, and if any member of the unitary group is subject to the taxing jurisdiction of this state, the receipts of each financial institution in the unitary group shall be included in the numerator of this state's receipts factor as provided in C.I. through C.14. [which include the customer sourcing rules noted above] rather than being attributed to the commercial domicile of the financial institution as provided in C.15.a).
>
> (2) If a unitary group includes one or more financial institutions whose commercial domicile is in this state, and if any member of the unitary group is taxable in another state under section 59-7-305, the receipts of each financial institution in the unitary group that would be included in the numerator of the other state's receipts factor under C.l. through C.l4. [which include the customer sourcing rules noted above] may not be included in the numerator of this state's receipts factor.

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[18] For this purpose, regulation section R865-6F-32.A.3 provides that "commercial domicile" means the principal place from which the trade or business of the taxpayer is directed or managed.

[19] Cal. State Bd. Of Equiliz., August 28,1988, Dkt. No. 88-SBE-022, *on reh'g,* Jan. 24,1990 (referred to as *Finnigan I* and *Finnigan II).* Cf. There also is the *Joyce* rule, which is another line of California cases that came to the opposite conclusion of *Finnigan* (i.e., a unitary affiliate that has nexus with a state will not impact a selling corporation that does not have nexus).

The first exception (1) presumably is directed at a financial institution within a Utah unitary group that is commercially domiciled outside of Utah (it would not otherwise make sense, when read in the context of the second exception). Employing the *Finnigan* principle, it provides that even though a non-commercially domiciled financial institution does not have nexus with Utah, as long as a unitary affiliate does, such financial institution may not throw its receipts back to its commercial domicile; rather, it should continue to source based on the regular sourcing rules (which include customer sourcing in Cl. to C.l4.). This ensures, for example, that if the financial institution had credit card holders residing in Utah, income earned from such persons would be included in the unitary group's Utah numerator.

The second exception (2), which is directed at a financial institution that is commercially domiciled in Utah, virtually encapsulates the basic facts and premise of *Finnigan.* It provides that, to the extent a unitary affiliate (of a financial institution that is commercially domiciled in Utah) is "taxable" in another state, the throwback rule does not apply to such financial institution. Code section 59-7-305 provides that a taxpayer is taxable in another state if "that state has jurisdiction to subject the taxpayer to a net income tax regardless of whether, in fact, the state does or does not."

It is the second exception that is applicable for purposes of this ruling request. In this regard, the throwback rule would not apply to a financial institution that is commercially domiciled in Utah where, at least, a unitary affiliate is registered to do business in every state (and, thus, "taxable" in other states and, where necessary, filing tax returns in such states)20 and where the financial institution has credit card holders in every state. Accordingly, such financial institution would be subject to the receipts sourcing rules contained in regulation section R865-6F-32.C.l. through C.l4, which include customer sourcing for credit card receivables, interchange fees and interest from loans not secured by real property.

IV. RULING REQUEST£D

COMPANY and 2ND COMPANY file a Unitary return for Utah corporate franchise tax purposes (collectively referred to as "Taxpayers"). Based on the foregoing, Taxpayers' income would be subject to apportionment because they are doing business within and without Utah. The apportionment rules applicable to financial institutions would apply to Taxpayers because COMPANY is a financial institution that is commercially domiciled in Utah within the meaning of regulation section R865-6F-32.A.8 and R865-6F-32.A.3. For this purpose, the Credit Card income earned by COMPANY is a "credit card receivable" because such income consists of interest and penalties and fees from credit cards issued by COMPANY; the Interchange Fee is a "credit card issuer's reimbursement fee" because it is a fee earned by COMPANY with respect to charges made by its cardholders to merchants who contract with other banks for reimbursements; and the Loan Interest is "interest from loans not secured by real property." Utah's throwback rule does not apply to Taxpayers because, in the aggregate, COMPANY is "taxable" in those

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[20] The vast majority of the states require taxpayers that are merely registered to do business in such states to file a return.

states in which cardholders reside (in addition to the states, listed in the Assumptions) and 2ND COMPANY/4TH COMPANY, its unitary affiliate, is "taxable" in all states in which it is registered both as a debt collector and to do business and in which its files income/ franchise/ other tax returns (as set forth in the Assumptions.)

Accordingly:

1. Only Credit Card Income collected from cardholders with billing addresses in Utah must be included in the numerator of Taxpayers' receipts factor;

2. Only *a Pro rata* portion of Interchange Fees, based on a ratio of Taxpayers" Credit Card Income sourced to Utah over Taxpayers' total Credit Card Income, must be included in the numerator of Taxpayers' receipts factor; and

3. Only Loan Interest received from borrowers located in Utah must be included in the numerator of Taxpayers' receipts factor.

RESPONSE LETTER

January 26, 2007

NAME
ADDRESS

RE: Application of Corporate Franchise Tax Apportionment

Dear NAME,

We are in receipt of your request for a ruling as to the application of Utah's corporate franchise tax apportionment rules to your client, COMPANY. Based on the information you provided, and as discussed in greater detail below, we understand COMPANY is an incorporated financial services business doing business in Utah, and having several employees in 2ND STATE. The financial services business is a subsidiary of a parent company, 2ND COMPANY. COMPANY issues credit cards to individuals residing in the fifty states and the District of Columbia. It derives income from three sources: interest and fees; interchange fees; and, interest from installment loans.

The parent company, 2ND COMPANY, does business in multiple states. It services the credit cards issued by COMPANY and unrelated third parties. Because it collects debts in all fifty states, it is registered to do business in all fifty states. It also files tax returns in many of those states.

Both are corporations for federal income and Utah corporate franchise tax purposes. They are members of a unitary group under Title 59, Chapter 7 of the Utah Code Annotated. The subsidiary is a financial institution under R865-6F-32 (A)(8). It is "commercially domiciled" in Utah under R865-6F-32 (A)(3). 2ND COMPANY is not a financial institution under those provisions and you have represented it does not have taxable nexus to Utah for franchise tax purposes.

We have reviewed your request for a specific ruling regarding certain provisions of Utah Administrative Rule R865-6F-32. These provisions deal with whether certain income should be "thrown back" to Utah as Commercial Domicile within the context of a unitary business and applying Utah rule provisions similar to 'Finnigan'. The Finnigan approach to determining tax liability in Utah is based on whether any member of the unitary group of the corporation has a sufficient nexus with Utah.

As you noted, there were two Finnigan decisions. The issue in Finnigan I was application

of the throw back rule. As explained in Finnigan I, the general rule is that sales of tangible personal property are assigned to the state of destination of the goods for purposes of the sales factor of the apportionment formula. The throw back rule applies when property is shipped from State "A" to State "B" and the taxpayer is not taxable in State "B." The result in Finnigan I was that the affiliate's sales to foreign states were not thrown back to California because a member of the unitary group was taxable in the foreign state.

We understand the essence of your question to be whether the 'Finnigan' language within the Utah Financial Institutions Rule serves to negate the throwback provisions within the same rule based upon a factual determination in the scenario you have outlined, that either (i) CardWorks has nexus in every state by virtue of having to register as a debt collector in all 50 states, or (ii) COMPANY has nexus in every state because it has credit card holders that exceed a *de minimis* level in every state.

We agree with your conclusion that receipts from credit card income, interchange fees and loan interest from loans not secured by real property, to the extent the cardholders address or borrower is not in Utah, is not required to be thrown back if any member of the unitary group is taxable in each of the states to which such receipts would otherwise be assigned under applicable Utah administrative rules.

Therefore, it is necessary to examine the facts associated with both 2ND COMPANY and COMPANY in order to make a determination as to whether under the facts presented, nexus would be created in all states. You have indicated that 2ND COMPANY as a debt collector is required to register in all 50 states. However, a corporation that is merely registered to do business in a state cannot be subjected to a state income or franchise tax (other than a minimum tax) if its activities either do not exceed the limitations of Public Law 86-272 or constitutional requirements governing those activities performed by a corporation that give a state the right to impose its tax. Therefore, the mere registration to do business in a state by the parent corporation may not create nexus unless 2ND COMPANY engages in business activities in every state that exceed the above thresholds.

You indicate that COMPANY is a financial institution with credit card holders in every state ranging from 1,200 to 110,000 cardholders. It is clear that COMPANY is targeting the market of every state and is therefore 'doing business' or 'deriving income' from within every state. Since the number of credit card holders in the state where the least amount of operations conducted is 1,200, a level we would consider beyond *de minimis*, we conclude that COMPANY is conducting business in every state. Because COMPANY is doing business in every state, no throwback to Utah as commercial domicile is required for interest and fees from credit card operations or interest from loans not secured by real property. Since Interchange Fees are sourced using the ratio of credit card income in Utah to credit card income everywhere, such fees would likewise not be required to be thrown back.

This decision is based on your representations that COMPANY is actually taxable in

every state in which it has credit card holders. To the extent that another state's law concludes that the presence of cardholders in that state is not sufficient to make COMPANY'S income subject to tax, however, the throwback rule could apply. See, e.g., *J.C. Penney National Bank v. Johnson*, 19 S.W.3d 831, 840 (Tenn. Ct. App. 1999), holding that an out-of-state bank was not "taxable" in Tennessee, even though it had between 11,000 and 17,000 cardholders in that state. Thus, if COMPANY were to take the position that it is not "taxable" in any particular state under such reasoning, we would expect the receipts from that state to be thrown back to Utah.

We therefore, agree with the three conclusions listed in your summary based on the facts presented in your ruling request as follows:

1. Only credit card income collected from cardholders with billing addresses in Utah must be included in the numerator of taxpayer's receipts factor;

2. Only a portion of interchange fees, based on a ratio of taxpayers' total credit card income, must be included in the numerator of taxpayers' receipts factor; and

3. Only loan interest received from borrowers located in Utah must be included in the numerator of the taxpayers' receipts factor.

Should the facts be different from those represented in this letter, or if 2ND COMPANY or COMPANY was to take a filing position in any other state that it was not "taxable" in that state, our opinion may change accordingly. Thank you for your inquiry into this matter.

For the Commission,

Marc Johnson
Commissioner

MBJ/SR
06-027