RULE-MAKING ORDER

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

Agency: Department of Revenue

Permanent Rule Only

Effective date of rule:
Permanent Rules
☒ 31 days after filing.
☐ Other (specify) **(If less than 31 days after filing, a specific finding under RCW 34.05.380(3) is required and should be stated below)**

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

Purpose: WAC's 458-20-19401-19404 are amended to reflect the adoption of WAC 45-20-19405. WAC 458-20-19405 is adopted because RCW 82.04.067 requires the Department of Revenue every December to review the change in the Consumer Price Index and to adjust the thresholds whenever the cumulative change exceeds 5%.

Citation of existing rules affected by this order:
Repealed:
Amended: WAC 458-20-19401 - *Minimum nexus thresholds for apportionable activities;*
WAC 458-20-19402 - *Single factor receipts apportionment – Generally;*
WAC 458-20-19403 - *Apportionable royalty receipts attribution;*
WAC 458-20-19404 - *Financial institutions -- Income apportionment;*
WAC 458-20-19405 - *CPI-U Adjustments to Minimum Nexus Thresholds for Apportionable Activities*
Suspended:

Statutory authority for adoption: RCW 82.04.067, 82.32.300, and 82.01.060(2)

Other authority :

PERMANENT RULE (Including Expedited Rule Making)
Adopted under notice filed as WSR **13-17-124** on **August 21, 2013**.
Describe any changes other than editing from proposed to adopted version: None.

If a preliminary cost-benefit analysis was prepared under RCW 34.05.328, a final cost-benefit analysis is available by contacting: Not applicable.

Name: phone ( )
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Date adopted:
October 31, 2013

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CODE REVISER USE ONLY

OFFICE OF THE CODE REVISER
STATE OF WASHINGTON
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WSR 13-22-044

(COMPLETE REVERSE SIDE)

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Federal statute:	New	Amended	Repealed
Federal rules or standards:	New	Amended	Repealed
Recently enacted state statutes:	New	Amended	Repealed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 1 Amended 4 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

AMENDATORY SECTION (Amending WSR 11-19-038, filed 9/12/11, effective 10/13/11)

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 458-20-19405, CPI-U adjustments to minimum nexus thresholds for apportionable activities. This rule describes the minimum nexus thresholds adjustment that must be made to account for increases to the consumer price index for tax periods after May 31, 2010.

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

((~~(v)~~)) (vi) 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.

The minimum nexus thresholds described in this rule and used in examples are subject to change because of consumer price index changes. Refer to WAC 458-20-19405 for the current threshold amounts.

(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. <u>(See WAC 458-20-19405 for the current threshold amounts.)</u>

(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~~)) worldwide 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.

AMENDATORY SECTION (Amending WSR 12-19-071, filed 9/17/12, effective 10/18/12)

WAC 458-20-19402 Single factor receipts apportionment—Generally.

PART 1. INTRODUCTION.

(101) **General.** RCW 82.04.462 establishes the apportionment method for businesses engaged in apportionable activities and that have nexus with Washington for business and occupation (B&O) tax liability incurred after May 31, 2010. The express purpose of the change in the law was to require businesses "earn(ing) significant income from Washington residents from providing services" to "pay their fair share of the cost of services that this state renders and the infrastructure it provides." Section 101, chapter 23, 1st special session, 2010.

(102) **Guide to this rule.** This rule is divided into six parts, as follows:

1. Introduction.
2. Overview of single factor receipts apportionment.
3. How to attribute receipts.
4. Receipts factor.
5. How to determine Washington taxable income.
6. Reporting instructions.

(103) **Scope of rule.** This rule applies to the apportionment of income from engaging in apportionable activities as defined in WAC 458-20-19401, except:

(a) To the apportionment of income received by financial institutions and taxable under RCW 82.04.290, which is governed by WAC 458-20-19404; and

(b) To the attribution of royalty income from granting the right to use intangible property, which is governed by WAC 458-20-19403.

(104) **Separate accounting and cost apportionment.** The apportionment method explained in this rule replaces the previously allowed separate accounting and cost apportionment methods. Separate accounting and cost apportionment are not authorized for periods after May 31, 2010.

(105) **Other rules.** Taxpayers may also find helpful information in the following rules:

(a) WAC 458-20-19401 **Minimum nexus thresholds for apportionable activities.** This rule describes minimum nexus thresholds applicable to apportionable activities that are effective after May 31, 2010.

(b) WAC 458-20-19403 **Royalty receipts attribution.** This rule describes the attribution of royalty income for the purposes of single factor receipts apportionment and applies only to tax liability incurred after May 31, 2010.

(c) 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.

(d) WAC 458-20-19405, CPI-U adjustments to minimum nexus thresholds for apportionable activities. This rule describes the minimum nexus thresholds adjustment that must be made to account for increases to the consumer price index for tax periods after May 31, 2010.

(e) 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.

((~~(e)~~)) (f) 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.

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

(a) **"Apportionable activities"** has the same meaning as used in WAC 458-20-19401 Minimum nexus thresholds for apportionable activities.

(b) **"Apportionable income"** means apportionable receipts less the deductions allowable under chapter 82.04 RCW.

(c) **"Apportionable receipts"** means gross income of the business from engaging in apportionable activities, including income received from apportionable activities attributed to locations outside this state.

(d) **"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. In the case of sole proprietorships and pass-through entities, 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 retail sales, use, or similar transaction taxes, imposed on the sale or acquisition of goods or services, whether or not named a gross receipts tax or a tax imposed on the privilege of doing business.

(e) **"Customer"** means a person or entity to whom the taxpayer makes a sale, grants the right to use intangible property, or renders services or from whom the taxpayer otherwise directly or indirectly receives gross income of the business. If the taxpayer performs apportionable services for the benefit of a third party, the term "customer" means the third party beneficiary.

Example 1. Assume a parent purchases apportionable services for their child. The child is the customer for the purpose of determining where the benefit is received.

(f) **"Reasonable method of proportionally attributing"** means a method of determining where the benefit of an activity is received and where the receipts are attributed that is uniform, consistent, and accurately reflects the market, and does not distort the taxpayer's market.

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

(A) The taxpayer is subject to a business activities tax by another state on the taxpayer's income received from engaging in apportionable activity; or

(B) The taxpayer is not subject to a business activities tax by another state on the taxpayer's income received from engaging in apportionable activity, but the taxpayer meets the substantial nexus thresholds described in WAC 458-20-19401 for that state.

(ii) The determination of whether a taxpayer is taxable in a foreign country or political subdivision of a foreign country is made at the country or political subdivision level.

Example 2. Assume Taxpayer A is subject to a business activity tax in State X of Mexico (e.g., Taxpayer pays tax to State X), but no-where else in Mexico. Also, assume that Taxpayer A is not subject to any national business activity tax in Mexico and does not meet the substantial nexus thresholds described in WAC 458-20-19401 for Mexico as a whole. In this case, Taxpayer is taxable in State X, but not taxable in any other portion or any other State of Mexico.

Example 3. Assume Taxpayer B is not subject to any business activity taxes in Mexico, but satisfies the substantial nexus thresholds described in WAC 458-20-19401 for Mexico as a whole. Taxpayer B is taxable in all of Mexico.

PART 2. OVERVIEW OF SINGLE FACTOR RECEIPTS APPORTIONMENT.

(201) **Single factor receipts apportionment generally.** Except as provided in WAC 458-20-19404 persons earning apportionable income who have substantial nexus with Washington as specified in WAC 458-20-19401 and who are also taxable in another state must use the apportionment method provided in this rule to determine their taxable income from apportionable activities for B&O tax purposes. Taxable income is determined by multiplying apportionable income from each apportionable activity by the receipts factor for that apportionable activity.

This formula is:

(Taxable income) = **(Apportionable income)** x **(Receipts factor)**

See Part 4 of this rule for a discussion of the receipts factor.

(202) **Tax year.** The receipts factor applies to each tax year. A tax year is the calendar year, unless the taxpayer has specific permission from the department to use another period. (RCW 82.32.270.) For the purposes of this rule, "tax year" and "calendar year" have the same meaning.

PART 3. HOW TO ATTRIBUTE RECEIPTS.

(301) **Attribution of receipts generally.** Except as specifically provided for in WAC 458-20-19403 for the attribution of apportionable royalty receipts, this Part 3 explains how to attribute apportionable receipts. Receipts are attributed to states based on a cascading method or series of steps. The department expects that most taxpayers will attribute apportionable receipts based on (a)(i) of this subsection because the department believes that either the taxpayer will know where the benefit is actually received or a "reasonable method of pro-

portionally attributing receipts" will generally be available. These steps are:

(a) Where the customer received the benefit of the taxpayer's service (see subsection (302) of this rule for an explanation and examples of the benefit of the service);

(i) If a taxpayer can reasonably determine the amount of a specific apportionable receipt that relates to a specific benefit of the services received in a state, that apportionable receipt is attributable to the state in which the benefit is received. This may be shown by application of a reasonable method of proportionally attributing the benefit among states. The result determines the receipts attributed to each state. Under certain situations, the use of data based on an attribution method specified in (b) through (f) of this subsection may also be a reasonable method of proportionally attributing receipts among states (see Examples 4 and 5 below).

(ii) If a taxpayer is unable to separately determine or use a reasonable method of proportionally attributing the benefit of the services in specific states under (a)(i) of this subsection, and the customer received the benefit of the service in multiple states, the apportionable receipt is attributed to the state in which the benefit of the service was primarily received. Primarily means, in this case, more than fifty percent.

(b) If the taxpayer is unable to attribute an apportionable receipt under (a) of this subsection, the apportionable receipt must be attributed to the state from which the customer ordered the service.

(c) If the taxpayer is unable to attribute an apportionable receipt under (a) or (b) of this subsection, the apportionable receipt must be attributed to the state to which the billing statements or invoices are sent to the customer by the taxpayer.

(d) If the taxpayer is unable to attribute an apportionable receipt under (a), (b), or (c) of this subsection, the apportionable receipt must be attributed to the state from which the customer sends payment to the taxpayer.

(e) If the taxpayer is unable to attribute an apportionable receipt under (a), (b), (c), or (d) of this subsection, the apportionable receipt 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, including any address of a customer's payment instrument when readily available to the taxpayer and no other address is available.

(f) If the taxpayer is unable to attribute an apportionable receipt under (a), (b), (c), (d), or (e) of this subsection, the apportionable receipt must be attributed to the commercial domicile of the taxpayer.

(g) The taxpayer may not use an attribution method that distorts the apportionment of the taxpayer's apportionable receipts.

(302) **Examples.** 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. The examples in this rule assume all gross income received by the taxpayer is from engaging in apportionable activities. Unless otherwise stated, the examples do not apply to tax liability prior to June 1, 2010.

When an example states that a particular attribution method is a reasonable method of proportionally attributing the benefit of a service, this does not preclude the existence of other reasonable methods of proportionally attributing the benefit depending on the specific facts and circumstances of a taxpayer's situation.

Example 4. Assume Law Firm has thousands of charges to clients. It is not commercially reasonable for Law Firm to track each charge to each client to determine where the benefit related to each service is received. Assume the scope of Law Firm's practice is such that it is reasonable to assume that the benefits of Law Firm's services are received at the location of the customer as reflected by the customer's billing address. Under these circumstances, Law Firm can use the billing addresses of each client as a reasonable method of proportionally attributing the benefit of its services.

Example 5. Same facts as Example 4 except, Law Firm has a single client that represents a statistically significant portion of its revenue and whose billing address is unrelated to any of the services provided. In this case, using the billing address of this client would not relate to the benefit of the services. Using the billing address for this client to determine where the benefit is received would significantly distort the apportionment of Law Firm's receipts. Therefore, Law Firm would need to evaluate the specific services provided to that client to determine where the benefits of those services are received and may use billing address to attribute the income received from other clients.

Example 6. Assume Taxpayer R attributes an apportionable receipt based on its customer's billing address, using (c) of this subsection, and the billing address is a P.O. Box located in another state. Taxpayer R also knows that mail delivered to this P.O. Box is automatically forwarded to the customer's actual location. In this case, use of the billing address is not allowed because it would distort the apportionment of Taxpayer R's receipts.

(303) **Benefit of the service explained.** The first two steps (subsection (301)(a)(i) and (ii) of this rule) used to attribute apportionable receipts to a state are based on where the taxpayer's customer receives the benefit of the service. This subsection explains the framework for determining where the benefit of a service is received.

(a) **If the taxpayer's service relates to real property, then the benefit is received where the real property is located.** The following is a nonexclusive list of services that relate to real property:

(i) Architectural;

(ii) Surveying;

(iii) Janitorial;

(iv) Security;

(v) Appraisals; and

(vi) Real estate brokerage.

(b) **If the taxpayer's service relates to tangible personal property, then the benefit is received where the tangible personal property is located or intended/expected to be located.**

(i) Tangible personal property is generally treated as located where the place of principal use occurs. If the tangible personal property is subject to state licensing (e.g., motor vehicles), the principal place of use is presumed to be where the property is licensed; or

(ii) If the tangible personal property will be created or delivered in the future, the principal place of use is where it is expected to be used or delivered.

(iii) The following is a nonexclusive list of services that relate to tangible personal property:

(A) Designing specific/unique tangible personal property;

(B) Appraisals;

(C) Inspections of the tangible personal property;

(D) Testing of the tangible personal property;

(E) Veterinary services; and

(F) Commission sales of tangible personal property.

(c) **If the taxpayer's service does not relate to real or tangible personal property, the service is provided to a customer engaged in business, and the service relates to the customer's business activities, then the benefit is received where the customer's related business activities occur.** The following is a nonexclusive list of business related services:

(i) Developing a business management plan;

(ii) Commission sales (other than sales of real or tangible personal property);

(iii) Debt collection services;

(iv) Legal and accounting services not specific to real or tangible personal property;

(v) Advertising services; and

(vi) Theatre presentations.

(d) **If the taxpayer's service does not relate to real or tangible personal property, is either provided to a customer not engaged in business or unrelated to the customer's business activities((~~,~~)); and:**

(i) The service requires the customer to be physically present, then the benefit is received where the customer is located when the service is performed. The following is a nonexclusive list of services that require the customer to be physically present:

(A) Medical examinations;

(B) Hospital stays;

(C) Haircuts; and

(D) Massage services.

(ii) The taxpayer's service relates to a specific, known location(s), then the benefit is received at those location(s). The following is a nonexclusive list of services related to specific, known location(s):

(A) Wedding planning;

(B) Receptions;

(C) Party planning;

(D) Travel agent and tour operator services; and

(E) Preparing and/or filing state and local tax returns.

(iii) If (d)(i) and (ii) of this subsection do not apply, the benefit of the service is received where the customer resides. The following is a nonexclusive list of services whose benefit is received at the customer's residence:

(A) Drafting a will;

(B) Preparing and/or filing federal tax returns;

(C) Selling investments; and

(D) Blood tests (not blood drawing).

(e) **Special rule for extension of credit.** See subsection ((~~(304)~~)) (305) of this rule for special rules attributing income related to loans (secured and unsecured) and credit cards that is received by persons who are not financial institutions as defined in WAC 458-20-19404.

(304) **Examples of the application of the benefit of service analysis and reasonable methods of proportionally attributing receipts.**

(a) **Services related to real property:**

Example 7. Architect drafts plans for a building to be built in Washington. Architect's services relate to real property which is located in Washington, therefore the customer receives the benefit of that service in Washington at the location of the real property. Architect's receipts for this service are solely attributed to Washington because the entire benefit is received in Washington.

Example 8. Franchisor hires Taxpayer, an architect, to create a design of a standardized building that will be used at four locations in Washington and two locations in Oregon. Taxpayer's services relate to real property at those six locations, therefore the customer receives the benefit of the service at the four Washington locations and the two Oregon locations. Taxpayer will attribute 2/3 (4 of 6 sites) of the receipts for this service to Washington and 1/3 (2 of 6 sites) of the receipts to Oregon.

Example 9. Assume the same facts as Example 8 except Franchisor will use the same design in all 50 states for all its franchisee's locations. Taxpayer and Franchisor do not know at the time the service is provided (and cannot reasonably estimate) how many franchise locations will exist in each state. Therefore, there is no reasonable means of proportionally attributing receipts at the time the services are performed and it is clear that no state will have a majority of the franchise locations. Accordingly, the apportionable receipts must be attributed following the steps in subsection (301)(b) through (f) of this rule.

Example 10. Real estate broker located in Florida receives a commission for arranging the sale of real property located in Washington. The real estate broker's service is related to the real property, therefore the benefit is received in Washington, where the real property is located, and the commission income is attributed to Washington.

(b) **Services related to tangible personal property.**

Example 11. Big Manufacturing hires an engineer to design a tool that will only be used in a factory located in Brewster, Washington. Big Manufacturing receives the benefit of the engineer's services at a single location in Washington where the tool is intended to be used. Therefore, 100% of engineer's receipts from this service must be attributed to Washington.

Example 12. The same facts as in Example 11, except Big Manufacturing will use the tool equally in factories located in Brewster and in Kapa'a, Hawai'i. Therefore, Big Manufacturer receives the benefit of the service equally in two states. Because the benefit of the service is received equally in both states, a reasonable method of proportionally attributing receipts would be to attribute 1/2 of the receipts to each state.

Example 13. Taxpayer, a commissioned salesperson, sells tangible personal property (100 widgets) for Distributor to XYZ Company for delivery to Spokane. Distributor receives the benefit of Taxpayer's service where the tangible personal property will be delivered. Therefore, Taxpayer will attribute the commission from this sale to Washington.

Example 14. Same facts as in Example 13, but the widgets are to be delivered 50 to Spokane, 25 to Idaho, and 25 to Oregon. In this case, the benefit is received in all three states. Taxpayer shall attribute the receipts (commission) from this sale 50% to Washington, 25% to Idaho, and 25% to Oregon where the tangible personal property is delivered to the buyer.

Example 15. Training Company provides training to Customer's employees on how to operate a specific piece of equipment used solely in Washington. Customer receives the benefit of the service where the equipment is used, which is in Washington. Therefore, Training Company will attribute 100% of its receipts received from Customer to Washington.

(c) **Services related to customer's business activities.** The examples in this subsection assume that the customer is engaged in business and the services relate to the customer's business activities.

Example 16. Manufacturer hires Law Firm to defend Manufacturer in a class action product liability lawsuit involving Manufacturer's Widgets. The benefit of Law Firm's services relates to Manufacturer's widget selling activity in various states. A reasonable method of proportionally attributing receipts in this case would be to attribute the receipts to the locations where the Manufacturer's Widgets were delivered, which relates to Manufacturer's business activities.

Example 17. Debt Collector provides debt collection services to ABC. The benefit of Debt Collector's services relates to ABC's selling activity in various states. It is reasonable to assume that where the debtors are located is the same as where ABC's business activity occurred. If Debt Collector is able to attribute specific receipts to a specific debtor, then the receipt is attributed to where the debtor is located.

Example 18. Same facts as Example 17, except Debt Collector is unable to attribute specific benefits with specific debtors. In this case, a reasonable method of proportionally attributing benefits/receipts should be employed. Depending on Debt Collector's specific facts and circumstances, a reasonable method of proportionally attributing benefits/receipts could be: Relative number of debtors in each state; relative debt actually collected from debtors in each state; the relative amount of debt owed by debtors in each state; or another method that does not distort the apportionment of Debt Collector's receipts.

Example 19. Training Company provides training to Customer's employees who are all located in State A. The training is provided in State B. The training relates to the employees' ethical behavior within Customer's organization. Customer receives the benefit of Training Company's service in State A, where Customer's office is located and the employees presumably practice their ethical behavior. Training Company must attribute the apportionable receipts to State A where the benefit is solely received.

Example 20. Same facts as Example 19, except the training is provided for employees from several states and Training Company knows where each employee works. The benefit of the Training Company's services is received in those several states. Attributing receipts from the training based on where the employees work is a reasonable method of proportionally attributing the receipts income.

Example 21. Call Center provides "customer service" services to Retailer who has customers in all 50 states. Call Center's services relate to Retailer's selling activity in all 50 states, therefore Retailer receives the benefit of Call Center's services in all 50 states. Call Center has offices in Iowa and Alabama that answer questions about Retailer's products. Call Center records Retailer's customer's calls by area code. Call Center may attribute receipts received from Retailer based on the number of calls from area codes assigned to each state. This would be a reasonable method of proportionally attributing receipts notwithstanding the fact that mobile phone numbers and related area codes may not exactly reflect the physical location of the customer in all cases.

Example 22. Taxpayer provides internet advertising services to national retail chains, regional businesses, businesses with a single location, and businesses that operate solely over the Internet. Generally, the benefit of the advertising services is received where the customer's related business activities occur. Depending on what products or services are being provided by Taxpayer's customers, the use of relative population in the customer's market may be a reasonable method of proportionally attributing the benefit of Taxpayer's services.

Example 23. Oregon Newspaper sells newspaper advertising to Merlin's Potion Shop. Merlin's only makes over-the-counter sales from its single location in Vancouver, Washington. Merlin's Potion Shop receives the benefit of the Oregon Newspaper's advertising services in Washington where it makes sales to its customers. In this case Oregon Newspaper will report 100% of its receipts received from Merlin's to Washington.

Example 24. Company A provides human resources services to Racko, Inc. which has three offices that use those services in Washington, Oregon, and Idaho. Racko sells widgets and has customers for its widgets in all 50 states. The benefit of the service performed by Company A is received at Racko's locations in Washington, Oregon, and Idaho. Assuming that each office is approximately the same size and uses the services to approximately the same extent, then attributing 1/3 of the receipts to each of the states in which Racko has locations using the services is a reasonable method of proportionally attributing Company A's receipts from Racko.

Example 25. Director serves on the board of directors for DEF, Inc. Director's services relate to the general management of DEF, Inc. DEF, Inc. is Director's customer and receives the benefit of Director's services at its corporate domicile. Therefore, Director must attribute the receipts earned from Director's services to DEF to DEF's corporate domicile.

(d) **Services not related to real or tangible personal property and either provided to customers not engaged in business or unrelated to the customer's business activities.**

Example 26. A Washington resident travels to California for a medical procedure. Because the Washington resident must be physically in California, the Washington resident receives the benefit of the service in California. Therefore, the service provider must attribute its income from the procedure to California.

Example 27. Washington accountant prepares a Nevada couple's Arizona and Oregon state income tax returns as well as their federal income tax return. The benefit of the accountant's service associated with the state income tax returns is attributed to Arizona and Oregon because these returns relate to specific locations (states). The benefit associated with the federal income tax return is attributed to the couple's residence. The fees for the state tax returns are attributed to Arizona and Oregon, respectively, and the fee for the federal income tax return is attributed to Nevada.

Example 28. Tour Operator provides cruises through Washington's San Juan Islands for four days and Victoria, British Columbia for one day. The benefit of the tour is received where the tour occurs. Tour Operator may use a reasonable method of proportionally attributing the benefit to determine that its customers receive 80% of the benefit in Washington and 20% outside of Washington. Therefore, Tour Operator must attribute 80% of apportionable receipts to Washington and 20% to British Columbia.

Example 29. A Washington couple hires a Washington attorney to prepare a last will and testament for Daughter who lives in California. Daughter is a third-party beneficiary and receives the benefit of the attorney's services in California because that is where Daughter lives. Washington Attorney must attribute the fee to California.

Example 30. A Washington couple hires a California accountant to prepare their joint federal income tax return. Because the couple does not have to be physically present for the accountant to perform services and services are not related to a specific location, the Washington couple receives the benefit of the accountant's services at their residence in Washington. California accountant must attribute its fee for this service to Washington.

Example 31. An Arizona resident retains a Washington stock broker to handle its investments. The stock broker receives orders from the client and executes trades of securities on the New York Stock Exchange. Because (a) the Arizona resident is not investing as part of a business; (b) the activity does not relate to real or tangible personal property; (c) and the client does not need to be physically present for the stock broker to perform its services; and (d) the services are not related to a specific location, the client receives the benefit of the services at client's place of residence. Washington stockbroker must attribute the fee to Arizona.

Example 32. Investment Manager manages a mutual fund. Investment Manager receives a fee for managing the fund based on the value of the assets in the fund on particular days. Investment Manager knows or should know the identity of the investors in the fund and their mailing addresses. The fees received by Investment Manager (whether from the mutual fund or from individual investor's accounts) are for the services provided to the investors. Investment Manager's services do not relate to real or tangible personal property and do not require that the client be physically present, therefore, the benefit of Investment Manager's services is received where the investors are located and Investment Manager's apportionable receipts must be attributed to those locations.

(305) **Special rules related to extending credit performed by nonfinancial institutions.** Businesses not included in the definition of a financial institution under WAC 458-20-19404 that provide services related to the extension of credit must attribute their income from such activities as follows:

(a) **Activities related to extending credit where real property secures the debt.** Such activities include, but are not limited to, servicing loans, making loans subject to deeds of trust or mortgages (including any fees in the nature of interest related to the loan), and buying and selling loans. Apportionable receipts from these activities are attributed in the same manner as a financial institution attributes these apportionable receipts under WAC 458-20-19404.

(b) **Activities related to credit cards.** Such activities include, but are not limited to, issuing credit cards, servicing, and billing. Apportionable receipts from these activities are attributed to the billing address of the card holder.

(c) **Other activities related to extending credit where real property does not secure the debt.** Such activities include, but are not limited to, servicing loans, making loans (including any fees related to such loans), and buying and selling loans. Apportionable receipts from these activities are attributed in the same manner a financial institution attributes income under WAC 458-20-19404.

(d) **All other apportionable receipts from such businesses are attributed using subsections (301) through (304) of this rule or WAC 458-20-19403.**

(306) **What does "unable to attribute" mean?** A taxpayer is "unable to attribute" apportionable receipts when the taxpayer has no commercially reasonable means to acquire the information necessary to attribute the apportionable receipts. Cost and time may be considered to determine whether a taxpayer has no commercially reasonable means to acquire the information necessary to attribute apportionable receipts.

Example 33. One office of ZYX LLC has information that can easily be used to determine a reasonable proportional attribution of receipts, but does not provide this information to the office preparing the tax returns. ZYX LLC must use the information maintained by the marketing office to attribute its receipts.

Example 34. CBA, Inc. is entitled to receive information from an affiliate or unrelated third party which it could use to determine where the benefit of its services is received but chooses not to obtain that information. CBA, Inc. must use the information maintained by the affiliate or unrelated third party to attribute its apportionable receipts.

Example 35. Same facts as Example 34, except that the information is raw data that must be formatted and otherwise processed at a cost that exceeds a reasonable estimate of the possible difference in the amount of tax CBA, Inc. would owe if used another attribution method authorized in subsection 301(b) through (f). In this case, it is not commercially reasonable for CBA, Inc. to use this data to determine where to attribute its income.

PART 4. RECEIPTS FACTOR.

(401) **General.** The receipts factor is a fraction that applies to apportionable income for each calendar year. Taxpayers must calculate a separate receipts factor for each apportionable activity (business and occupation tax classification) engaged in.

(402) **Receipts factor calculation.** The receipts factor is: Washington attributed apportionable receipts divided by world-wide apportionable receipts less throw-out income (see subsection (403) of this section). The receipts factor expressed algebraically is:

$$\textbf{(Receipts factor)} = \frac{\textbf{(Washington apportionable receipts)}}{\textbf{((((}\cancel{\textbf{World-wide}}\textbf{))}\ \underline{\textbf{worldwide}}\ \textbf{apportionable receipts) - (Throw-out income))}}$$

(a) The numerator of the receipts factor is: The total apportionable receipts attributable to Washington during the calendar year from engaging in the apportionable activity.

(b) The denominator of the receipts factor is: The total (((~~world-wide~~)) worldwide, including Washington) apportionable receipts from engaging in the apportionable activity during the calendar year, less throw-out income.

Example 36. NOP, Inc. has $400,000 of receipts attributed to Washington and $1,000,000 of ((~~world-wide~~)) worldwide receipts. Assuming that there is no throw-out income, NOP's receipts factor is 40% (400,000/1,000,000).

(c) In the very rare situation where the receipts factor (after reducing the denominator by the throw-out income) is zero divided by zero, the receipts factor is deemed to be zero.

(403) **Throw-out income.** Throw-out income includes all apportionable receipts attributed to states where the taxpayer:

(a) Is not taxable (see subsection (107) of this rule); and

(b) At least part of the activity of the taxpayer related to the throw-out income is performed in Washington.

Example 37. XYZ Corp. performs all services in Washington and has apportionable receipts attributed using the criteria listed in subsections (301) through (305) of this rule or WAC 458-20-19403 as follows: Washington $500,000; Idaho $200,000; Oregon $100,000; and California $300,000. XYZ Corp. is subject to Oregon and Idaho corporate income tax, but does not owe any California business activities taxes. XYZ does not have any throw-out income because Oregon and Idaho impose a business activities tax on its activities and it is deemed to be taxable in California because it satisfies the minimum nexus standards explained in WAC 458-20-19401 (more than $250,000 in receipts). XYZ's receipts factor is: 500,000/1,100,000 or 45.45%.

Example 38. Same facts as Example 37 except Idaho does not impose any tax on XYZ Corp. The $200,000 attributed to Idaho is throw-out income that is excluded from the denominator because: XYZ Corp. is not subject to Idaho business activities taxes; does not have substantial nexus with Idaho under Washington standards; and performs in Washington at least part of the activities related to the receipts attributed to Idaho. The receipts factor is 500,000/900,000 or 55.56%.

Example 39. The same facts as Example 38 except XYZ Corp. performs no activities in Washington related to the $200,000 attributed to Idaho. In this situation, the $200,000 is not throw-out income and remains in the denominator. The receipts factor is: 500,000/1,100,000 or 45.45%.

PART 5. HOW TO DETERMINE WASHINGTON TAXABLE INCOME.

(501) **General.** Washington taxable income is determined by multiplying apportionable income by the receipts factor for each apportionable activity the taxpayer engages in. While the receipts factor is calculated without regard to deductions authorized under

chapter 82.04 RCW, apportionable income is determined by reducing the apportionable receipts by amounts that are deductible under chapter 82.04 RCW regardless of where the deduction may be attributed. This formula can be expressed algebraically as:

(Taxable Income)	=	(Receipts Factor)	x	(Apportionable receipts - deductions)

Example 40. Calculating apportionable income. Corporation A received $2,000,000 in apportionable receipts from its ((~~world-wide~~)) worldwide apportionable activities, which included $500,000 of receipts that are deductible under Washington law. Corporation A's total apportionable income is $1,500,000 ($2,000,000 minus $500,000 of deductions). If Corporation A's receipts factor is 31.25%, then its taxable income is $468,750 ($1,500,000 multiplied by 0.3125).

PART 6. REPORTING INSTRUCTIONS.

(601) **General.**

(a) Taxpayers required to use this rule's apportionment method may report their taxable income based on their apportionable income for the reporting period multiplied by the receipts factor for the most recent calendar year the taxpayer has available.

(b) If a taxpayer does not calculate its taxable income using (a) of this subsection, the taxpayer must use actual current calendar year information.

(602) **Reconciliation.** Regardless of how a taxpayer reports its taxable income under subsection (601)(a) or (b) of this rule, when the taxpayer has the information to determine the receipts factor for an entire calendar year, it must file a reconciliation and either obtain a refund or pay any additional tax due. The reconciliation must be filed on a form approved by the department. In either event (refund or additional taxes due), interest will apply in a manner consistent with tax assessments. If the reconciliation is completed prior to October 31st of the following year, no penalties will apply to any additional tax that may be due.

AMENDATORY SECTION (Amending WSR 12-19-072, filed 9/17/12, effective 10/18/12)

WAC 458-20-19403 Apportionable royalty receipts attribution.

PART 1. INTRODUCTION.

(101) **General.** Effective June 1, 2010, Washington changed its method of apportioning royalty receipts. This rule only addresses how apportionable royalty receipts must be attributed for the purposes of economic nexus and single factor receipts apportionment. This rule is limited to the attribution of apportionable royalty receipts for periods after May 31, 2010.

(102) **Guide to this rule.** This rule is divided into two parts as follows:

1. Introduction.
2. How to attribute apportionable royalty receipts.

(103) **Reference to WAC 458-20-19402.** This rule only provides a method to attribute apportionable royalty receipts in lieu of the attribution methods specified in WAC 458-20-19402 (301)(a) and (b). Otherwise, WAC 458-20-19402 controls the apportionment of royalty receipts. Specifically, WAC 458-20-19402 provides: (a) An overview of single factor receipts apportionment (Part 2); (b) guidance on how to attribute apportionable royalty receipts if this rule does not apply (Part 3); (c) guidance on how to calculate the receipts factor (Part 4); (d) guidance on how to determine taxable income (Part 5); and (e) reporting instructions (Part 6).

(104) **Other rules.** Taxpayers may also find helpful information in the following rules:

(a) WAC 458-20-19401 **Minimum nexus thresholds for apportionable activities.** This rule describes minimum nexus thresholds applicable to apportionable activities that are effective after May 31, 2010.

(b) 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.

(c) 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.

(d) WAC 458-20-19405, CPI-U adjustments to minimum nexus thresholds for apportionable activities. This rule describes the minimum nexus thresholds adjustment that must be made to account for increases to the consumer price index for tax periods after May 31, 2010.

(e)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.

((~~(e)~~)) (f) 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.

(105) **Examples.** 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. The examples in this rule assume all gross income received by the taxpayer is apportionable royalty receipts. Unless otherwise stated, the examples do not apply to tax liability prior to June 1, 2010.

When an example states that a particular attribution method is a reasonable method of proportionally attributing the use of an intangible, this does not preclude the existence of other reasonable methods of proportionally attributing the use depending on the specific facts and circumstances of a taxpayer's situation.

(106) **Definitions.** The definitions included in WAC 458-20-19401 and 458-20-19402 apply to this rule unless the context clearly requires otherwise. Additionally, the definitions in this subsection apply specifically to this rule.

(a) **"Apportionable royalty receipts"** means all compensation for the use of intangible property, including charges in the nature of royalties, regardless of where the intangible property will be used. Apportionable royalty receipts does not include:

(i) Compensation for any natural resources;

(ii) The licensing of prewritten computer software to an end user;

(iii) The licensing of digital goods, digital codes, or digital automated services to an end user as defined in RCW 82.04.190(11); or

(iv) Receipts from the outright sale of intangible property.

(b) **"Intangible property"** includes: Copyrights, patents, licenses, franchises, trademarks, trade names, and other similar intangible property/rights.

(c) **"Reasonable method of proportionally attributing"** means a method of determining where the use occurs, and thus where receipts are attributed that is uniform, consistent, accurately reflects the market, and is not distortive.

PART 2. HOW TO ATTRIBUTE APPORTIONABLE ROYALTY RECEIPTS.

(201) **Attribution of income.** Apportionable royalty receipts are attributed to states based on a cascading method or series of steps. The department expects that most taxpayers will attribute apportionable royalty receipts based on (a)(i) of this subsection because the department believes that either taxpayers will know the place of use or a "reasonable method of proportionally attributing" receipts will generally be available. These steps are:

(a) **Where the customer uses the intangible property.**

(i) If a taxpayer can reasonably determine the amount of a specific apportionable royalty receipt that relates to a specific use in a state, that royalty receipt is attributable to that state. This may be shown by application of a reasonable method of proportionally attributing use, and thus receipts, among the states. The result determines the apportionable royalty receipts attributed to each state. Under certain situations, the use of data based on an attribution method specified in (b) and (c) of this subsection may also be a reasonable method of proportionally attributing receipts among states.

(ii) If a taxpayer is unable to separately determine, or use a reasonable method of proportionally attributing, the use and receipts in specific states under (a)(i) of this subsection, and the customer used the intangible property in multiple states, the apportionable royalty receipts are attributed to the state in which the intangible property was primarily used. Primarily means, in this case, more than fifty percent.

(b) **Office of negotiation.** If the taxpayer is unable to attribute apportionable royalty receipts to a location under (a) of this subsection, then apportionable royalty receipts must be attributed to the office of the customer from which the royalty agreement with the taxpayer was negotiated.

(c) If the taxpayer is unable to attribute apportionable royalty receipts to a location under (a) and (b) of this subsection, then the steps specified in WAC 458-20-19402 (301)(c) through (g) shall apply to apportionable royalty receipts.

(202) **Framework for analysis of the "use of intangible property."** The use of intangible property and therefore the attribution of apportionable royalty receipts from the use of intangible property will generally fall into one of the following three categories:

(a) **Marketing use** means the intangible property is used by the taxpayer's customer for purposes that include, but are not limited to, marketing, displaying, selling, and exhibiting. The use of the intangible property is connected to the sale of goods or services. Typically, this category includes trademarks, copyrights, trade names, logos, or other intangibles with promotional value. Receipts from the marketing use of intangible property are generally attributed to the location of the consumer of the goods or services promoted using the intangible property.

Example 1. SportsCo licenses to AthleticCo the right to use its trademark on a basketball that AthleticCo manufactures, markets, and sells at retail on its web site. This is a marketing use. SportsCo is paid a fee based on AthleticCo's basketball sales in multiple states. SportsCo knows that sales from the AthleticCo web site delivered to Washington represent 10% of AthleticCo's total sales. Pursuant to subsection (201)(a)(i) of this section, SportsCo will attribute 10% of its apportionable royalty receipts received from AthleticCo to Washington. The remaining 90% will be attributed to other states.

Example 2. Same facts as Example 1, except that AthleticCo sells its basketballs at wholesale to MiddleCo, a distributor with its receiving warehouse located in Idaho. MiddleCo then sells the basketballs to RetailW, a retailer with stores in Washington, Oregon, and California. SportsCo would generally attribute its apportionable royalty receipts to the location of RetailW's customers. However, SportsCo does not have any data, and cannot reasonably obtain any data, relating to RetailW's customer locations. Pursuant to subsection (201)(a)(i) of this section, SportsCo may reasonably attribute receipts to Washington based on the percentage of RetailW's store locations in Washington as long as such attribution does not distort the number of customers in each state. SportsCo knows that 15% of RetailW's store locations are in Washington therefore it is reasonable for SportsCo to attribute 15% of its apportionable royalty receipts to Washington. The remaining 85% will be attributed to other states.

Example 3. MusicCo licenses to RetailCo the right to make copies of a digital song and sell those copies at retail on the internet for the U.S. market only. This is a marketing use. RetailCo has a single copy of the song on its server in Virginia. Each time a customer comes to RetailCo's web site and makes a purchase of the song, RetailCo creates a copy of the song (e.g., a new file) that is then available for sale to the customer. MusicCo would usually attribute its apportionable royalty receipts to the location of RetailCo's customers. However, MusicCo does not have any data, and cannot reasonably obtain any specific data, relating to RetailCo's customers' locations. Pursuant to subsection (201)(a)(i) of this section, MusicCo may reasonably attribute receipts to each state based on the percentage that each state's population represents in relation to the total market population, which in this case is the U.S. population, as long as such attribution does not distort the number of customers in each state.

Example 4. A local baseball star, Joe Ball, plays for a professional athletic franchise located in Washington. Joe Ball licenses to T-ShirtCo the right to put his image on t-shirts and sell them on the internet in the U.S. market. This is a marketing use limited to the U.S. by license. Joe Ball does not know where T-ShirtCo's customers are located and cannot reasonably obtain data to reasonably attribute receipts. In the absence of actual sales data from T-ShirtCo, Joe Ball cannot use relative population data to attribute receipts to the states as was done in Example 3 above. This is because Joe Ball is an overwhelmingly "local" celebrity in Washington. Joe Ball does not have a "national appeal" such that t-shirt sales by T-ShirtCo would be significant outside Washington. In this case, Joe Ball is unable to separately determine the use of the intangible property in specific states pursuant to subsection (201)(a)(i) of this section. However, it is reasonable for Joe Ball to assume that sales by T-ShirtCo of Joe Ball shirts are primarily delivered to customers in Washington. Accordingly, Joe Ball should assign all receipts received from T-ShirtCo to Washington, pursuant to subsection (201)(a)(ii) of this section.

Example 5. MegaComputer ("Mega") manufactures and sells computers. SoftwareCo licenses to MegaComputer the right to copy and install the software on Mega's computers, which are then offered for sale to consumers. This is a marketing use by Mega. Mega sells its computers to DistributorX that in turn sells the computers to RetailerY. Mega uses the intangible property at the location of the consumer. If SoftwareCo can attribute its receipts to the location of the consumer (e.g., through the use of software registration data obtained from consumer), SoftwareCo should do so. In the absence of that more precise information, and pursuant to subsection (201)(a)(i) of this section, it would be "reasonable" for SoftwareCo to attribute its receipts in proportion to the number of RetailerY stores in each state.

(b) **Nonmarketing use** means the intangible property is used for purposes other than marketing, displaying, selling, and exhibiting. This use of the intangible property is often connected to manufacturing, research and development, or other similar nonmarketing uses. Typically, this category includes patents, know-how, designs, processes, models, and similar intangibles. Receipts from the nonmarketing use of intangible property are generally attributed to a specific location or locations where the manufacturing, research and development, or other similar nonmarketing use occurs.

Example 6. RideCo licenses the right to use its patented scooter brake to FunRide for the purpose of manufacturing scooters. FunRide will market the scooter under its own brand. This is a nonmarketing use. RideCo knows that FunRide will manufacture scooters in Michigan and Washington and that the scooter design is used equally in Michigan and Washington. Pursuant to subsection (201)(a)(i) of this section, RideCo will attribute its receipts from the license of its patent equally to Michigan and Washington.

Example 7. BurgerZ licenses to JoeHam the right to use its jumbo hamburger making process and know-how. This is a nonmarketing use. JoeHam markets the jumbo hamburgers under its own brand. JoeHam has two restaurant locations, one in Washington and one in Oregon. BurgerZ's fee for the intangible rights is based on a percentage of sales at each location. Pursuant to subsection (201)(a)(i) of this section, BurgerZ will attribute receipts from its license with JoeHam to each location based on sales at those locations.

Example 8. WidgetCo licenses the use of its patent to ManuCo, to manufacture widgets. ManuCo has three manufacturing plants located in Michigan where it will use the patent for manufacturing widgets. ManuCo also has a single research and development (R&D) facility in Washington where it will use the patented technology to develop the next generation of its widgets. These are nonmarketing uses. WidgetCo charges ManuCo a single price for the use of the patent in manufacturing and R&D. In the absence of information to the contrary, it is reasonable for WidgetCo to assume ManuCo's use of the patent is equal at all of ManuCo's relevant locations. Pursuant to subsection (201)(a)(i) of this section, because there are four locations where the patent is used equally, WidgetCo will attribute 25% of its apportionable royalty receipts to each of the four locations. Accordingly, 75% of the apportionable royalty receipts will be attributed to Michigan to reflect the use of the patent at the three manufacturing locations, and 25% of the apportionable royalty receipts will be attributable to Washington to reflect the use of the patent at the single R&D location.

(c) **Mixed use** means licensing the use of intangible property for both marketing and nonmarketing uses. Mixed use licenses may be sold for a single fee or more than one fee.

(i) **Single fee.** Where a single fee is charged for the mixed use license, it will be presumed that receipts were earned for a "marketing use" pursuant to the guidelines provided in (a) of this subsection, except to the extent that the taxpayer can reasonably establish otherwise or the department of revenue determines otherwise.

Example 9. ProcessCo licenses to KimchiCo, for a single fee, the right to use its patent and trademark for manufacturing and marketing a food processing device. KimchiCo has a single manufacturing plant in Washington and markets the finished product solely in Korea. This mixed use license for a single fee is presumed to be for a marketing use. Accordingly, ProcessCo must attribute receipts under the guidelines established for marketing uses. Pursuant to subsection (201)(a)(i) of this section, KimchiCo is marketing and selling the device only in Korea; therefore, all receipts will be attributed to Korea.

Example 10. FranchiseCo operates a restaurant franchising business and licenses the right to use its trademark, patent, and know-how to EatQuick for a single fee. EatQuick will use the intangibles to create and market its food product. This is a mixed use license for a single fee and will be presumed to be for a marketing use. EatQuick has a single restaurant location in Washington, where all sales are made. Pursuant to subsection (201)(a)(i) of this section, the intangible property is used by EatQuick in Washington at its restaurant location. Taxpayer will attribute 100% of its apportionable royalty receipts earned under the EatQuick license to Washington.

Example 11. Same facts as Example 10, except that EatQuick has five restaurant locations, one each in: Washington, California, Oregon, Idaho, and Montana. EatQuick pays an annual lump sum to FoodCo. This is a mixed use license for a single fee and will be presumed to be for marketing use. Further, FranchiseCo knows that EatQuick's use of the intangible property is equal at all locations. The intangible property is used equally by EatQuick in five states including Washington. Accordingly, pursuant to subsection (201)(a)(i) of this section, FoodCo will attribute 20% of its apportionable royalty receipts to each location, including Washington.

(ii) **More than one fee.** Where the mixed use license involves separate fees for each type of use and separate itemization is reasonable, then each fee will receive separate attribution treatment pursuant to (a) and (b) of this subsection. If the department determines that the separate itemization is not reasonable, the department may provide for more accurate attribution using the guidelines in (a) and (b) of this subsection.

Example 12. Same as Example 9, except the license agreement states that the nonmarketing use of the patent is valued at $450,000, and the marketing use of the trademark is valued at $550,000. This is a mixed use license with more than one fee. The stated values for the separate uses are reasonable. Pursuant to subsection (201)(a)(i) of this section, the receipts associated with the nonmarketing use are $450,000 and attributable to Washington where the patent is used in manufacturing. The receipts associated with the marketing use are $550,000 and attributed to Korea where the trademark is used for marketing and selling the finished product.

AMENDATORY SECTION (Amending WSR 12-19-064, filed 9/14/12, effective 10/15/12)

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 after May 31, 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 after May 31, 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 458-20-19405, CPI-U adjustments to minimum nexus thresholds for apportionable activities. This rule describes the minimum nexus thresholds adjustment that must be made to account for increases to the consumer price index for tax periods after May 31, 2010.

(v) 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)~~)) (vi) 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 attribute 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 as defined in WAC 458-20-19401, Minimum nexus thresholds for 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 any deductions allowable under chapter 82.04 RCW. All gross income that is not includable from apportionable activities 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) All apportionable income shall be apportioned to this state by multiplying such income by the apportionments percentage. 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. The reconciliation must be filed on a form approved by the department. 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) In either event (refund or additional taxes due), interest will apply in a manner consistent with tax assessments.

(ii) 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) 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 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. 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 apportionable income of the taxpayer in this state during the taxable period and the denominator of which is the apportionable 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.

(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.

(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.

NEW SECTION

WAC 458-20-19405 CPI-U adjustments to minimum nexus thresholds for apportionable activities. (1) **Introduction.**

(a) RCW 82.04.067(5) directs the department of revenue (department) to review the "substantial nexus thresholds" (thresholds) in RCW 82.04.067 (1)(c)(i) through (iii) each December. When the cumulative percentage change in the consumer price index for all urban consumers (CPI-U) changes by five percent or more from the measurement date, the department must adjust the thresholds to reflect that cumulative change in the CPI-U. For the first review, the measurement date is June 1, 2010. For all subsequent annual reviews, the measurement date is the date the thresholds were last adjusted.

(b) For purposes of determining the cumulative percentage change in the CPI-U, the department must compare the CPI-U available as of December 1st of the current year with the consumer price index as of the measurement date. For purposes of this subsection, the "measurement date" means the same as in (a) of this subsection.

(c) Adjustments to the thresholds will (i) be rounded to the nearest one thousand dollars, (ii) be effective as of January 1st immediately following the most recent annual review of the thresholds, and (iii) apply to tax periods beginning after the adjustments are made.

(2) **Adjusted substantial nexus thresholds.**

(a) The table below reflects the changes in the CPI-U and adjustments to the thresholds.

Calendar Year	CPI-U % Change	Time Period Measured	Receipts Threshold	Property Threshold	Payroll Threshold
2010			$250,000	$50,000	$50,000
2011	0.9%	6/1/2010 – 10/31/2010	$250,000	$50,000	$50,000
2012	4.5%	6/1/2010 – 10/31/2011	$250,000	$50,000	$50,000
2013	6.8%	6/1/2010 – 10/31/2012	$267,000	$53,000	$53,000
2014	TBD	1/1/2013 – 10/31/2013	TBD	TBD	TBD

CPI-U data through the month of October is generally the most current data available as of December 1st.

(b) The calendar year's thresholds in this subsection apply to the thresholds in RCW 82.04.067 and WAC 458-20-19401.

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