RULE-MAKING ORDER

CR-103E (May 2009)
(Implements RCW 34.05.360)

Agency: Department of Revenue

Emergency Rule Only

Effective date of rule:
Emergency Rules
☒ Immediately upon filing.
☐ Later (specify) ________________

Any other findings required by other provisions of law as precondition to adoption or effectiveness of rule?
☐ Yes ☒ No If Yes, explain:

Purpose: Part I of Chapter 23, 2010 Laws 1st Special Session (2ESSB 6143) changed the apportionment and nexus requirements for apportionable activities, effective June 1, 2010. The Department has adopted the following emergency rules to explain how these requirements apply:

- WAC 458-20-19401 (Rule 19401) *Minimum nexus thresholds for apportionable activities*
- WAC 458-20-19402 (Rule 19402) *Single factor receipts apportionment – Generally*
- WAC 458-20-19403 (Rule 19403) *Single factor receipts apportionment – Royalties*
- WAC 458-20-19404 (Rule 19404) *Financial institutions – Income apportionment*

Changes from the previous emergency rules filed October 1, 2010 under WSR 10-20-104 were made in the following subsections:

- Rule 19401 – No changes
- Rule 19402 –Subsection (5) *Attribution of income*
- Rule 19403 - Subsection (5) *How are royalty receipts attributed to Washington*
- Rule 19404 – No changes

Citation of existing rules affected by this order:
Repealed:
Amended:
Suspended:

Statutory authority for adoption: RCW 82.32.300 and 82.01.060 (2)

Other authority :

EMERGENCY RULE
Under RCW 34.05.350 the agency for good cause finds:

☒ That immediate adoption, amendment, or repeal of a rule is necessary for the preservation of the public health, safety, or general welfare, and that observing the time requirements of notice and opportunity to comment upon adoption of a permanent rule would be contrary to the public interest.

☐ That state or federal law or federal rule or a federal deadline for state receipt of federal funds requires immediate adoption of a rule.

☐ That in order to implement the requirements or reductions in appropriations enacted in any budget for fiscal years 2009, 2010, or 2011, which necessitates the need for the immediate adoption, amendment, or repeal of a rule, and that observing the time requirements of notice and opportunity to comment upon adoption of a permanent rule would be contrary to the fiscal needs or requirements of the agency.

Reasons for this finding: **An emergency adoption of these new rules is necessary because permanent rules cannot be adopted at this time.**

Date adopted: January 28, 2011

NAME Alan R. Lynn

SIGNATURE Alan R Lynn

TITLE Rules Coordinator

CODE REVISER USE ONLY

OFFICE OF THE CODE REVISER
STATE OF WASHINGTON
FILED

DATE: January 28, 2011
TIME: 1:26 PM

WSR 11-04-068

Note: If any category is left blank, it will be calculated as zero.
No descriptive text.

Count by whole WAC sections only, from the WAC number through the history note.
A section may be counted in more than one category.

The number of sections adopted in order to comply with:

Federal statute:	New	___	Amended	___	Repealed	___
Federal rules or standards:	New	___	Amended	___	Repealed	___
Recently enacted state statutes:	New	4	Amended	___	Repealed	___

The number of sections adopted at the request of a nongovernmental entity:

New ___ Amended ___ Repealed ___

The number of sections adopted in the agency's own initiative:

New 4 Amended ___ Repealed ___

The number of sections adopted in order to clarify, streamline, or reform agency procedures:

New ___ Amended ___ Repealed ___

The number of sections adopted using:

Negotiated rule making:	New	___	Amended	___	Repealed	___
Pilot rule making:	New	___	Amended	___	Repealed	___
Other alternative rule making:	New	___	Amended	___	Repealed	___

This rule was adopted on an emergency basis effective January 28, 2011. It may be used to determine tax liability until May 28, 2011, unless the Department adopts a permanent rule prior to this date.

NEW SECTION

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

(a) Business and occupation (B&O) taxes may not be imposed on a business unless that business has a substantial nexus with this state. The terms "nexus" and "substantial nexus" are used interchangeably in this rule.

Section 104, chapter 23, Laws of 2010 1st sp. sess. establishes, effective June 1, 2010, minimum nexus thresholds for the B&O taxation of apportionable activities. The minimum nexus thresholds are determined on a tax year basis. Generally, a tax year is the same as a calendar year. For the purposes of this rule, tax years will be referred to as calendar years. This means that if a taxpayer's activities in Washington meet the minimum nexus thresholds in a calendar year, the taxpayer is subject to B&O taxes for the entire calendar year. For 2010, the minimum nexus thresholds are based on the entire 2010 calendar year, but taxes are only due under the new thresholds from June 1, 2010, forward. Whether a taxpayer had substantial nexus with Washington prior to June 1, 2010, is determined by a physical presence standard. See WAC 458-20-194 for more information.

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

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

(ii) 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.

(c) 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.

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

(a) "Apportionable activities" include only those activities subject to business and occupation tax under the following classifications:

(i) Service and other activities,

(ii) Royalties (see WAC 458-20-19403 for apportionment of 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 (xviii) of this subsection (2) if this special tax classification did not exist.

(b) "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.

(c)(i) “Property” means tangible, intangible, and real property owned or rented and used in this state during the calendar year, except as provided in (ii) of this subsection (2)(c).

(ii) 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.”

(d) “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.

(3) **How is substantial nexus for apportionable activities determined?** A person is deemed to have substantial nexus for apportionable activities with this state in any calendar year if the person is:

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

(b) A business entity and is organized or commercially domiciled in this state during the calendar year; or

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

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

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

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

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

(d) The Department will adjust the amounts listed in (c) of this subsection (3) based on changes in the consumer price index as required by section 104(5), chapter 23, Laws of 2010 1st sp. sess.

(4) **How is the property threshold determined?**

(a) The value of property is determined by averaging the values at the beginning and ending of the calendar year; but 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.

(b) What value is placed on 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.

(ii) 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 charged off in whole or in part for federal income tax purposes, the portion of the loan or credit card receivable charged off is deducted from the outstanding principal balance.

(A) A loan is located in this state if:

(I) More than fifty percent (50%) of the fair market value of the real and/or personal property securing the loan is located in this state. The determination of whether the real or personal 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; or

(II) The borrower is located in this state, but only if a loan is:

- unsecured; or
- secured and there is no state where more than fifty percent (50%) of the fair market value of property securing the loan is located.

A borrower that is engaged in business is located in this state if the borrower's commercial domicile is located in this state. A borrower who is not engaged in business is located in this state if the borrower's billing address is located in this state.

(B) Credit card receivables are located in this state if the billing address of the card holder is located in this state.

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

(c) For purposes of this subsection, the following definitions apply:

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

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

(5) **How is the payroll threshold determined?** "Payroll" is the total compensation (wages, salaries, commissions, and any other form of remuneration defined as gross income under 26 U.S.C. Sec. 61 of the federal internal revenue code of 1986, as of June 1, 2010) paid during the calendar year to employees and non-employees (third-party representatives) who represent the taxpayer in interactions with the taxpayer's clients and includes sales commissions.

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

(b) Nonemployee compensation is paid in this state if the service performed by the representative third party occurs entirely or primarily within this state.

(6) **How is the receipts threshold determined?** The receipts threshold includes only the taxpayer's gross income assigned to this state from engaging in apportionable activities. The gross income of the business is attributed to this state if it is part of the numerator of the apportionment calculation as explained in WAC 458-20-19402, 19403, or 19404.

(7) **If an out-of-state taxpayer does not meet the $50,000 property, $50,000 payroll, or $250,000 receipts nexus thresholds, can it still have substantial nexus with Washington?** Yes. If twenty-five percent (25%) 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 (25%) threshold is determined by dividing the value of property located in Washington by the total value of taxpayer's property, payroll located in Washington by taxpayer's total payroll, or the receipts attributed to Washington by total receipts.

(8) **Do the minimum nexus thresholds explained in this rule apply to local gross receipts business and occupations taxes?** No. Taxpayers must still comply with their local business and occupations tax nexus laws. This rule does not apply to the nexus requirements for local gross receipts business and occupation taxes.

(9) **Once established, how long does nexus continue?** A person who establishes substantial nexus with this state in any calendar year will be deemed to have a substantial nexus with this state for the following calendar year. This applies for all taxpayers, regardless of the business and occupation tax classification(s) they are subject to, e.g. service and other activities, retailing, or wholesaling.

(10) **Do the nexus thresholds in subsection (3) of this rule apply to non-apportionable activities?** No. The nexus thresholds in subsection (3) of this rule apply only with respect to apportionable activities.

(a) A person engaged in non-apportionable activities is subject to B&O tax on a non-apportionable activity only if the person has a physical presence in this state, which need only be demonstrably more than a slightest presence. This is true even if the person is engaged in apportionable activities in this state and has nexus under the thresholds in subsection (3) of this rule. A person is physically present in this state if the person has property or employees in this state. A person is also physically present in this
state if the person, either directly or through an agent or other representative, engages in activities in this state that are significantly associated with the person's ability to establish or maintain a market for its products in this state.

(b) Non-apportionable activities include those activities taxed under the following B&O tax classifications: Retailing, wholesaling, manufacturing, processing for hire, extracting, extracting for hire, printing and publishing (except for advertising), government contracting, public road construction, the classifications in RCW 82.04.280 (2) and (6), and any other activity not specifically included in the definition of apportionable activities in subsection (3) of this rule.

(11) **Examples.** For each of the examples in this subsection (11), gross income received by the taxpayer is from engaging in apportionable activities. Also, the examples have no applicability to tax liability prior to June 1, 2010.

(a) **Example 1:** Company A is 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 income from other apportionable activities attributed to Washington per WAC 458-20-19402.
Company A has substantial nexus with Washington because it has a total of $300,000 in receipts 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. Substantial nexus is determined by the totality of the taxpayer's apportionable activities in Washington.

(b) **Example 2:** Company B is domiciled in state Y. In a calendar year it has $45,000 in property, $45,000 in payroll, and $240,000 in gross income attributed to Washington. Its total property is valued at $200,000; its world-wide payroll is $200,000; and its total gross income is $2,000,000.

Company B does not have substantial nexus with Washington during the calendar year based on the minimum thresholds listed in subsection (3) above.

(c) **Example 3:** Assume the same facts as Example 2 except world-wide payroll is $150,000. With the changed facts, Company B has substantial nexus with Washington because thirty percent (30%) of its payroll is located in Washington.

(d) **Example 4:** Company C is domiciled in Canada. It has $200,000 of gross income attributed to Washington and $300,000 of gross income attributed to Canada. Company C has no property or payroll located in Washington. Company C has substantial nexus with Washington because forty percent of its receipts are attributed to Washington.

(e) **Example 5:** Company D 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 D's property on a monthly basis in this situation because it is required to properly reflect the average value of Company D's property in Washington ($100,000 multiplied by ten divided by 12 which is $83,333). Company D has nexus with Washington based on the value of the property averaged over the calendar year.

(f) **Example 6:** Company E receives $100,000 in gross income attributed to Washington on each of March 15, 2010; July 12, 2010; and November 1, 2010. Company E has substantial nexus with Washington for the period June 1, 2010, through December 31, 2010, because it received $300,000 in gross income during 2010. Company E will also have substantial nexus with Washington for 2011 regardless of the amount of gross income attributed to Washington in 2011.

This rule was adopted on an emergency basis effective January 28, 2011. It may be used to determine tax liability until May 28, 2011, unless the Department adopts a permanent rule prior to this date.

NEW SECTION

WAC 458-20-19402 Single factor receipts apportionment – Generally. (1) **Introduction.**

(a) Section 105, chapter 23, Laws of 2010 1st sp. sess. establishes a new apportionment method for businesses engaged in apportionable activities and that have nexus with Washington. The new apportionment method explained in this rule only applies to business and occupation (B&O) tax liability incurred after May 31, 2010. This rule does not apply to the apportionment of income of financial institutions taxable under RCW 82.04.290, which is governed by WAC 458-20-19404, nor the receipt of royalty income from granting the right to use intangible property under WAC 458-20-19403.

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

(i) WAC 458-20-19401 Minimum nexus thresholds for apportionable activities. This rule describes minimum nexus thresholds that are effective June 1, 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 Single factor receipts apportionment – Financial institutions. 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 458-20-194 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.

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

(c) 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

(2) **Definitions.** The following definitions apply to this rule:

(a) "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 this chapter if received from activities in this state, less the exemptions and deductions allowable under chapter 82.04 RCW.

(i) Example 1. Corporation A received $2,000,000 in gross income from its world-wide apportionable activities, including $500,000 in world-wide bona fide initiation fees deductible under RCW 82.04.4282. Corporation A's apportionable income would be $1,500,000.

(b) "Apportionable activities" means only those activities subject to B&O tax under the following classifications:

(i) Service and other activities,

(ii) Royalties (see WAC 458-20-19403 for apportionment of 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 (xviii) of this subsection (2) if this special tax classification did not exist.

(c) "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. The term includes personal income taxes if the gross income from apportionable activities is included in the gross income subject to the personal income tax. The term "business activities tax" does not include a sales tax, use tax, or 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.

(d) "Customer" means a person or entity to whom the taxpayer makes a sale or renders services or from whom the taxpayer otherwise receives gross income of the business.

(e) "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.

(f) "Taxable in another state" means either:

(i) The taxpayer is actually subject to a business activities tax by another state on its income received from engaging in apportionable activity; or

(ii) The taxpayer is not subject to a business activities tax by another state on its income received from engaging in apportionable activity, but the other state has jurisdiction to subject the taxpayer to a business activities tax on such income under the substantial nexus thresholds described in WAC 458-20-19401.

(3) **Apportionment general:** Persons earning apportionable income subject to B&O tax and that are also taxable in another state are entitled to determine their taxable income for B&O

tax purposes by using the apportionment method provided in this rule. Taxable income is determined by multiplying apportionable income from each apportionable activity by its receipts factor.

(4) **Receipts Factor.** The receipts factor is a fraction that applies to all apportionable income for each calendar year. Separate receipts factors must be calculated for each apportionable activity taxed under a separate business and occupation tax classification.

(a) The numerator of the receipts factor is the total gross income of the business of the taxpayer attributable to this state during the calendar year from engaging in an apportionable activity.

(b) The denominator of the receipts factor is the total gross income of the business of the taxpayer from engaging in an apportionable activity everywhere in the world during the tax year, less amounts that are attributed to states where the taxpayer is not taxable and at least some of the activity is performed in Washington.

(c) Example 2. XYZ Corp. is a Washington business, has no property or payroll outside of Washington, and performs all of its services inside this state. XYZ Corp. has gross income from apportionable activities that is attributed using the criteria listed in subsection (5) below as follows: Washington $500,000; Idaho $200,000; Oregon $100,000; and California $300,000. XYZ Corp. is subject to Oregon corporate income tax, but does not owe any California or Idaho business activities taxes. The $200,000 that would be attributed to Idaho is excluded from the denominator because XYZ Corp. performs the services in Washington, and it is not subject to actual Idaho business activities taxes and does not have substantial nexus with Idaho under Washington thresholds. Although California does not impose a business activities tax on XYZ Corp., XYZ Corp. does have substantial nexus with California using Washington thresholds (more than $250,000 in receipts). Therefore, the California attributed income is not excluded from the denominator. The Oregon receipts remain in the denominator because XYZ Corp. is subject to Oregon corporate income taxes. The receipts factor is 500,000/900,000 or 55.56%.

(d) Example 3. The same facts as Example 2 except all of XYZ's property and payroll are located in Oregon, and XYZ Corp. performs no activities in Washington related to the $200,000 attributed to Idaho. In this situation, the $200,000 is not excluded from the denominator. The receipts factor is 500,000/1,100,000 or 45.45%.

(5) **Attribution of income.** Income is attributed to states based on a cascading method. That is, each receipt is attributed to a state based on a series of rules. These rules are:

(a)(i) If a taxpayer can reasonably determine the amount of apportionable receipts related to the benefit of the services received in a state, that amount of apportionable receipts is attributable to that state. This may be shown by application of a reasonable method of proportionally assigning the benefit among states. The result determines the receipts attributed to each state. A taxpayer receives the benefit of a service in this state when:

(A) The service relates to real property that is located in this state;

(B) An apportionable service relates to tangible personal property that is located in this state at the time the service is received; or

(C) The service does not relate to real or tangible personal property, and:

(I) The service is provided to a person not engaged in business who is physically present in this state at the time the service is received; or

(II) The service is provided to a person engaged in business in this state, and the service relates to the person's business activities in this state.

(ii) Examples.

(A) Example 4. Director serves on the board of directors of DEF, Inc. DEF, Inc. is commercially domiciled in State Z. DEF, Inc. is Director's customer. DEF is engaged in business in State Z, and the director's services relate to the management of DEF, Inc. Therefore, DEF, Inc. receives the benefit of Director's services in State Z.

(B) Example 5. ABC is headquartered outside of Washington and provides retail services to customers in Washington, Oregon, and Idaho. When those customers fail to pay ABC for its services, ABC contracts with Debt Collector located outside of Washington to collect the debt. ABC pays Debt Collector a percentage of the amount collected. ABC is engaged in business in Washington and the activities of Debt Collector relate to that business, therefore the benefit of the service is received by ABC in Washington when Debt Collector obtains payment from debtors located in Washington.

(C) Example 6. The same facts as Example 5, except Debt Collector is paid a fixed amount per month regardless of the total amount collected from debtors, and the debtors are located in Idaho and Washington. If Debt Collector can reasonably determine the proportion of the benefit received by ABC in each state, then that proportion of the fixed amount is the benefit received in each state. Depending on the circumstances, reasonable means to determine the proportion received in each state could be amounts recovered.

(b) If a taxpayer is unable to separately determine the benefit of the services in specific states under (a), and as a result the customer received the benefit of the service in multiple states, the apportionable receipts of the business is attributed to the state in which the benefit of the service was primarily received. Primarily means in this case more than 50%.

(i) Example 7. The same facts as Example 6, except Debt Collector cannot reasonably determine the portion of the benefit received in each state, Debtor Collector will have to use the remaining rules in (c) through (g) of this subsection (5) to attribute the income from ABC.

(c) If the taxpayer is unable to attribute gross income of the business under (a) or (b) of this subsection (5), gross income of the business must be attributed to the state from which the customer ordered the service.

(d) If the taxpayer is unable to attribute gross income of the business under (a), (b), or (c) of this subsection (5), gross income of the business must be attributed to the state to which the billing statements or invoices are sent to the customer by the taxpayer.

(e) If the taxpayer is unable to attribute gross income of the business under (a), (b), (c), or (d) of this subsection (5), gross income of the business must be attributed to the state from which the customer sends payment to the taxpayer.

(f) If the taxpayer is unable to attribute gross income of the business under (a), (b), (c), (d), or (e) of this subsection (5), gross income of the business must be attributed to the state where the customer is located as indicated by the customer's address: (i) Shown in the taxpayer's business records maintained in the regular course of business; or (ii) obtained during consummation of the sale or the negotiation of the contract for services, including any address of a customer's payment instrument when readily available to the taxpayer and no other address is available.

(g) If the taxpayer is unable to attribute gross income of the business under (a), (b), (c), (d), (e) or (f) of this subsection (5), gross income of the business must be attributed to the commercial domicile of the taxpayer.

(6) **Reporting methods.**

(a) Taxpayers entitled to use the apportionment method described in this rule may report their apportionable income based on the receipts factor for the most recent calendar year for which the taxpayer has information. If a taxpayer does not calculate the receipts factor for the current tax year based on the most recent tax year for which information is available, the taxpayer must use current year information.

(b) Regardless of how a taxpayer reports its apportionable income under (a) of this subsection 6, when the taxpayer has the information from which to determine the receipts for a calendar year, it must file reconciliation and either obtain a refund or pay the additional tax. In either event (refund or additional taxes due), interest will apply retroactively to the due date of each tax return. If the reconciliation is completed prior to October 31st of the following year, no penalties will apply.

(c) Example 8: Assume that LMN is headquartered in Washington, reports B&O taxes on a quarterly basis, and its apportionable income is a constant $300,000 per quarter. LMN's receipts factor after performing the reconciliation is as follows:

Year	Receipt factor	When Determined
Year 1	0.28	March of Year 2
Year 2	0.25	September of Year 3
Year 3	0.35	June of Year 4
Year 4	0.30	June of Year 5

The following table demonstrates how LMN should report its apportionable income for Years 3 and 4.

Tax return	Gross income	Receipt factor used	Taxable reported	Reconciliation amount
Year 3 Quarter 1	300,000	0.28[1]	84,000	
Year 3 Quarter 2	300,000	0.28	84,000	
Year 3 Quarter 3	300,000	0.25[2]	75,000	
Year 3 Quarter 4	300,000	0.25	75,000	
Year 4 Quarter 1	300,000	0.25	75,000	
Year 4 Quarter 2	300,000	0.35[3]	105,000	
Year 3 reconciliation	1,200,000	0.35	420,000	102,000[4]
Year 4 Quarter 3	300,000	0.35	105,000	
Year 4 Quarter 4	300,000	0.35	105,000	
Year 4 reconciliation	1,200,000	0.30	360,000	(30,000)[5]

[1] LMN will be using its year 1 receipts factor for the first 2 quarters of year 3 because it is the most recent year for which it has accurate numbers.
[2] LMN will change its receipts factor for the third quarter to year 2's actual receipts factor because it now has that information.
[3] LMN will change its receipts factor for the third quarter to year 3's actual receipts factor because it now has that information.
[4] LMN will file its reconciliation for Year 3. The taxable amount is $420,000 less the previously reported taxable amount of $318,000. This means LMN will owe taxes on $102,000 plus interest on the underpaid taxes. However, no penalties will be imposed if the reconciliation is filed with the department no later than October 31st of Year 4.

[5] LMN will file its reconciliation for Year 3. The taxable amount is $360,000 less the previously reported taxable amount of $390,000. This means LMN overpaid taxes by $30,000. LMN will receive interest on the overpaid taxes.

This rule was adopted on an emergency basis effective January 28, 2011. It may be used to determine tax liability until May 28, 2011, unless the Department adopts a permanent rule prior to this date.

NEW SECTION

WAC 458-20-19403 Single factor receipts apportionment – Royalties. (1) **Introduction.** Effective June 1, 2010, section 105, chapter 23, Laws of 2010 1st sp. sess. changed Washington's method of apportioning the gross income from royalties. This rule addresses how such gross income must be apportioned when the business receives royalty payments from both within and outside the state.

(a) This rule is limited to the apportionment of gross income from royalties. This rule does not apply to apportionment or allocation of income from any other business activity.

(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 thresholds 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 458-20-19404 Single factor receipts apportionment – Financial institutions. 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 458-20-194 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.

(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.

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

(a) "Apportionable activity" means those activities conducted by a person in the business of receiving gross income from royalties.

(b) "Apportionable income" means gross income of the business generated from engaging in apportionable activity, including income received from apportionable activity performed outside Washington if the income would be taxable under the business and occupation tax if received from activities in Washington less any allowable exemptions and deductions under chapter 82.04 RCW.

(c) "Business activities tax" means a tax measured by the amount of, or economic results of, business activity conducted in a state by a person. The term includes taxes measured in whole or in part on net income or gross income or receipts. In the case of sole proprietorships and pass-through entities, the term includes personal income taxes if the gross income from royalties is included in the gross income subject to the personal income tax. The term "business activities tax" does not include a sales tax, use tax, or similar transaction tax, imposed on the sale or acquisition of goods or services, whether or not referred to as a gross receipts tax or a tax imposed on the privilege of doing business.

(d) "Customer" means a person who pays royalties or charges in the nature of royalties for the use of the taxpayer's intangible property.

(e) "Gross income from royalties" means compensation for the use of intangible property, including charges in the nature of royalties regardless of where the intangible property will be used. "Gross income from royalties" does not include compensation for any natural resources, the licensing of prewritten computer software to the end user, or the licensing of digital goods, digital codes, or digital automated services to the end user as defined in RCW 82.04.190(11).

(f) "Intangible property" includes: copyrights, patents, licenses, franchises, trademarks, trade names and similar items.

(g) "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.

(h) "Taxable in another state" means either:

(i) The taxpayer is actually subject to a business activities tax by another state on its income received from engaging in apportionable activity; or

(ii) The taxpayer is not subject to a business activities tax by another state on its income received from engaging in apportionable activity, but the other state has jurisdiction to subject the taxpayer to a business activities tax on such income under the substantial nexus thresholds described in WAC 458-20-19401.

(iii) "Not Taxable" with respect to a particular state means the taxpayer is not actually subject to a business activities tax by that state on its income received from engaging in apportionable activities and that state does not have jurisdiction to subject the taxpayer to a business activities tax on such income under the substantial nexus thresholds described in WAC 458-20-19401.

(3) **How does a taxpayer apportion its gross income from royalties?** A taxpayer earning gross income from royalties generated on or after June 1, 2010, must apportion such income when the taxpayer is taxable in another state. Gross income is apportioned to Washington by multiplying apportionable income by the receipts factor. The resulting amount of taxable income is then multiplied by the applicable tax rate.

(4) **What is the receipts factor?** The "receipts factor" is a fraction with the following numerator and denominator:

(a) Numerator: is the total gross income from royalties attributable to Washington during the tax year. Generally, a tax year is the same as a calendar year. For the purposes of this rule, tax years will be referred to as calendar years.

(b) Denominator: is the total gross income from royalties attributable to everywhere in the world during the calendar year, less amounts that are attributed to states where the taxpayer is not taxable if at least some of the apportionable activity is performed in Washington.

(5) **How are royalty receipts attributed to Washington?** To compute the numerator of the receipts factor, gross income from royalties is attributable to states as follows:

(a) Place of use: where the customer used the taxpayer's intangible property. If a taxpayer can reasonably determine the amount of royalty receipts related to the use in a state, that amount of royalty receipts is attributable to that state. This may be shown by application of a reasonable method of proportionally assigning the use of the intangible property among states.

(b) If a taxpayer is unable to separately determine the use of the intangible property in specific states under (a), and as a result the customer used the intangible property in multiple states, the royalty receipts are attributed to the state in which the intangible property was primarily used. Primarily means in this case more than 50%.

(c) Office of negotiation: if the taxpayer is unable to attribute gross income to a location under (a) or (b) of this subsection (5), then gross income must be attributed to the office of the customer from which the royalty agreement with the taxpayer was negotiated.

(d) Billing state: if the taxpayer is unable to attribute gross income to a location under (a), (b), or (c) of this subsection (5), then gross income must be attributed to the state to which the billing statement or invoices are sent to the customer by the taxpayer.

(e) Payment state: if the taxpayer is unable to attribute gross income to a location under (a), (b), (c), or (d) of this subsection (5), then gross income must be attributed to the state from which the customer sends payment to taxpayer.

(f) Customer's address: if the taxpayer is unable to attribute gross income under (a), (b), (c), (d), or (e) of this subsection (5), then gross income must be attributed to the state where the customer is located as indicated by customer's address:

(i) As shown in the taxpayer's business records maintained in the regular course of business; or

(ii) Obtained during negotiation of the contract for the use of the taxpayer's intangible property, including any address of a customer's payment instrument when readily available to the taxpayer and no other address is available.

(g) Taxpayer's domicile: if the taxpayer is unable to attribute gross income under (a), (b), (c), (d), (e), or (f) of this subsection (5), then gross income must be attributed to the commercial domicile of the taxpayer.

(6) **Examples.** Examples included in this subsection 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.

(a) **Example 1:** Taxpayer has its domicile in California and runs a national restaurant franchising business. Taxpayer enters into a contract with Company A under which Taxpayer licenses the right to use its trademark to Company A's so that Company A can display that trademark on its restaurant, menus, marketing materials, etc. Company A has a single restaurant that is located in Washington. Company A pays Taxpayer $500,000 per calendar year for the right to use the trademark at its restaurant in Washington. Pursuant to the first sourcing rule, the intangibles (trademark) are used in Washington. Therefore, Taxpayer would attribute the $500,000 in receipts from Company A to Washington.

(b) **Example 2:** Same facts as Example 1 except Company A in a single contract receives the right to use Taxpayer's trademark in as many restaurants as it wants in Washington and Idaho and pays $500,000 for each restaurant when the restaurant opens and each calendar year thereafter. Company A opens two restaurants in Idaho and one in Washington. Taxpayer would attribute $500,000 it received from Company A to Washington and $1,000,000 to Idaho.

(c) **Example 3**: Same facts as Example 1 above, except that Company A now has many locations in Idaho but still only one in Washington. Further, Company A enters into a new contract with Taxpayer under which Company A must now pay $1,500,000 per calendar year for the exclusive and unlimited right to the use of the trademark in Idaho but only a single location in Washington. Because the intangible is used in more than one state, but is primarily used in Idaho, Taxpayer would attribute all receipts received from Company A, (i.e. $1,500,000) to Idaho pursuant to the second sourcing rule.

(7) **What data can be used for calculating the receipts factor?**

(a) A taxpayer may calculate the receipts factor for the current calendar year based on the most recent calendar year for which information is available for the full calendar year. Taxpayers may refer to WAC 458-20-19402 for an example of the application of the use of the most current information available.

(b) If a taxpayer does not calculate the receipts factor for the current calendar year based on the previous calendar year information as authorized in this rule, the business must use current year information to calculate the receipts factor for the current tax year.

(c) In either case, a taxpayer must correct the reporting for the current calendar year when complete information is available to calculate the receipts factor for that year, but not later than October 31st of the following calendar year. Taxpayers may refer to WAC 458-20-19402 for an example of the reconciliation.

(8) **What interest applies to underpayments and overpayments?**

(a) Interest will apply to any additional tax due on a corrected tax return. Interest must be assessed at the rate provided for delinquent excise taxes under RCW 82.32.050 retroactively to the date the original return was due and will accrue until the additional taxes are paid.

(b) 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.

(9) **What penalties may apply?** Penalties as provided in RCW 82.32.090 will apply to any additional taxes due only if the current calendar year reporting is not corrected and the additional tax is not paid by October 31st of the following calendar year.

This rule was adopted on an emergency basis effective January 28, 2011. It may be used to determine tax liability until May 28, 2011, unless the Department adopts a permanent rule prior to this date.

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 RCW 82.04 if received from activities in this state, less the exemptions and deductions allowable under chapter RCW 82.04. 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 31th 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 (2) 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 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 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 Titles 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":

<u>(i)</u> 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 this subsection (3)(i) 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; 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.

(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 this subsection (3)(s), "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 (4)(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 (4)(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 section 112, chapter 23, Laws of 2010, 1st sp. sess. are not to be included in either numerator nor 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 (4) 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 (4) 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 (4) 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 (4) 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 (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.

(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 (4), 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 (4) 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 (4) 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 (4)), attributable to this state and included in the numerator is determined by multiplying the amount described in (k)(i)(B) of this subsection (4) 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 this subsection (4)(k)(ii), 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 (4), 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 (4) 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 (4)), attributable to this state and included in the numerator is determined by multiplying the amount described in (k)(i)(B) of this subsection (4) 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 (4), 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.

(l) 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.