

BEFORE THE DEPARTMENT OF REVENUE
OF THE STATE OF MONTANA

In the matter of the adoption of New) NOTICE OF PUBLIC HEARING ON
Rules I through III pertaining to) PROPOSED ADOPTION
apportionment and allocation of)
income for financial institutions)

TO: All Concerned Persons

1. On November 2, 2017, at 9 a.m., the Department of Revenue will hold a public hearing in the Third Floor Reception Conference Room of the Sam W. Mitchell Building, located at 125 North Roberts, Helena, Montana, to consider the proposed adoption of the above-stated rules. The hearing room is most readily accessed by entering through the east doors of the building facing Sanders Street.

2. The Department of Revenue will make reasonable accommodations for persons with disabilities who wish to participate in this public hearing or need an alternative accessible format of this notice. If you require an accommodation, contact the department no later than 5 p.m. on October 23, 2017, to advise us of the nature of the accommodation you need. Please contact Laurie Logan, Department of Revenue, Director's Office, P.O. Box 7701, Helena, Montana 59604-7701; telephone (406) 444-7905; fax (406) 444-3696; or e-mail lalogan@mt.gov.

3. The rules as proposed to be adopted provide as follows:

NEW RULE I DEFINITIONS The following definitions apply to terms used in this subchapter.

(1) "Billing address" means the location indicated in the books and records of the taxpayer on the first day of the taxable year, or on such later date in the taxable year when the customer relationship began, as the address where any notice, statement, and/or bill relating to a customer's account is mailed.

(2) "Borrower or credit card holder located in this state" means:

(a) a borrower, other than a credit card holder, that is engaged in a trade or business which maintains its commercial domicile in Montana; or

(b) a borrower that is not engaged in a trade or business or a credit card holder whose billing address is in Montana.

(3) "Card issuer's reimbursement fee" means the fee a taxpayer receives from a merchant's bank because one of the persons to whom the taxpayer has issued a credit, debit, or similar type of card has charged merchandise or services to the card.

(4) "Commercial domicile" means:

(a) the headquarters of the trade or business, that is, the place from which the trade or business is principally managed and directed; or

(b) if a taxpayer is organized under the laws of a foreign country, or of the Commonwealth of Puerto Rico, or any territory or possession of the United States, such taxpayer's commercial domicile shall be deemed for the purposes of the rules

in ARM Title 42, chapter 26, [subchapter 13] to be the state of the United States or the District of Columbia from which such taxpayer's trade or business in the United States is principally managed and directed. It shall be presumed, subject to rebuttal, that the location from which the taxpayer's trade or business is principally managed and directed is the state of the United States or the District of Columbia to which the greatest number of employees are regularly connected or out of which they are working, irrespective of where the services of such employees are performed, as of the last day of the taxable year.

(5) "Credit card" means a card, or other means of providing information, that entitles the holder to charge the cost of purchases, or a cash advance, against a line of credit.

(6) "Debit card" means a card, or other means of providing information, that enables the holder to charge the cost of purchases, or a cash withdrawal, against the holder's bank account or a remaining balance on the card.

(7) "Employee" means, with respect to a particular taxpayer, any individual who, under the usual common-law rules applicable in determining the employer-employee relationship, has the status of an employee of that taxpayer.

(8) "Financial institution" means:

(a) any corporation or other business entity registered under state law as a bank holding company or registered under the Federal Bank Holding Company Act of 1956, as amended, or registered as a savings and loan holding company under the Federal National Housing Act, as amended;

(b) a national bank organized and existing as a national bank association pursuant to the provisions of the National Bank Act, 12 U.S.C. sections 21 et seq.;

(c) a savings association or federal savings bank as defined in the Federal Deposit Insurance Act, 12 U.S.C. section 1813(b)(1);

(d) any bank or thrift institution incorporated or organized under the laws of any state;

(e) any corporation organized under the provisions of 12 U.S.C. sections 611 through 631;

(f) any agency or branch of a foreign depository as defined in 12 U.S.C. section 3101;

(g) a state credit union the loan assets of which exceed \$50,000,000 as of the first day of its taxable year;

(h) a production credit association organized under the Federal Farm Credit Act of 1933, all of whose stock held by the Federal Production Credit Corporation has been retired;

(i) any corporation whose voting stock is more than fifty percent owned, directly or indirectly, by any person or business entity described in subsections (a) through (h) above other than an insurance company;

(j) a corporation or other business entity that derives more than fifty percent of its total gross income for financial accounting purposes from finance leases. For purposes of the rules in ARM Title 42, chapter 26, [subchapter 13], a "finance lease" shall mean any lease transaction which is the functional equivalent of an extension of credit and that transfers substantially all of the benefits and risks incident to the ownership of property. The phrase shall include any "direct financing lease" or "leverage lease" that meets the criteria of Financial Accounting Standards Board

Statement No. 13, "Accounting for Leases," or any other lease that is accounted for as a financing by a lessor under generally accepted accounting principles. For this classification to apply:

(i) the average of the gross income in the current tax year and immediately preceding two tax years must satisfy the more than fifty percent requirement; and

(ii) gross income from incidental or occasional transactions shall be disregarded; or

(k) any other person or business entity, other than an insurance company, a real estate broker, or a securities dealer which derives more than fifty percent of its gross income from activities that a person described in (b) and (h) through (j) above.

(9) "Loan" means any extension of credit resulting from direct negotiations between the taxpayer and its customers, and/or the purchase, in whole or in part, of such extension of credit from another. Loans include participations, syndications, and leases treated as loans for federal income tax purposes. Loans shall not include: futures or forward contracts; options; notional principal contracts such as swaps; credit card receivables, including purchased credit card relationships; non-interest bearing balances due from depository institutions; cash items in the process of collection; federal funds sold; securities purchased under agreements to resell; assets held in a trading account; securities; interests in a REMIC, or other mortgage backed or asset backed security; and other similar items.

(10) "Loan secured by real property" means that fifty percent or more of the aggregate value of the collateral used to secure a loan or other obligation, when valued at fair market value as of the time the original loan or obligation was incurred, was real property.

(11) "Merchant discount" means the fee (or negotiated discount) charged to a merchant by the taxpayer for the privilege of participating in a program whereby a credit, debit, or similar type of card is accepted in payment for merchandise or services sold to the card holder, net of any card holder charge-back and unreduced by any interchange transaction or issuer reimbursement fee paid to another for charges or purchases made by its card holder.

(12) "Participation" means an extension of credit in which an undivided ownership interest is held on a pro rata basis in a single loan or pool of loans and related collateral. In a loan participation, the credit originator initially makes the loan and then subsequently resells all or a portion of it to other lenders. The participation may or may not be known to the borrower.

(13) "Person" means an individual, estate, trust, partnership, corporation, or any other business entity.

(14) "Principal base of operation" with respect to transportation property means the place of more or less permanent nature from which said property is regularly directed or controlled. With respect to an employee, the "principal base of operations" means the place of more or less permanent nature from which the employee regularly starts his or her work and to which he or she customarily returns in order to receive instructions from his or her employer; or communicates with his or her customers or other persons; or performs any other functions necessary to the exercise of his or her trade or profession at some other point or points.

(15) "Regular place of business" means an office at which the taxpayer carries on its business in a regular and systematic manner and which is continuously maintained, occupied, and used by employees of the taxpayer.

(16) "State" means a state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, any territory or possession of the United States, or any foreign country.

(17) "Syndication" means an extension of credit in which two or more persons fund and each person is at risk only up to a specified percentage of the total extension of credit or up to a specified dollar amount.

(18) "Transportation property" means vehicles and vessels capable of moving under their own power, such as aircraft, trains, water vessels, and motor vehicles, as well as any equipment or containers attached to such property, such as rolling stock, barges, trailers, or the like.

AUTH: 15-1-201, 15-1-313, MCA

IMP: 15-1-601, 15-31-301, 15-31-302, 15-31-303, 15-31-304, 15-31-305, 15-31-306, 15-31-307, 15-31-308, 15-31-309, 15-31-310, 15-31-311, 15-31-312, MCA

REASON: The department proposes adopting New Rule I to define terms that are used in New Rule III, which is also proposed for adoption in this same notice. The three rules being proposed in this notice will be placed in a new subchapter 13 of ARM Title 42, chapter 26, "Corporate Multistate Activities." As proposed, this new definition rule will aid taxpayers in the application of New Rule III, "Receipts Factor."

New Rule I and the other two rules being proposed for adoption in this notice are modeled after regulations adopted by the Multistate Tax Commission. The proposed new rules are intended to more fairly apportion the receipts of financial institutions to states in which they do business.

NEW RULE II APPORTIONMENT AND ALLOCATION (1) Except as specifically modified by the administrative rules in this subchapter, a financial institution whose business activity is taxable both within and without Montana shall allocate and apportion its net income as provided in Title 15, chapter 31, part 3, MCA, and the supporting administrative rules located in ARM Title 42, chapter 26.

AUTH: 15-1-201, 15-1-313, MCA

IMP: 15-1-601, 15-31-301, 15-31-302, 15-31-303, 15-31-304, 15-31-305, 15-31-306, 15-31-307, 15-31-308, 15-31-309, 15-31-310, 15-31-311, 15-31-312, MCA

REASON: The department proposes adopting New Rule II to provide specific direction to financial institutions for including specific types of receipts in the numerator of the receipts apportionment factor. As proposed, New Rule II directs taxpayers to Title 15, chapter 31, part 3, MCA, and the supporting administrative rules in ARM Title 42, chapter 26, for apportionment and allocation issues not specifically addressed in this subchapter.

New Rule II and the other two rules being proposed for adoption in this notice are modeled after regulations adopted by the Multistate Tax Commission. The

proposed new rules are intended to more fairly apportion the receipts of financial institutions to states in which they do business.

NEW RULE III RECEIPTS FACTOR (1) The receipts factor is a fraction, the numerator of which is the receipts of the taxpayer in Montana during the taxable year and the denominator of which is the receipts of the taxpayer within and without Montana during the taxable year. The method of calculating receipts for purposes of the denominator is the same as the method used in determining receipts for purposes of the numerator. The receipts factor shall include only those receipts described herein which constitute apportionable income and are included in the computation of the apportionable income base for the taxable year.

(2) Interest, fees, and penalties imposed in connection with loans secured by real property.

(a) The numerator of the receipts factor includes interest, fees, and penalties imposed in connection with loans secured by real property if the property is located within Montana. If the property is located both within Montana and one or more other states, the receipts described in this subsection are included in the numerator of the receipts factor if more than fifty percent of the fair market value of the real property is located within Montana. If more than fifty percent of the fair market value of the real property is not located within any one state, then the receipts described in this subsection shall be included in the numerator of the receipts factor if the borrower is located in Montana.

(b) The determination of whether the real property securing a loan is located within Montana shall be made as of the time the original agreement was made and any and all subsequent substitutions of collateral shall be disregarded.

(3) Interest, fees, and penalties imposed in connection with loans not secured by real property. The numerator of the receipts factor includes interest, fees, and penalties imposed in connection with loans not secured by real property if the borrower is located in Montana.

(4) Net gains from the sale of loans. The numerator of the receipts factor includes net gains from the sale of loans. Net gains from the sale of loans includes income recorded under the coupon stripping rules of Section 1286 of the Internal Revenue Code.

(a) The amount of net gains (but not less than zero) from the sale of loans secured by real property included in the numerator is determined by multiplying such net gains by a fraction the numerator of which is the amount included in the numerator of the receipts factor pursuant to (2) above, and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans secured by real property.

(b) The amount of net gains (but not less than zero) from the sale of loans not secured by real property included in the numerator is determined by multiplying such net gains by a fraction the numerator of which is the amount included in the numerator of the receipts factor pursuant to (5) below, and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans not secured by real property.

(5) Receipts from fees, interest, and penalties charged to card holders. The numerator of the receipts factor includes fees, interest, and penalties charged to

credit, debit, or similar card holders, including but not limited to annual fees and overdraft fees, if the billing address of the card holder is in Montana.

(6) Net gains from the sale of credit card receivables. The numerator of the receipts factor includes net gains (but not less than zero) from the sale of credit card receivables multiplied by a fraction, the numerator of which is the amount included in the numerator of the receipts factor pursuant to (5) above, and the denominator of which is the taxpayer's total amount of interest and fees or penalties in the nature of interest from credit card receivables and fees charged to card holders.

(7) Card issuer's reimbursement fees. The numerator of the receipts factor includes:

(a) All credit card issuer's reimbursement fees multiplied by a fraction, the numerator of which is the amount of fees, interest, and penalties charged to credit card holders included in the numerator of the receipts factor pursuant to (5) above, and the denominator of which is the taxpayer's total amount of fees, interest, and penalties charged to credit card holders.

(b) All debit card issuer's reimbursement fees multiplied by a fraction, the numerator of which is the amount of fees, interest, and penalties charged to debit card holders included in the numerator of the receipts factor pursuant to (5) above, and the denominator of which is the taxpayer's total amount of fees, interest, and penalties charged to debit card holders.

(c) All other card issuer's reimbursement fees multiplied by a fraction, the numerator of which is the amount of fees, interest, and penalties charged to all other card holders included in the numerator of the receipts factor pursuant to (5) above, and the denominator of which is the taxpayer's total amount of fees, interest, and penalties charged to all other card holders.

(8) Receipts from merchant discount.

(a) If the taxpayer can readily determine the location of the merchant and if the merchant is in Montana, the numerator of the receipts factor includes receipts from the merchant discount.

(b) If the taxpayer cannot readily determine the location of the merchant, the numerator of the receipts factor includes such receipts from the merchant discount multiplied by a fraction:

(i) in the case of a merchant discount related to the use of a credit card, the numerator of which is the amount of fees, interest, and penalties charged to credit card holders that is included in the numerator of the receipts factor pursuant to (5) above, and the denominator of which is the taxpayer's total amount of fees, interest, and penalties charged to credit card holders; and

(ii) in the case of a merchant discount related to the use of a debit card, the numerator of which is the amount of fees, interest, and penalties charged to debit card holders that is included in the numerator of the receipts factor pursuant to (5) above, and the denominator of which is the taxpayer's total amount of fees, interest, and penalties charged to debit card holders.

(c) The taxpayer's method for sourcing each receipt from a merchant discount must be consistently applied to such receipt in all states that have adopted sourcing methods substantially similar to (a) and (b) above, and must be used on all subsequent return for sourcing receipts from such merchant unless the department permits or requires application of the alternative method.

(9) Receipts from ATM fees. The receipts factor includes all ATM fees that are not forwarded directly to another bank.

(a) The numerator of the receipts factor includes fees charged to a card holder for the use at an ATM of a card issued by the taxpayer if the card holder's billing address is in Montana.

(b) The numerator of the receipts factor includes fees charged to a card holder, other than the taxpayer's card holder, for the use of such card at an ATM owned or rented by the taxpayer, if the ATM is in Montana.

(10) Loan servicing fees.

(a) The numerator of the receipts factor includes loan servicing fees derived from loans secured by real property multiplied by a fraction the numerator of which is the amount included in the numerator of the receipts factor pursuant to (2) above, and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans secured by real property.

(b) The numerator of the receipts factor includes loan servicing fees derived from loans not secured by real property multiplied by a fraction the numerator of which is the amount included in the numerator of the receipts factor pursuant to (3) above, and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans not secured by real property.

(c) In circumstances in which the taxpayer receives loan servicing fees for servicing either the secured or the unsecured loans of another, the numerator of the receipts factor shall include such fees if the borrower is located in Montana.

(11) Receipts from the financial institution's investment assets and activity and trading assets and activity.

(a) Interest, dividends, net gains (but not less than zero), and other income from investment assets and activities and from trading assets and activities that are reported on the taxpayer's financial statements, call reports, or similar reports shall be included in the receipts factor. Investment assets and activities and trading assets and activities include but are not limited to: investment securities; trading account assets; federal funds; securities purchased and sold under agreements to resell or repurchase; options; futures contracts; forward contracts; notional principal contracts such as swaps; equities; and foreign currency transactions. With respect to the investment and trading assets and activities described in (i) and (ii) below, the receipts factor shall include the amounts described.

(i) The receipts factor shall include the amount by which interest from federal funds sold and securities purchased under resale agreements exceeds interest expense on federal funds purchased and securities sold under repurchase agreements.

(ii) The receipts factor shall include the amount by which interest, dividends, gains, and other income from trading assets and activities, including but not limited to assets and activities in the matched book, in the arbitrage book, and foreign currency transactions, exceed amounts paid in lieu of interest, amounts paid in lieu of dividends, and losses from such assets and activities.

(b) The numerator of the receipts factor includes interest, dividends, net gains (but not less than zero), and other income from investment assets and activities and from trading assets and activities described in (a) above, that are attributable to Montana.

(i) The amount of interest, dividends, net gains (but not less than zero), and other income from investment assets and activities in the investment account to be attributed to Montana and included in the numerator is determined by multiplying all such income from such assets and activities by a fraction, the numerator of which is the average value of such assets which are properly assigned to a regular place of business of the taxpayer within Montana, and the denominator of which is the average value of all such assets.

(ii) The amount of interest from federal funds sold and purchased and from securities purchased under resale agreements and securities sold under repurchase agreements attributable to Montana and included in the numerator is determined by multiplying the amount described in (a)(i) above, from such funds and such securities by a fraction, the numerator of which is the average value of federal funds sold and securities purchased under agreements to resell which are properly assigned to a regular place of business of the taxpayer within Montana and the denominator of which is the average value of all such funds and such securities.

(iii) The amount of interest, dividends, gains, and other income from trading assets and activities, including but not limited to assets and activities in the matched book, in the arbitrage book, and foreign currency transactions (but excluding amounts described in (i) and (ii) above, attributable to Montana and included in the numerator is determined by multiplying the amount described in (a)(ii) above, by a fraction, the numerator of which is the average value of such trading assets which are properly assigned to a regular place of business of the taxpayer within Montana and the denominator of which is the average value of all such assets.

(iv) For purposes of this section, average value shall be determined using the rules for determining the average value of tangible personal property set forth in 15-31-307, MCA.

(c) In lieu of using the method set forth in (b) above, the taxpayer may elect, or the department may require in order to fairly represent the business activity of the taxpayer in Montana, the use of the method set forth in this subsection.

(i) The amount of interest, dividends, net gains (but not less than zero), and other income from investment assets and activities in the investment account to be attributed to Montana and included in the numerator is determined by multiplying all such income from such assets and activities by a fraction, the numerator of which is the gross income from such assets and activities which are properly assigned to a regular place of business of the taxpayer within Montana and denominator of which is the gross income from all such assets and activities.

(ii) The amount of interest from federal funds sold and purchased and from securities purchased under resale agreements and securities sold under repurchase agreements attributable to Montana and included in the numerator is determined by multiplying the amount described in (a)(i) above, from such funds and such securities by a fraction, the numerator of which is the gross income from such funds and such securities which are properly assigned to a regular place of business of the taxpayer within Montana and denominator of which is the gross income from all such funds and such securities.

(iii) The amount of interest, dividends, gains, and other income from trading assets and activities, including but not limited to assets and activities in the matched book, in the arbitrage book, and foreign currency transactions (but excluding

amounts described in (c)(i) and (c)(ii) above), attributable to Montana and included in the numerator is determined by multiplying the amount described in (a)(ii) by a fraction, the numerator of which is the gross income from such trading assets and activities which are properly assigned to a regular place of business of the taxpayer within Montana and the denominator of which is the gross income from all such assets and activities.

(d) If the taxpayer elects or is required by the department to use the method set forth in subsection (c) above, it shall use this method on all subsequent returns unless the taxpayer receives prior permission from the department to use, or the department requires, a different method.

(e) The taxpayer shall have the burden of proving that an investment asset or activity or trading asset activity was properly assigned to a regular place of business outside of Montana by demonstrating that the day-to-day decisions regarding the asset or activity occurred at a regular place of business outside Montana. Where the day-to-day decisions regarding an investment asset or activity or trading asset or activity occur at more than one regular place of business and one such regular place of business is in Montana and one such regular place of business is outside Montana, such asset or activity shall be considered to be located at the regular place of business of the taxpayer where the investment or trading policies or guidelines with respect to the asset or activity are established. Unless the taxpayer demonstrates to the contrary, such policies and guidelines shall be presumed to be established at the commercial domicile of the taxpayer.

(12) Attribution of certain receipts to commercial domicile. All receipts which would be assigned under this rule 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 Montana.

AUTH: 15-1-201, 15-1-313, MCA

IMP: 15-1-601, 15-31-301, 15-31-302, 15-31-303, 15-31-304, 15-31-305, 15-31-310, 15-31-311, 15-31-312, MCA

REASON: The department proposes adopting New Rule III to provide specific direction to financial institutions for including specific types of receipts in the numerator of the receipts apportionment factor. As proposed, New Rule III addresses specific types of receipts and how those receipts are assigned to the Montana receipts factor numerator for financial institutions.

New Rule III and the other two rules being proposed for adoption in this notice are modeled after regulations adopted by the Multistate Tax Commission. The proposed new rules are intended to more fairly apportion the receipts of financial institutions to states in which they do business.

4. Concerned persons may submit their data, views, or arguments, either orally or in writing, at the hearing. Written data, views, or arguments may also be submitted to: Laurie Logan, Department of Revenue, Director's Office, P.O. Box 7701, Helena, Montana 59604-7701; telephone (406) 444-7905; fax (406) 444-3696; or e-mail lalogan@mt.gov and must be received no later than November 13, 2017.

5. Laurie Logan, Department of Revenue, Director's Office, has been designated to preside over and conduct this hearing.

6. The Department of Revenue maintains a list of interested persons who wish to receive notices of rulemaking actions proposed by this agency. Persons who wish to have their name added to the list shall make a written request that includes the name and e-mail or mailing address of the person to receive notices and specifies that the person wishes to receive notice regarding a particular subject matter or matters. Notices will be sent by e-mail unless a mailing preference is noted in the request. A written request may be mailed or delivered to the person in 4 above or faxed to the office at (406) 444-3696, or may be made by completing a request form at any rules hearing held by the Department of Revenue.

7. An electronic copy of this notice is available on the department's web site at revenue.mt.gov/rules, or through the Secretary of State's web site at sos.mt.gov/ARM/register.

8. The bill sponsor contact requirements of 2-4-302, MCA, do not apply.

9. With regard to the requirements of 2-4-111, MCA, the department has determined that the adoption of the above-referenced rules will not significantly and directly impact small businesses. Documentation of the department's determination is available at revenue.mt.gov/rules or upon request from the person in 4.

/s/ Laurie Logan
Laurie Logan
Rule Reviewer

/s/ Mike Kadas
Mike Kadas
Director of Revenue

Certified to the Secretary of State October 2, 2017.