



PROPOSED RULE MAKING

CR-102 (June 2004)

(Implements RCW 34.05.320)

Do NOT use for expedited rule making

Agency: Department of Revenue

- Preproposal Statement of Inquiry was filed as WSR 10-12-128 ; or
- Expedited Rule Making--Proposed notice was filed as WSR ; or
- Proposal is exempt under RCW 34.05.310(4).

- Original Notice
- Supplemental Notice to WSR
- Continuance of WSR

Title of rule and other identifying information:

WAC 458-20-19401 *Minimum nexus thresholds for apportionable activities* – Washington's business and occupation (B&O) taxes may be imposed only if a business has substantial nexus with this state. This rule explains the minimum nexus thresholds for the B&O taxation of businesses engaged in apportionable activities.

WAC 458-20-19404 *Financial institutions – Income apportionment* – this rule addresses how gross income from engaging in business as a financial institution is apportioned when the financial institution engages in business both within and outside the state.

Hearing location(s):

Capitol Plaza Building
4th Floor Exec Conference Room
1025 Union Avenue SE
Olympia, Washington 98504

Copies of draft rules are available for viewing and printing on our website at [Rules Agenda](#)

Date: July 27, 2011
Time: 9:30 A.M.

Date of intended adoption: August 5, 2011
(Note: This is **NOT** the **effective** date)

Submit written comments to:

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By: July 27, 2011

Assistance for persons with disabilities: Contact Mary Carol LaPalm (360) 725-7499 or Renee Cosare (360) 725-7514 no later than 10 days before the hearing date. For Hearing impaired please contact us via the Washington Relay Operator at (800) 833-6384.

Purpose of the proposal and its anticipated effects, including any changes in existing rules:

The Department is proposing two new rules. Part I of chapter 23, Laws of 2010 1st sp. sess. (2ESSB 6143) changed the apportionment and nexus requirements for apportionable activities, effective June 1, 2010. These rules are necessary to explain how this new law applies.

Reasons supporting proposal: New rules are needed to recognize law changes.

Statutory authority for adoption: RCW 82.32.300 and 82.01.060

Statute being implemented: Provisions of chapter 23, Laws of 2010 1st sp. sess. (2ESSB 6143) Part I

Is rule necessary because of a:

- Federal Law? Yes No
 - Federal Court Decision? Yes No
 - State Court Decision? Yes No
- If yes, CITATION:

Date June 10, 2011

Name Alan R. Lynn

Signature

Title Rules Coordinator

CODE REVISER USE ONLY

OFFICE OF THE CODE REVISER
STATE OF WASHINGTON
FILED

DATE: June 10, 2011

TIME: 10:40 AM

WSR 11-13-051

Agency comments or recommendations, if any, as to statutory language, implementation, enforcement, and fiscal matters: None.

Name of proponent: Department of Revenue

- Private
 Public
 Governmental

Name of agency personnel responsible for:

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Drafting..... Chris Coffman	1025 Union Ave. SE. Ste #544, Olympia ,Wa	(360) 534-1590
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Has a small business economic impact statement been prepared under chapter 19.85 RCW?

Yes. Attach copy of small business economic impact statement.

A copy of the statement may be obtained by contacting:

Name:

Address:

Phone:

E-mail:

No. Explain why no statement was prepared.

These rules do not impose any new performance requirements or administrative burden on any small business not required by statute.

Is a cost-benefit analysis required under RCW 34.05.328?

Yes A preliminary cost-benefit analysis may be obtained by contacting:

Name:

Address:

Phone:

E-mail:

No: Please explain: **The proposed rules are not significant legislative rules as defined by RCW 34.05.328.**

THIS PROPOSED RULE IS SUBMITTED FOR PUBLIC COMMENTS AFTER INPUT FROM INTERESTED PARTIES AND IS TO BE USED SOLELY FOR DISCUSSION PURPOSES AT THE PUBLIC HEARING ON THE PROPOSED RULE. UNDER NO CIRCUMSTANCES IS THIS PROPOSED RULE TO BE USED TO DETERMINE TAX LIABILITY AND OR EXEMPTIONS.

NEW SECTION

WAC 458-20-19401 Minimum nexus thresholds for apportionable activities. (1) Introduction.

(a) This rule only applies to periods after May 31, 2010.

(b) The state of Washington imposes business and occupation (B&O) tax on apportionable activities measured by the gross income of the business. B&O tax may only be imposed if a person has a "substantial nexus" with this state. For the purposes of apportionable activities, substantial nexus does not require a person to have physical presence in this state.

(c) The following rules may also be helpful:

(i) WAC 458-20-19402, Single factor receipts apportionment--Generally. This rule describes the general application of single factor receipts apportionment and applies only to tax liability incurred after May 31, 2010.

(ii) WAC 458-20-19403, Single factor receipts apportionment--Royalties. This rule describes the application of single factor receipts apportionment to gross income from royalties and applies only to tax liability incurred after May 31, 2010.

(iii) WAC 458-20-19404, Financial institutions--Income apportionment. This rule describes the application of single factor receipts apportionment to certain income of financial institutions and applies only to tax liability incurred after May 31, 2010.

(iv) WAC 458-20-193, Inbound and outbound interstate sales of tangible personal property.

(v) WAC 458-20-194, Doing business inside and outside the state. This rule describes separate accounting and cost apportionment and applies only to tax liability incurred from January 1, 2006 through May 31, 2010.

(d) Examples included in this rule identify a number of facts and then state a conclusion; they should be used only as a general guide. The tax results of all situations must be determined after a review of all the facts and circumstances. For the examples in this rule, gross income received by the taxpayer is from engaging in apportionable activities. Also, unless otherwise stated, the examples do not apply to tax liability prior to June 1, 2010.

(2) **Definitions.** Unless the context clearly requires otherwise, the definitions in this subsection apply throughout

this rule.

(a) **"Apportionable activities"** includes only those activities subject to B&O tax under the following classifications:

- (i) Service and other activities;
- (ii) Royalties;
- (iii) Travel agents and tour operators;
- (iv) International steamship agent, international customs house broker, international freight forwarder, vessel and/or cargo charter broker in foreign commerce, and/or international air cargo agent;
- (v) Stevedoring and associated activities;
- (vi) Disposing of low-level waste;
- (vii) Title insurance producers, title insurance agents, or surplus line brokers;
- (viii) Public or nonprofit hospitals;
- (ix) Real estate brokers;
- (x) Research and development performed by nonprofit corporations or associations;
- (xi) Inspecting, testing, labeling, and storing canned salmon owned by another person;
- (xii) Representing and performing services for fire or casualty insurance companies as an independent resident managing general agent licensed under the provisions of chapter 48.17 RCW;
- (xiii) Contests of chance;
- (xiv) Horse races;
- (xv) International investment management services;
- (xvi) Room and domiciliary care to residents of a boarding home;
- (xvii) Aerospace product development;
- (xviii) Printing or publishing a newspaper (but only with respect to advertising income);
- (xix) Printing materials other than newspapers and publishing periodicals or magazines (but only with respect to advertising income); and
- (xx) Cleaning up radioactive waste and other by-products of weapons production and nuclear research and development, but only with respect to activities that would be taxable as an "apportionable activity" under any of the tax classifications listed in (a)(i) through (xix) of this subsection if this special tax classification did not exist.

(b) **"Credit card"** means a card or device existing for the purpose of obtaining money, property, labor, or services on credit.

(c) **"Gross income of the business"** means the value proceeding or accruing by reason of the transaction of the business engaged in and includes gross proceeds of sales, compensation for the rendition of services, gains realized from

trading in stocks, bonds, or other evidences of indebtedness, interest, discount, rents, royalties, fees, commissions, dividends, and other emoluments however designated, all without any deduction on account of the cost of tangible property sold, the cost of materials used, labor costs, interest, discount, delivery costs, taxes, or any other expense whatsoever paid or accrued and without any deduction on account of losses. The term gross receipts means gross income from apportionable activities.

(d) **"Loan"** means any extension of credit resulting from direct negotiations between the taxpayer and its customer, and/or the purchase, in whole or in part, of such extension of credit from another. Loan includes participations, syndications, and leases treated as loans for federal income tax purposes. Loan does not include: Futures or forward contracts; options; notional principal contracts such as swaps; credit card receivables, including purchased credit card relationships; noninterest 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 real estate mortgage investment conduit (REMIC) or other mortgage-backed or asset-backed security; and other similar items.

(e) **"Net annual rental rate"** means the annual rental rate paid by the taxpayer less any annual rental rate received by the taxpayer from subrentals.

(f) The terms **"nexus"** and **"substantial nexus"** are used interchangeably in this rule.

(g) **"Property"** means tangible, intangible, and real property owned or rented and used in this state during the calendar year, except property does not include ownership of or rights in computer software, including computer software used in providing a digital automated service; master copies of software; and digital goods or digital codes residing on servers located in this state. Refer to RCW 82.04.192 and 82.04.215 for definitions of the terms computer software, digital automated services, digital goods, digital codes, and master copies.

(h) **"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 or political subdivision of a foreign country.

(i) **"Securities"** includes any intangible property defined as a security under section 2(a)(1) of the Securities Act of 1933 including, but not limited to, negotiable certificates of deposit and municipal bonds.

(3) **Substantial nexus.**

(a) Substantial nexus exists where a person is:

(i) An individual and is a resident or domiciliary of this state during the calendar year;

(ii) A business entity and is organized or commercially

domiciled in this state during the calendar year; or

(iii) A nonresident individual or a business entity that is organized or commercially domiciled outside this state, and in any calendar year the person has:

(A) More than fifty thousand dollars of property in this state;

(B) More than fifty thousand dollars of payroll in this state;

(C) More than two hundred fifty thousand dollars of receipts from this state; or

(D) At least twenty-five percent of the person's total property, total payroll, or total receipts in this state.

Example 1. Company commercially domiciled in Washington. Company C is commercially domiciled in Washington and has one employee in Washington who earns \$30,000 per year. Company C has substantial nexus with Washington because it is commercially domiciled in Washington. The minimum nexus thresholds for property, payroll, and receipts do not apply to a business entity commercially domiciled in this state.

(b) The department will adjust the amounts listed in (a) of this subsection based on changes in the consumer price index as required by RCW 82.04.067.

(c) The minimum nexus thresholds are determined on a tax year basis. Generally, a tax year is the same as a calendar year. See RCW 82.32.270. For the purposes of this rule, tax years will be referred to as calendar years. This means that if a person meets the minimum nexus thresholds in a calendar year, that person is subject to B&O taxes for the entire calendar year.

Example 2. Company Q is organized and domiciled outside of Washington. Company Q maintains an office in Washington which houses a single employee. Company Q has \$40,000 in property located in Washington, the employee receives \$45,000 in compensation, and has \$200,000 in apportionable receipts attributed to Washington. Company Q's total property is valued at \$200,000, total payroll compensation is \$400,000, and total apportionable receipts is \$5,000,000. Although Company Q has physical presence in Washington, it does not have substantial nexus with Washington because: (a) It is not organized or domiciled in Washington; and (b) does not have sufficient property, payroll, or receipts to meet the minimum nexus thresholds identified in subsection (2)(a) of this rule.

(4) **Property threshold.**

(a) **Location of property.**

(i) Real property - Real property owned or rented is in this state if the real property is located in this state.

(ii) Tangible personal property - Tangible personal property is in this state if it is physically located in this state.

(iii) Intangible property - Intangible property is in this state based on the following:

A loan is located in this state if:

(A) More than fifty percent of the fair market value of the real and/or personal property securing the loan is in this state. An automobile loan is in this state if the vehicle is properly registered in this state. Other than for property that is subject to registered ownership, the determination of whether the real or personal property securing a loan is in this state must be made as of the time the original agreement was made, and any and all subsequent substitutions of collateral must be disregarded; or

(B) If (a)(iii)(A) of this subsection does not apply and the borrower is located in this state.

(iv) A borrower located in this state if:

(A) The borrower is engaged in business and the borrower's commercial domicile is located in this state; or

(B) The borrower is not engaged in business and the borrower's billing address is located in this state.

(v) A credit card receivable is in this state if the billing address of the card holder is located in this state.

(vi) A nonnegotiable certificate of deposit is property in this state if the issuing bank is in this state.

(vii) Securities:

(A) A negotiable certificate of deposit is property in this state if the owner is located in this state.

(B) A municipal bond is property in this state if the owner is located in this state.

(b) **Value of property.**

(i) Property the taxpayer owns and uses in this state, other than loans and credit card receivables, is valued at its original cost basis.

Example 3. In January 2008, ABC Corp. bought Machinery for \$65,000 for use in State X. On January 1, 2011, ABC Corp. brought that Machinery into Washington for the remainder of the year. ABC Corp. has nexus with Washington based on Machinery's original cost basis value of \$65,000. The value is \$65,000 even though the property has depreciated prior to entering the state.

(ii) Property the taxpayer rents and uses in this state is valued at eight times the net annual rental rate.

Example 4. Out-of-state Business X rents office space in Washington for \$6,000 per year and has \$5,000 of office furniture and equipment in Washington. Business X has nexus with Washington because the value of the rented office space (\$6,000 multiplied by eight, which is \$48,000) plus the value of office furniture and equipment exceeds the \$50,000 property threshold.

(iii) Loans and credit card receivables owned by the taxpayer are valued at their outstanding principal balance,

without regard to any reserve for bad debts. However, if a loan or credit card receivable is actually charged off as a bad debt in whole or in part for federal income tax purposes (see 26 U.S.C. 166), the portion of the loan or credit card receivable charged off is deducted from the outstanding principal balance.

(c) **Calculating property value.** To determine whether the \$50,000 property threshold has been met, average the value of property in this state on the first and last day of the calendar year. The department may require the averaging of monthly values during the calendar year if reasonably required to properly reflect the average value of the taxpayer's property in this state throughout the taxable period.

Example 5. Company Y has property in Washington valued at \$90,000 on January 1st and \$20,000 on December 31st of the same year. The value of property in Washington is \$55,000 $((90,000 + 20,000)/2)$. Company Y has substantial nexus with Washington.

Example 6. Company A has no property located in Washington on January 1st and on December 31st of a calendar year. However, it brought \$100,000 in property into Washington on January 15th and removed it from Washington on November 15th of that calendar year. The department may compute the value of Company A's property on a monthly basis in this situation because it is required to properly reflect the average value of Company A's property in Washington ($\$100,000$ multiplied by ten (months) divided by 12 (months), which is $\$83,333$). Company A has nexus with Washington based on the value of the property averaged over the calendar year.

Example 7. Company B has no property located in Washington on January 1st and on December 31st of a calendar year. However, it brought \$100,000 in property into Washington on January 15th and removed it from Washington on February 15th of that calendar year. The department may compute the value of Company A's property on a monthly basis in this situation because it is required to properly reflect the average value of Company B's property in Washington ($\$100,000$ multiplied by one (month) divided by 12 (months), which is $\$8,333$.) Company B does not have nexus with Washington based on the value of the property averaged over the calendar year, unless this amount exceeds 25% of Company B's total property value.

Example 8. IT Co. is domiciled in State X with Employee located in Washington who works from a home office. IT Co. provided to Employee \$5,000 of office supplies and \$15,000 of equipment owned by IT Co. IT Co. does not have nexus with Washington based on the value of the property in this State ($\$20,000$) because it does not exceed \$50,000, unless this amount exceeds 25% of IT Co.'s total property value. This example does not address the payroll threshold.

(5) **Payroll threshold.** "Payroll" is the total compensation

defined as gross income under 26 U.S.C. Sec. 61 (section 61 of the Internal Revenue Code of 1986), as of June 1, 2010, paid during the calendar year to employees and to third-party representatives who represent the taxpayer in interactions with the taxpayer's clients and includes sales commissions.

(a) Payroll compensation is received in this state if it is properly reportable in this state for unemployment compensation tax purposes, regardless of whether it was actually reported to this state.

Example 9. Company D is commercially domiciled in State X and has a single Employee whose payroll of \$80,000 is properly reportable in Washington for unemployment compensation purposes. Company D has substantial nexus with Washington during the calendar year based on compensation paid Employee.

Example 10. Assume the same facts as Example 9 except only 50% of Employee's payroll is properly reportable in Washington for unemployment compensation purposes for the calendar year. Employee's Washington compensation of \$40,000 does not meet the payroll threshold to establish substantial nexus with Washington, unless this amount exceeds 25% of total payroll compensation.

(b) Third-party representatives receive payroll compensation in this state if the service(s) performed occurs entirely or primarily within this state.

(6) **Receipts threshold.** The receipts threshold is met if a taxpayer receives more than \$250,000 from apportionable activities that is attributed to Washington.

(a) All receipts from all apportionable activities are accumulated to determine if the receipts threshold is satisfied. Receipts from activities that are not subject to apportionment (e.g., retailing, wholesaling, and extracting) are not used to determine if the receipts threshold has been satisfied.

(b) Receipts are attributed to Washington per WAC 458-20-19402 (general attribution), 458-20-19403 (royalties), and 458-20-19404 (financial institutions).

Example 11. Company E is commercially domiciled in State X. In a calendar year it has \$150,000 in royalty receipts attributed to Washington per WAC 458-20-19403 and \$150,000 in gross receipts from other apportionable activities attributed to Washington per WAC 458-20-19402. Company E has substantial nexus with Washington because it has a total of \$300,000 in receipts from apportionable activities attributed to Washington in a calendar year. It does not matter that the receipts were from apportionable activities that are subject to tax under different B&O tax classifications. The receipts threshold is determined by the totality of the taxpayer's apportionable activities in Washington.

Example 12. Calculation of minimum nexus thresholds during the 2010 transition year. Company F receives \$200,000 in gross

receipts attributed to Washington on March 15, 2010; \$100,000 on July 12, 2010; and \$100,000 on November 1, 2010. Company F has substantial nexus with Washington for the period June 1, 2010, through December 31, 2010, because it received \$400,000 in gross receipts during 2010.

(7) **Application of 25% threshold.** If at least twenty-five percent of an out-of-state taxpayer's property, payroll, or receipts from apportionable activities is in Washington, then the taxpayer has substantial nexus with Washington. The twenty-five percent threshold is determined by dividing:

(a) The value of property located in Washington by the total value of taxpayer's property;

(b) Payroll located in Washington by taxpayer's total payroll; or

(c) Receipts attributed to Washington by total receipts.

Example 13. Company G is organized and commercially domiciled in State X. In a calendar year it has \$45,000 in property, \$45,000 in payroll, and \$240,000 in gross receipts attributed to Washington. Its total property is valued at \$200,000; its world-wide payroll is \$150,000; and its total gross receipts are \$2,000,000. Company G has twenty-two and a half percent of its property, thirty percent of its payroll, and twelve percent of its receipts attributed to Washington. Company G has substantial nexus with Washington because more than twenty-five percent of its payroll is located in Washington.

(8) **Application to local gross receipts business and occupations taxes.** This rule does not apply to the nexus requirements for local gross receipts business and occupation taxes.

(9) **Continuing substantial nexus.** Pursuant to RCW 82.04.220, if a person meets any of the minimum nexus thresholds in subsection (2) of this section in a calendar year, the person has nexus for the following calendar year and will owe B&O tax on its gross receipts attributable to Washington for that additional year.

Example 14. Assume Corporation J earns receipts attributable to Washington that do not exceed the minimum threshold from apportionable activities in any year, and whose physical presence in Washington ends on July 20, 2008. Corporation J's B&O tax reporting obligation for any gross receipts earned in Washington ends on December 31, 2010.

Example 15. Assume Corporation K earns receipts attributable to Washington from July 1, 2008 through March 1, 2010 and exceeds the minimum threshold from apportionable activities in 2010. Assuming Corporation K does not exceed any of the minimum nexus thresholds in 2011, the taxpayer's B&O tax reporting obligation for any gross receipts attributable to Washington ends on December 31, 2011.

Example 16. Assume Corporation L exceeded Washington's minimum nexus thresholds for apportionable income from 2010 through 2012, but does not meet them in 2013. Corporation L's B&O tax reporting obligation for any gross receipts earned in Washington ends on December 31, 2013.

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NEW SECTION

WAC 458-20-19404 Financial institutions--Income apportionment. (1) Introduction.

(a) Effective June 1, 2010, section 108, chapter 23, Laws of 2010 1st sp. sess. changed Washington's method of apportioning certain gross income from engaging in business as a financial institution. This rule addresses how such gross income must be apportioned when the financial institution engages in business both within and outside the state.

(b) Taxpayers may also find helpful information in the following rules:

(i) WAC 458-20-19401, Minimum nexus thresholds for apportionable activities. This rule describes minimum nexus standards that are effective June 1, 2010.

(ii) WAC 458-20-19402, Single factor receipts apportionment--Generally. This rule describes the general application of single factor receipts apportionment that is effective June 1, 2010.

(iii) WAC 458-20-19403, Single factor receipts apportionment--Royalties. This rule describes the application of single factor receipts apportionment to gross income from royalties and applies only to tax liability incurred after May 31, 2010.

(iv) WAC 458-20-194, Doing business inside and outside the state. This rule describes separate accounting and cost apportionment. It applies only to the periods January 1, 2006, through May 31, 2010.

(v) WAC 458-20-14601, Financial institutions--Income apportionment. This rule describes the apportionment of income for financial institutions for periods prior to June 1, 2010.

(c) Financial institutions engaged in making interstate sales of tangible personal property should also refer to WAC 458-20-193, Inbound and outbound interstate sales of tangible personal property.

(2) Apportionment and allocation.

(a) Except as otherwise specifically provided, a financial institution taxable under RCW 82.04.290 and taxable in another state must allocate and apportion its service and other activities income as provided in this rule. Any other apportionable income must be apportioned pursuant to WAC 458-20-19402, Single factor receipts apportionment--Generally or WAC

458-20-19403, Single factor receipts apportionment--Royalties. "Apportionable income" means gross income of the business generated from engaging in apportionable activities, including income received from apportionable activities performed outside this state if the income would be taxable under chapter 82.04 RCW if received from activities in this state, less the exemptions and deductions allowable under chapter 82.04 RCW. All gross income that is not includable in service and other activities income or gross income must be allocated pursuant to chapter 82.04 RCW. A financial institution organized under the laws of a foreign country, the Commonwealth of Puerto Rico, or a territory or possession of the United States, except such institutions that are exempt under RCW 82.04.315, whose effectively connected income (as defined under the federal Internal Revenue Code) is taxable both in this state and another state, other than the state in which it is organized, must allocate and apportion its gross income as provided in this rule.

(b) The apportionment percentage is determined by the taxpayer's receipts factor (as described in subsection (4) of this rule).

(c) The receipts factor must be computed according to the method of accounting (cash or accrual basis) used by the taxpayer for Washington state tax purposes for the taxable period. Persons should refer to WAC 458-20-197, When tax liability arises and WAC 458-20-199, Accounting methods for further guidance on the requirements of each accounting method. Generally, financial institutions are required to file returns on a monthly basis. To enable financial institutions to more easily comply with this rule, financial institutions may file returns using the receipts factor calculated based on the most recent calendar year for which information is available. If a financial institution does not calculate its receipts factor based on the previous calendar year for which information is available, it must use the current year information to make that calculation. In either event, a reconciliation must be filed for each year not later than October 31st of the following year. See WAC 458-20-19402 for an example of how to use the most recent calendar year for which information is available. In the case of consolidations, mergers, or divestitures, a taxpayer must make the appropriate adjustments to the factors to reflect its changed operations.

(d) Interest and penalties on reconciliations under (c) of this subsection apply as follows:

(i) Interest must be assessed on any additional tax due at the rate provided for delinquent excise taxes under chapter 82.32 RCW, retroactively to the date the original return was due, and will accrue until the additional taxes are paid.

(ii) Interest as provided in RCW 82.32.060 will apply to

any tax paid in excess of that properly due on a return as a result of a taxpayer using previous calendar year data or incomplete current year data to calculate the receipts factor.

(iii) Penalties as provided in RCW 82.32.090 will apply to any such additional tax due only if the reconciliation for a tax year is not completed and additional tax is not paid by October 31st of the following year.

(e) See WAC 458-20-19402 for an example of the reconciliation process.

(f) If the allocation and apportionment provisions of this rule do not fairly represent the extent of its business activity in this state, the taxpayer may petition for, or the department may require, in respect to all or any part of the taxpayer's business activity:

(i) Separate accounting;

(ii) The inclusion of one or more additional factors which will fairly represent the taxpayer's business activity in this state; or

(iii) The employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's receipts.

(3) **Definitions.** The following definitions apply throughout this rule unless the context clearly requires otherwise:

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

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

(i) A borrower, other than a credit card holder, that is engaged in a trade or business and maintains its commercial domicile in this state; or

(ii) A borrower that is not engaged in a trade or business or a credit card holder, whose billing address is in this state.

(c) **"Commercial domicile"** means:

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

(ii) 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 is deemed for the purposes of this rule 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 is presumed, subject to rebuttal by a preponderance of the evidence, that the location from which the

taxpayer's trade or business is principally managed and directed in 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 period.

(d) **"Credit card"** means credit, travel or entertainment card.

(e) **"Credit 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 card has charged merchandise or services to the credit card.

(f) **"Department"** means the department of revenue.

(g) **"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.

(h) **"Financial institution"** means:

(i) Any corporation or other business entity chartered under Title 30, 31, 32, or 33 RCW, 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;

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

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

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

(v) Any corporation organized under the provisions of 12 U.S.C. Secs. 611 to 631;

(vi) Any agency or branch of a foreign depository as defined in 12 U.S.C. Sec. 3101 that is not exempt under RCW 82.04.315;

(vii) Any credit union, other than a state or federal credit union exempt under state or federal law;

(viii) 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) **"Gross income of the business," "gross income," or "income":**

(i) Has the same meaning as in RCW 82.04.080 and means the value proceeding or accruing by reason of the transaction of the business engaged in and includes compensation for the rendition of services, gains realized from trading in stocks, bonds, or other evidences of indebtedness, interest, discount, rents, royalties, fees, commissions, dividends, and other emoluments

however designated, all without any deduction on account of the cost of tangible property sold, the cost of materials used, labor costs, interest, discount, delivery costs, taxes, or any other expense whatsoever paid or accrued and without any deduction on account of losses; and

(ii) Does not include amounts received from an affiliated person if those amounts are required to be determined at arm's length per sections 23A or 23B of the Federal Reserve Act. For the purpose of (3)(i) of this subsection, affiliated means the affiliated person and the financial institution are under common control. Common control means the possession (directly or indirectly), of more than fifty percent of power to direct or cause the direction of the management and policies of each entity. Control may be through voting shares, contract, or otherwise.

(iii) Financial institutions must determine their gross income of the business from gains realized from trading in stocks, bonds, and other evidences of indebtedness on a net annualized basis.

(j) **"Loan"** means any extension of credit resulting from direct negotiations between the taxpayer and its customer, and/or the purchase, in whole or in part, of such extension of credit from another. Loan includes participations, syndications, and leases treated as loans for federal income tax purposes. Loan does not include: Futures or forward contracts; options; notional principal contracts such as swaps; credit card receivables, including purchased credit card relationships; noninterest 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 real estate mortgage investment conduit (REMIC), or other mortgage-backed or asset-backed security; and other similar items.

(k) **"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 was real property, when valued at fair market value as of the time the original loan or obligation was incurred.

(l) **"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 card is accepted in payment for merchandise or services sold to the card holder.

(m) **"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.

(n) **"Person"** has the meaning given in RCW 82.04.030.

(o) **"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.

(p) **"Service and other activities income"** means the gross income of the business taxable under RCW 82.04.290, including income received from activities outside this state if the income would be taxable under RCW 82.04.290 if received from activities in this state, less the exemptions and deductions allowable under chapter 82.04 RCW.

(q) **"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 or political subdivision of a foreign country.

(r) **"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.

(s) **"Taxable in another state"** means either:

(i) The taxpayer is subject to business activities tax by another state on its service and other activities income; or

(ii) The taxpayer is not subject to a business activities tax by another state on its service and other activities income, but that state has jurisdiction to subject the taxpayer to a business activities tax on such income under the substantial nexus standards explained in WAC 458-20-19401. For purposes of (s) of this subsection, "business activities tax" means a tax measured by the amount of, or economic results of, business activity conducted in a state. The term includes taxes measured in whole or in part on net income or gross income or receipts. Business activities tax does not include a sales tax, use tax, or a similar transaction tax, imposed on the sale or acquisition of goods or services, whether or not denominated a gross receipts tax or a tax imposed on the privilege of doing business.

(t) **"Taxable period"** means the calendar year during which tax liability is incurred.

(4) **Receipts factor.**

(a) General. The receipts factor is a fraction, the numerator of which is the gross income of the taxpayer in this state during the taxable period and the denominator of which is the gross income of the taxpayer inside and outside this state during the taxable period. 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.

(b) Interest from loans secured by real property.

(i) The numerator of the receipts factor includes interest

and fees or penalties in the nature of interest from loans secured by real property if the property is located within this state. If the property is located both within this state and one or more other states, the income described in this subsection (b)(i) is 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 this state. If more than fifty percent of the fair market value of the real property is not located within any one state, then the income described in this subsection (b)(i) must be included in the numerator of the receipts factor if the borrower is located in this state.

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

(c) Interest from loans not secured by real property. The numerator of the receipts factor includes interest and fees or penalties in the nature of interest from loans not secured by real property if the borrower is located in this state. Interest and fees on loans secured by commercial aircraft that qualifies for the exemption from business and occupation tax under RCW 82.04.43391 are not included in either numerator or the denominator of the receipts factor.

(d) 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 federal Internal Revenue Code.

(i) 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 (b) of this subsection 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.

(ii) 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 (c) of this subsection (4) 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.

(e) Receipts from credit card receivables. The numerator of the receipts factor includes interest and fees or penalties in the nature of interest from credit card receivables and income from fees charged to card holders, such as annual fees, if the billing address of the card holder is in this state.

(f) 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 (e) of this subsection 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.

(g) Credit card issuer's reimbursement fees. The numerator of the receipts factor includes all credit card issuer's reimbursement fees multiplied by a fraction, the numerator of which is the amount included in the numerator of the receipts factor pursuant to (e) of this subsection 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.

(h) Receipts from merchant discount. The numerator of the receipts factor includes receipts from merchant discount if the commercial domicile of the merchant is in this state. Such receipts must be computed net of any cardholder charge backs, but must not be reduced by any interchange transaction fees or by any issuer's reimbursement fees paid to another for charges made by its card holders.

(i) Loan servicing fees.

(i)(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 under (b) of this subsection 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 under (c) of this subsection 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.

(ii) If the taxpayer receives loan servicing fees for servicing either the secured or the unsecured loans of another, the numerator of the receipts factor includes such fees if the borrower is located in this state.

(j) Receipts from services. The numerator of the receipts factor includes receipts from services not otherwise apportioned under this subsection (4) if the service is performed in this state. If the service is performed both inside and outside this state, the numerator of the receipts factor includes receipts from services not otherwise apportioned under this subsection

(4), if a greater proportion of the activity producing the receipts is performed in this state based on cost of performance.

(k) Receipts from investment assets and activities and trading assets and activities.

(i) Interest, dividends, net gains (but not less than zero) and other income from investment assets and activities and from trading assets and activities are 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 (k)(i)(A) and (B) of this subsection, the receipts factor includes the following:

(A) The receipts factor includes 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.

(B) The receipts factor includes the amount by which interest, dividends, gains and other receipts 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.

(ii) The numerator of the receipts factor includes interest, dividends, net gains (but not less than zero) and other receipts from investment assets and activities and from trading assets and activities described in (k)(i) of this subsection that are attributable to this state.

(A) 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 this state 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 this state and the denominator of which is the average value of all such assets.

(B) 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 this state and included in the numerator is determined by multiplying the amount described in (k)(i)(A) of this subsection 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 this state and the denominator of which is the average value of all such funds and such securities.

(C) 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 (k)(i)(A) and (B) of this subsection), attributable to this state and included in the numerator is determined by multiplying the amount described in (k)(i)(B) of this subsection 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 this state and the denominator of which is the average value of all such assets.

(D) For purposes of (k)(ii) of this subsection, the average value of trading assets owned by the taxpayer is the original cost or other basis of such property for federal income tax purposes without regard to depletion, depreciation, or amortization.

(iii) In lieu of using the method set forth in (k)(ii) of this subsection, the taxpayer may elect, or the department may require in order to fairly represent the business activity of the taxpayer in this state, the use of the method set forth in this paragraph.

(A) 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 this state 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 receipts from such assets and activities which are properly assigned to a regular place of business of the taxpayer within this state and the denominator of which is the gross income from all such assets and activities.

(B) 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 this state and included in the numerator is determined by multiplying the amount described in (k)(i)(A) of this subsection 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 this state and the denominator of which is the gross income from all such funds and such securities.

(C) The amount of interest, dividends, gains and other receipts 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 (k)(ii)(A) or (B) of this subsection), attributable to this state and included in the numerator is determined by multiplying the amount described in (k)(i)(B) of this subsection 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 this state and the denominator of which is the gross income from all such assets and activities.

(iv) If the taxpayer elects or is required by the department to use the method set forth in (k)(iii) of this subsection, it must 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.

(v) The taxpayer has the burden of proving that an investment asset or activity or trading asset or activity was properly assigned to a regular place of business outside of this state by demonstrating that the day-to-day decisions regarding the asset or activity occurred at a regular place of business outside this state. If 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 this state and one such regular place of business is outside this state, such asset or activity is 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. Such policies and guidelines are presumed, subject to rebuttal by preponderance of the evidence, to be established at the commercial domicile of the taxpayer.

(1) 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 are included in the numerator of the receipts factor, if the taxpayer's commercial domicile is in this state.

(5) **Effective date.** This rule applies to gross income that is reportable with respect to tax liability beginning on and after June 1, 2010.

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