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The Honorable Ginny Burdick
Chairwoman, Committee on Revenue
Oregon State Senate
900 East Court St.
Salem, OR 97301

Dear Chairwoman Burdick:

We sincerely appreciate an opportunity to respond to the document that was prepared for you by the Oregon Department of Revenue (DOR) regarding the testimony of Brian O'Leary, Senior Vice President and tax Counsel for NBC Universal, on February 24, 2014 before your Committee. The DOR's description of the apportionment rules for broadcasters in other states, particularly in North Carolina, Florida, Michigan and Illinois, is incomplete and does not accurately describe all of the relevant rules adopted in the four referenced states.

At the outset, I would like to note that in each of the four states, the rules adopted were designed to address a genuine lack of clarity with respect to the application of the general apportionment rules to the unique circumstances of national broadcasters in those jurisdictions. This lack of clarity was fully resolved in all instances with the legislation enacted or the administrative guidance issued.

It is also worth noting that of the limited number of states that did adopt the viewing audience method for broadcasters, not a single state has adopted this method in the past ten years.[1]

[1] On the chart of 19 states included in the DOR submission to you, the audience rule: (1) in Florida is narrowly limited to certain types of broadcasters, (2) in Illinois, the rule applies to the television program distributors (e.g., cable operating systems), but it does not apply to free broadcast networks and cable program networks, (3) in Louisiana, the method only applies in certain narrow circumstances and was adopted by the State as a way to settle and resolve 10-15 years of industry litigation, (4) in Michigan, the Oregon DOR misinterpreted the application of

With respect to the DOR's analysis of the four states referenced by Mr. O'Leary during his testimony, attached please find an accurate description of why the statute or administrative guidance was adopted and how the apportionment method works.

Once again, we thank you for the opportunity to provide you with this information and would be pleased to answer any questions you may have.

Very truly yours,

Attachment

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the rule which is fundamentally a commercial domicile rather than a viewing audience rule, (5) in New Jersey, the rule was superseded by agreement between the Revenue Department and industry as part of a voluntary disclosure program, (6) in Washington, the State never had a viewing audience rule and the rule reflected in the citation provided by the DOR expired in 2011. Thus, of the 13 states identified by the DOR with an audience method in its chart and taking into account all of the above information, there are only a very limited number of states – less than half a dozen – that continue to cling to this archaic rule.

NORTH CAROLINA

The North Carolina Department of Revenue (NC DOR) issued administrative guidance to the MPAA members who own and operate all of the free broadcast networks and almost all of the cable programming networks in existence today. The industry had sought this guidance given the uncertainty in how the NC DOR would apply its general sales factor apportionment rules to license fees (i.e., fees received by broadcasters from granting others the right to distribute television programming). The NC DOR also elected to address the second stream of revenues earned by broadcasters in the same guidance, viz., advertising revenues.

With respect to license fees, North Carolina requires income from intangibles to be attributed to the State "if received from sources in the State". The NC DOR concluded in the guidance (referenced in the Oregon DOR's submission to Chairwoman Burdick) that license fees earned by broadcasters are sourced to North Carolina if the license fees are received pursuant to a contract approved by the executive management of the licensee or other party (i.e., the payor) in North Carolina. Contrary to the assertion of the Oregon DOR, the method indicated in the North Carolina ruling is tantamount or essentially identical to the commercial domicile rule included in HB 4138. This is because in our industry television programming distribution agreements require a substantial commitment of fees to be paid by licensees and the executive management of the licensees typically approves and executes these agreements at their corporate headquarters which is the commercial domicile for each. Therefore, the commercial domicile rule in HB 4138 is in fact the same apportionment rule that North Carolina requires broadcasters to follow.

Unlike license fees, advertising revenues in North Carolina are governed by the statutory rule for apportioning income from services. A national broadcaster's advertising revenues are sourced to the North Carolina only if the income-producing activities that give rise to the advertising receipts (i.e., the solicitation, negotiation and execution of the advertising services agreements) are performed by the broadcaster in North Carolina. The application of a commercial domicile rule was not necessary for advertising receipts because the general statutory apportionment rule for income from services looked to where the income-producing activities of the broadcaster occurred.

FLORIDA

To date, the State has issued two identical rulings on this issue dealing with the sourcing for license fees and advertising receipts for the cable program network industry. Those rulings require a cable program network to apportion broadcast revenues to Florida only if the principal place from which the business of its customers (program distributors such as cable operating systems and advertisers) is managed or directed is within Florida. The principal place from which a business is managed and controlled in both Florida and Oregon is its commercial domicile. While technically applicable only to the two taxpayers to which the rulings were issued, in practice any taxpayer in the cable program network industry has the same set of facts and the guidance in the two rulings will apply.

In August of 2011, a member of the MPAA approached the state of Florida to obtain guidance on how a cable television network that produces television shows and provides programming to cable distributors (e.g., Comcast, Direct TV, etc.) should source its income for Florida purposes. Whereas the State had previously issued guidance for "broadcasting" approximately 20 years ago, it had not specifically addressed the cable television network industry, therefore the taxpayer's request was to clarify the Department's treatment of this particular industry.

The MPAA member specifically requested clarification regarding its license fees from cable distributors (described in the ruling as subscription/affiliate receipts) and its advertising receipts. In response to the request, Florida issued Technical Assistance Advisement 11(C) 1-008. In the TAA, Florida concluded that license fees earned from Distributors (e.g., Comcast, Direct TV, etc.,) will constitute a Florida sale when the Distributor's principal place from which the business is managed or directed is within Florida. Likewise, advertising revenue earned by the Taxpayer will be sourced to Florida when the Advertiser's principal place from which the business is managed or directed is within Florida. Florida's position to source subscription and advertising revenue (i.e., license fees) based on the principal place from which a business is managed or directed conforms with Oregon's definition of "Commercial Domicile" (ORS 314.610(2)). Further, this apportionment methodology is the same as House Bill 4138.

Florida issued an identical ruling (Technical Assistance Advisement13(C)1-004) in May of 2013 that concluded that both subscription/affiliate receipts and advertising receipts earned from customers will constitute a Florida sale when the Taxpayer's customer's principal place from which the business is managed or directed is within Florida.

MICHIGAN

The Oregon DOR misstates the use of Audience in Michigan.

Michigan was reforming the state tax code, including the apportionment formula and method of calculating Michigan sales. The state transitioned from the older three factor apportionment formula to apportioning income entirely by sales (the single sales factor formula also provided under Oregon law). Michigan also moved from the old 'cost of performance' method to assigning sales to Michigan based on the taxpayer's market. Notably, Michigan bypassed the equally outdated 'audience' rule in favor of customer apportionment for broadcasters. In establishing contemporary rules for assigning customer sales for the general business community, Michigan received input from key industry segments including broadcasters. Michigan had an opportunity to revisit the state corporate tax code two years ago and through a second round of major reform, the single sales factor apportionment and customer based sales for broadcasters and the rest of the business community was all that remained unchanged.

Commercial domicile is required for apportioning all sales to Michigan. For advertising a second step is required for sales to Michigan customers.

The Department acknowledges that media receipts are in Michigan if the customer's commercial domicile is in Michigan. The Department, however, misstates the particular Michigan rule for

the apportionment of advertising sales by simply stating Michigan. ***'requires use of an audience factor for broadcaster advertising receipts'***.

The proper application of Michigan law requires the broadcaster first determine an advertising customer's commercial domicile and *then* for only advertisers with a commercial domicile in Michigan, apply a Michigan audience percentage. The law specifically provides as follows:

1) **if the customer of that advertising is commercially domiciled in this state** and if so,

2) **the media receipts for that sale of advertising from that customer shall be proportioned based on the ratio that the broadcaster's viewing or listening audience in this state bears to its total viewing or listening audience everywhere**

Example of advertising apportionment under Michigan law:

If a broadcaster sells $1MM in advertising to GM, 1) the sale is a Michigan sale as the customer is commercially domiciled in Michigan; 2) the GM sale is then apportioned within and without Michigan using an audience ratio.

If a broadcaster sells $1MM in advertising to Columbia Sports, the sale is not a Michigan sale as the customer is commercially domiciled outside of Michigan so no portion of the sale is assigned to Michigan.

OR HB 4138 applies commercial domicile for interstate broadcaster sales, just as Michigan law provides. Michigan further requires a second step to reduce the impact of assigning 100% of Michigan advertiser sales to the state. This second step is not part of the OR bill.

ILLINOIS

Illinois is NOT a hybrid method of apportionment for Broadcasters as stated by DOR.

Illinois, like Michigan, was transitioning from a cost of performance apportionment methodology to a true market based sourcing. Again, like Michigan, Illinois bypassed the outdated 'audience' rule in favor of customer apportionment for broadcasters. Unfortunately, the Department completely misapprehends the different sections of the Illinois statute which all relate to different types of activities by different types of taxpayers.

Subsection (i) relates to advertising revenue, which is sourced to the commercial domicile of the advertiser.

Subsection (ii) provides that in the case where film or radio programming is broadcast by a station, a network, or a cable system for a fee or other remuneration received from the recipient of the broadcast, the portion of the service that is received in Illinois is measured by the portion of the receipts of the broadcast located in Illinois. This section is to be used by cable system

operators, who receive their fees directly from individual subscribers. Cable program networks, free broadcast networks and television stations do not receive fees from viewers.

Subsection (iii) provides that in the case where film or radio programming is broadcast by a station, a network, or a cable system for a fee or other remuneration from the person providing the programming, the portion of the broadcast service that is received in Illinois is measured by the portion of the recipients of the broadcast located in Illinois. This subsection relates to the fees received by cable system operators to ensure that they include the programming received from other parties (such as cable program networks) in the broadcast service they provide to individual subscribers. This section does not relate to revenue received by national program networks.

Subsection (iv) provides that in the case where film or radio programming is provided by a taxpayer that is a network or station to a customer for broadcast in exchange for a fee or other remuneration from that customer, the broadcasting service is received at the location of the office of the customer from which the services were ordered in the regular course of business. This is exactly the revenue that is addressed in OR HB 4138. It is the license fees received by broadcasters from cable system operators and other distributors for the right to carry their programming. Similar to OR HB 4138, it is sourced to the location of the customer which is typically the principal place from which the business of the customer is managed and controlled (i.e., its commercial domicile).

Subsection (v) provides that in the case where film or radio programming is provided by a taxpayer that is not a network or station to another person for broadcasting in exchange for a fee or other remuneration from that person, the broadcasting service is received at the location of the office of the customer from which the services were ordered in the regular course of the customer's trade or business. This generally relates to revenue for syndicated programming and it is also sourced to the location of the customer (i.e., commercial domicile).

After a careful reading of the Illinois statute it becomes apparent that with respect to the revenue streams addressed by OR HB 4138, the Illinois statute, just like the Oregon proposed statute, sources revenue to the location of the customer from which the programming is ordered, viz., its commercial domicile.