MULTISTATE TAX COMMISSION

Working Draft

Section 17 Model Regulations

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Reg. IV.17. Sales Factor: Sales Other Than Sales of Tangible Personal Property in This State

1. General Rules.

Comment [A1]: Consider adding a provision saying that unless service receipt or license use in jurisdiction is material, it does not go into the denominator. The work group may want to limit this concept to services sold, or intangible property used, *in a non-U.S jurisdiction*, consistent with a comparable rule in the CA regulation.

a. Market-Based Sourcing.

Sales, other than sales of tangible personal property, are in [state] within the meaning of this regulation if and to the extent that the corporation's market for the sales is in [state]. In general, the provisions in this section establish uniform rules for (1) determining whether and to what extent the market for a sale other than the sale of tangible personal property is in [state], (2) reasonably approximating the state or states of assignment where such state or states cannot be determined, and (3) excluding the sale where the state or states of assignment cannot be determined or reasonably approximated.

b. Outline of topics.

The provisions in this regulation are organized as follows:

1. General Rules
   a. Market-Based Sourcing
   b. Outline of Topics
   c. Definitions
   d. General Principles of Application; Contemporaneous Records
   e. Rules of Reasonable Approximation
   f. Rules with respect to Exclusion of Sales from the Sales Factor
   g. Changes in Methodology; Commissioner Review
   h. Industry-Specific Alternative Apportionment Rules
   i. Application to Services Provided Directly or Indirectly to a RIC
   j. Further Guidance

2. Sale, Rental, Lease or License of Real Property
3. Rental, Lease or License of Tangible Personal Property
4. Sale of a Service
   a. General Rule
   b. In-Person Services
   c. Services Delivered to the Customer or on Behalf of the Customer, or Delivered Electronically Through the Customer
   d. Professional Services

5. License or Lease of Intangible Property
   a. General Rules
   b. License of a Marketing Intangible
   c. License of a Production Intangible
   d. License of a Mixed Intangible
   e. License of Intangible Property where Substance of the Transaction Resembles a Sale of Goods or Services

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f. Examples

6. Sale of Intangible Property
   a. Assignment of Sales
   b. Examples

7. Special Rules
   a. Software Transactions
   b. Sales or Licenses of Digital Goods and Services
   c. Enforcement of Legal Rights

c. Definitions.

For the purposes of this regulation the following terms have the following meanings:

"Billing address" means the location indicated in the books and records of the taxpayer as the primary mailing address relating to a customer's account as of the time of the transaction as kept in good faith in the normal course of business and not for tax avoidance purposes.

"Business customer" means a customer that is a business operating in any form, including an individual that operates a business through the form of a sole proprietorship. Sales to a non-profit organization, to a trust, to the U.S. Government, to any foreign, state or local government, or to any agency or instrumentality of such government shall be treated as sales to a business customer and shall be assigned consistent with the rules that apply to such sales.

"Individual customer" means any customer that is not a business customer.

"Intangible property," generally includes, without limitation, copyrights; patents; trademarks; trade names; brand names; franchises; licenses; trade secrets; trade dress; information; know-how; methods; programs; procedures; systems; formulae; processes; technical data; designs; licenses; literary, musical, or artistic compositions; information; ideas; contract rights including broadcast rights; agreements not to compete; goodwill and going concern value; securities; and, except as otherwise provided in this regulation, computer software. In the case of a sale of intangible property, such sale may or may not be includable in the numerator and denominator of the taxpayer's sales factor, depending upon the application of the rules set forth in in 6.

"Place of order," means the physical location from which a customer places an order for a sale other than a sale of tangible personal property from a taxpayer, resulting in a contract with the taxpayer.

"State where a contract of sale is principally managed by the customer," means the primary location at which an employee or other

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representative of a customer serves as the primary contact person for the taxpayer with respect to the implementation and day-to-day execution of a contract entered into by the taxpayer with the customer.

d. General Principles of Application; Contemporaneous Records.

In order to satisfy the requirements of this regulation, a taxpayer's assignment of sales of other than tangible personal property must be consistent with the following principles:

i. A taxpayer's application of the rules set forth in this regulation shall be based on objective criteria and shall consider all sources of information reasonably available to the taxpayer at the time of its tax filing including, without limitation, the taxpayer's books and records kept in the normal course of business. A taxpayer's method of assigning its sales shall be determined in good faith, applied in good faith, and applied consistently with respect to similar transactions and year to year. A taxpayer shall retain contemporaneous records that explain the determination and application of its method of assigning its sales, including its underlying assumptions, and shall provide such records to the Commissioner upon request.

ii. The provisions of 4-7 provide for various assignment rules that apply sequentially in a hierarchy. For each sale to which a hierarchical rule applies, a taxpayer must make a reasonable effort to apply the primary rule applicable to the sale before seeking to apply the next rule in the hierarchy (and must continue to do so with each succeeding rule in the hierarchy, where applicable). For example, in some cases, the applicable rule first requires a taxpayer to determine the state or states of assignment, and where the taxpayer cannot do so, the rule then requires the taxpayer to reasonably approximate such state or states. In such cases, the taxpayer must in good faith and with reasonable effort attempt to determine the state or states of assignment (i.e., apply the primary rule in the hierarchy) before it may reasonably approximate such state or states.

iii. A taxpayer's method of assigning its sales, including the use of a method of approximation, where applicable, must reflect an attempt to obtain the most accurate assignment of sales consistent with the regulatory standards set forth in in this regulation, rather than an attempt to lower the taxpayer's tax liability. A method of assignment that is reasonable for one taxpayer may not necessarily be reasonable for another taxpayer, depending upon the applicable facts.

e. Rules of Reasonable Approximation.

i. In General. In general, the provisions of 4-7 establish uniform rules for determining whether and to what extent the market for

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a sale other than the sale of tangible personal property is in [state]. The provisions of the regulation also set forth rules of reasonable approximation, which apply where the state or states of assignment cannot be determined. In some instances, the reasonable approximation must be made in accordance with specific rules of approximation prescribed by this regulation. *See, e.g.*, 4.d (pertaining to professional services). In other cases, the applicable rule in this regulation permits a taxpayer to reasonably approximate the state or states of assignment, using a method that reflects an effort to approximate the results that would be obtained under the applicable rules or standards set forth in this regulation.

ii. Approximation Based Upon Known Sales. In any instance where, applying the applicable rules set forth in (4), pertaining to sales of services, a taxpayer can ascertain the state or states of assignment of a substantial portion of its sales of substantially similar services ("assigned sales"), but not all of such sales, and the taxpayer reasonably believes, based on all available information, that the geographic distribution of some or all of the remainder of such sales generally tracks that of the assigned sales, it shall include those sales which it believes tracks the geographic distribution of the assigned sales in its sales factor in the same proportion as its assigned sales. This rule also applies in the context of licenses and sales of intangible property where the substance of the transaction resembles a sale of goods or services. *See* 5.e. and 6.a.v.

f. Rules with respect to Exclusion of Sales from the Sales Factor

i. In any case in which a taxpayer cannot ascertain the state or states to which a sale is to be assigned pursuant to the applicable rules set forth in this regulation (including through the use of a method of reasonable approximation, where relevant) using a reasonable amount of effort undertaken in good faith, the sale shall be excluded from the numerator and the denominator of the taxpayer's sales factor.

ii. In any case in which a taxpayer can ascertain the state or states to which a sale is to be assigned pursuant to the applicable rules set forth in this regulation, but the taxpayer is not taxable in one or more such states, the sales that would otherwise be assigned to such states where the taxpayer is not taxable shall be excluded from the numerator and denominator of the taxpayer's sales factor. The rules to determine whether a taxpayer is taxable in a state are set forth at (5).

g. Changes in Methodology; Commissioner Review

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i. General Rules Applicable to Original Returns. In any case in which a taxpayer files an original return for a taxable year in which it properly assigns its sales using a method of assignment, including a method of reasonable approximation, in accordance with the rules stated in this regulation, the application of such method of assignment shall be deemed to be a correct determination by the taxpayer of the state or states of assignment to which the method is properly applied. In such cases, neither the Commissioner nor the taxpayer (through the form of an audit adjustment, amended return, abatement application or otherwise) may modify the taxpayer's methodology as applied for assigning such sales for such taxable year. However, the Commissioner and the taxpayer may each subsequently, through the applicable administrative process, correct either factual errors or calculation errors with respect to the taxpayer's application of its filing methodology.

ii. Commissioner Authority to Adjust a Taxpayer's Return. The Commissioner's ability to review and adjust a taxpayer's assignment of sales on a return to more accurately assign such sales consistent with the rules or standards of this regulation, includes, but is not limited to, each of the following potential actions.

(A) In any case in which a taxpayer fails to properly assign a sale in accordance with the rules set forth in this regulation, including the failure to properly apply a hierarchy of rules consistent with the principles of 1.d.ii, the Commissioner may adjust the assignment of such sales in accordance with the applicable rules in this regulation.

(B) In any case in which a taxpayer uses a method of approximation to assign its sales and the Commissioner determines that the method of approximation employed by the taxpayer is not reasonable, the Commissioner may substitute a method of approximation that the Commissioner determines is appropriate or may exclude the sales from the taxpayer's numerator and denominator, as appropriate.

(C) In any case in which the Commissioner determines that a taxpayer's method of approximation is reasonable, but has not been applied in a consistent manner with respect to similar transactions or year to year, the Commissioner may require that the taxpayer apply its method of approximation in a consistent manner.

(D) In any case in which a taxpayer excludes sales from the numerator and denominator of its sales factor on the theory that the assignment of such sales cannot be reasonably approximated, the Commissioner may determine that the exclusion of such sales is not appropriate, and may instead

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substitute a method of approximation that the Commissioner determines is appropriate.

(E) In any case in which a taxpayer fails to retain contemporaneous records that explain the determination and application of its method of assigning its sales, including its underlying assumptions, or fails to provide such records to the Commissioner upon request, the Commissioner may treat the taxpayer's assignment of sales as unsubstantiated, and may adjust the assignment of such sales in a manner consistent with the applicable rules in this regulation.

(F) In any case in which the Commissioner concludes that a taxpayer's customer's billing address was selected for tax avoidance purposes, the Commissioner may adjust the assignment of sales to such customer in a manner consistent with the applicable rules in this regulation.

iii. Taxpayer Authority to Change a Method of Assignment on a Prospective Basis. In filing its original return for a tax year, a taxpayer may change its method of assigning its sales under this regulation from the method it used in the preceding year, including changing its method of approximation from that used on previous returns. However, the taxpayer may only make such change for purposes of improving the accuracy of assigning its sales consistent with the rules set forth in this regulation, including, for example, to address the circumstance where there is a change in the information that is available to the taxpayer as relevant for purposes of complying with such rules. Further, a taxpayer that seeks to change its method of assigning its sales must disclose, in the original return filed for the year of the change, the fact that it is has made the change, and must retain and provide to the Commissioner upon request documents that explain the nature and extent of the change, and the reason for the change. If a taxpayer fails to adequately disclose such change or retain and provide such records upon request, the Commissioner may disregard the taxpayer's change and substitute an assignment method that the Commissioner determines is appropriate.

iv. Commissioner Authority to Change a Method of Assignment on a Prospective Basis. The Commissioner may direct a taxpayer to change its method of assigning its sales in tax returns that have not yet been filed, including changing the taxpayer's method of approximation, if upon reviewing the taxpayer's filing methodology applied for a prior tax year, the Commissioner determines that such change is appropriate to reflect a more accurate assignment of the taxpayer's sales within the meaning of this regulation, and determines that such change can be reasonably adopted by the taxpayer. The Commissioner will provide the taxpayer with a written explanation as to the reason for making such change. In any

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case in which a taxpayer fails to comply with the Commissioner's direction on subsequently filed returns, the Commissioner may deem the taxpayer's method of assigning its sales on such returns to be unreasonable, and may substitute an assignment method that the Commissioner determines is appropriate.

h. Industry-Specific Alternative Apportionment Rules.

Prior to the enactment of St. 2013, c. 46, § 37, the Commissioner promulgated six industry-specific alternative apportionment regulations to address industries where the application of the provisions of M.G.L. c. 63, § 38 were not reasonably adapted to approximate the net income derived from business carried on within [state]. *See* M.G.L. c. 63, § 38(j). Following the enactment of St. 2013, c. 46, § 37, the Commissioner reviewed those six industry-specific alternative apportionment regulations, and determined for each industry that the provisions of M.G.L. c. 63, § 38 as a whole continue not to be reasonably adapted to approximate the net income derived from business carried on within [state]. However, in the case of three of the industries, the Commissioner determined that industry-specific alternative sales factor rules were no longer needed in light of St. 2013, c. 46, § 37. In the case of the other three industries, the Commissioner determined that the industry-specific alternative sales factor rules remain necessary.

i. Industry-Specific Sales Factor Provisions that Remain in Effect. Prior to the enactment of St. 2013, c. 46, § 37 the Commissioner promulgated industry-specific alternative apportionment regulations for pipeline companies, corporations engaged in the electricity industry, and corporations engaged in the telecommunications industry. *See* 830 CMR 63.38.8 (pipeline companies); 830 CMR 63.38.10 (electricity industry) and 830 CMR 63.38.11 (telecommunications industry). These industry-specific regulations remain fully in effect and are not superseded in whole or in part by the rules of 830 CMR 63.38.1(9)(d), as these regulations continue to address circumstances where the provisions of M.G.L. c. 63, § 38, including M.G.L. c. 63, § 38(f), are not reasonably adapted to approximate the net income derived from business carried on within [state]. However, a special rule pertaining to taxpayers that provide telecommunications services that are also engaged in the sale or license of digital goods and services shall apply notwithstanding the rules set forth in 830 CMR 63.38.11. *See* 830 CMR 63.38.1(9)(d)7.b.ii.

ii. Industry-Specific Sales Factor now Determined under 830 CMR 63.38.1.(9)(d). Prior to the enactment of St. 2013, c. 46, § 37 the Commissioner promulgated industry-specific alternative apportionment regulations for motor carriers, airlines, and courier and package delivery services. *See* 830 CMR 63.38.2 (airlines); 830 CMR 63.38.3 (motor carriers); 830 CMR 63.38.4 (courier and package delivery services). In each of these cases, the sales factor is

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now determined pursuant to the rules of 830 CMR 63.38.1(9)(d). The industry-specific property and payroll factor rules for those industries remain fully in effect.

i. Application to Services Provided Directly or Indirectly to a RIC.

Nothing in this regulation shall be construed to supersede or affect the application of the rules set forth that apply to mutual fund service corporations. However, rules with respect to mutual fund sales, as made by a taxpayer that is not a mutual fund service corporation, are set forth at 4.d.iii(D).

j. Further Guidance.

The Commissioner may issue further public written statements with respect to the rules set forth in this regulation. Such further guidance may, among other things, include guidance with respect to: (1) what constitutes a reasonable method of approximation within the meaning of such rules, and (2) the circumstances in which a filing change with respect to a taxpayer's method of reasonable approximation will be deemed appropriate.

2. *Sale, Rental, Lease or License of Real Property.*

In the case of a sale, rental, lease or license of real property, the sale is in [state] if and to the extent that the property is in [state].

3. *Rental, Lease or License of Tangible Personal Property.*

In the case of a rental, lease or license of tangible personal property, the sale is in [state] if and to the extent that the property is in [state]. If property is mobile property that is located both within and without [state] during the period of the lease or other contract, the receipts assigned to [state] shall be the receipts from the contract period multiplied by the fraction used by the taxpayer for property factor purposes under (7)(d) (as adjusted when necessary to reflect differences between usage during the contract period and usage during the taxable year).

4. *Sale of a Service.*

a. General Rule.

The sale of a service is in [state] if and to the extent that the service is delivered at a location in [state]. In general, the term "delivered" shall be construed to refer to the location of the taxpayer's market for the service provided and is not to be construed by reference to the location of the property or payroll of the taxpayer as otherwise determined for corporate apportionment purposes pursuant to Article IV(10)-(14). The rules to determine the location of the delivery of a service in the context of several specific types of service transactions are set forth at 4.b-d.

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b. In-Person Services.

i. In General.

Except as otherwise provided in this subsection, 4.b, in-person services are services that are physically provided in person by the taxpayer, where the customer or the customer's real or tangible property upon which the services are performed is in the same location as the service provider at the time the services are performed. This rule includes situations where the services are provided on behalf of the taxpayer by a third-party contractor. Examples of in-person services include, without limitation, warranty and repair services; cleaning services; plumbing services; carpentry; construction contractor services; pest control; landscape services; medical and dental services, including medical testing and x-rays and mental health care and treatment; child care; hair cutting and salon services; live entertainment and athletic performances; and in-person training or lessons. In-person services include services within the description above that are performed at (1) a location that is owned or operated by the service provider or (2) a location of the customer, including the location of the customer's real or tangible personal property. Various professional services, including legal, accounting, financial and consulting services, and other such services as described in 4.d, although they may involve some amount of in-person contact, are not treated as in-person services within the meaning of this section, 4.b.

ii. Assignment of Sales.

Comment [A2]: There has been a proposal to insert language for legal services.

Except as otherwise provided in this subsection 4.b, where the service provided by the taxpayer is an in-person service, the delivery of the service is at the location where the service is received. Therefore, the sale is in [state] if and to the extent the customer receives the in-person service in [state]. In assigning its sales of in-person services, a taxpayer shall first attempt to determine the location where a service is received, as follows:

(A) Where the service is performed with respect to the body of an individual customer in [state] (e.g. hair cutting or x-ray services) or in the physical presence of the customer in [state] (e.g. live entertainment or athletic performances), the service is received in [state].

(B) Where the service is performed with respect to the customer's real estate in [state] or where the service is performed with respect to the customer's tangible personal property at the customer's residence or in the customer's possession in [state], the service is received in [state].

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(C) Where the service is performed with respect to the customer's tangible personal property and the tangible personal property is to be shipped or delivered to the customer, whether the service is performed in [state] or outside [state], the service is received in [state] if such property is shipped or delivered to the customer in [state].

In any instance in which the state or states where a service is actually received cannot be determined, but the taxpayer has sufficient information regarding the place of receipt from which it can reasonably approximate the state or states where the service is received, the taxpayer shall reasonably approximate such state or states. In any instance where the state to which the sale is to be assigned can be determined or reasonably approximated, but the taxpayer is not taxable in such state, the sale that would otherwise be assigned to such state shall be excluded from the numerator and denominator of the taxpayer's sales factor. *See* 1.f.ii.

~~iii. Transportation and Delivery Services.~~

~~(A) In General. Transportation and delivery services, involving the physical transportation of people or tangible personal property from one destination to another, are in-person services within the meaning of this section, 4.b. Special rules of assignment apply to receipts from the provision of transportation and delivery services. The assignment of receipts from such services depends upon whether such services are provided by air or by other means as provided in 4.b.iii(B) and (C). Receipts from a taxpayer's sale of transportation and delivery services are assigned pursuant to this section whether the transportation and delivery services are provided directly by the taxpayer or indirectly by another entity under common ownership with the taxpayer as defined in [section]. If a taxpayer provides transportation and delivery services exclusively by air, the rule in 4.b.iii(B) applies to receipts from such services. If a taxpayer provides transportation and delivery services both by air and by means other than air, the rule in 4.b.iii(C) applies to receipts from such services. If a taxpayer that provides transportation and delivery services also derives receipts from activities other than transportation and delivery services, such other receipts are apportioned according to the applicable rules of Article IV.~~

~~(B) Transportation and Delivery Services Provided Exclusively by Air. Transportation and delivery services provided exclusively by air are assigned to the state or states of the aircraft departures associated with such services. Therefore, the receipts assigned to this state shall be determined by multiplying the taxpayer's total receipts from such services by the percentage of the aircraft departures occurring in this state relative to the~~

Comment [A3]: Chris Coffman proposes the following:
(B) Where the service is performed with respect to the customer's real estate in this state. or where the service is performed with respect to the customer's tangible personal property at the customer's residence or in the customer's possession in this state, the service is received in this state

(C) Where the service is performed with respect to the customer's tangible personal property:

(1) Where the service is performed with respect to the customer's tangible personal property at the customer's residence or in the customer's possession in this state, the service is received in this state.

(2) Where (C)(1) does not apply and the tangible personal property is to be shipped or delivered to the customer, whether the service is performed in this state or outside this state, the service is received in this state if such property is shipped or delivered to the customer in this state.

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~~aircraft departures that take place everywhere. In any case where the services are provided by multiple aircraft types, the calculation shall be weighted by the values of the aircraft types as provided in [section]. These rules supersede the rules set forth in [section] to the extent of any inconsistency.~~

~~(C) Transportation and Delivery Services Provided by Means other than Exclusively by Air.~~

~~1. Except as otherwise provided by this section, 4.b.iii(C), transportation and delivery services (other than exclusively by air) are assigned to the state or states of the departures and arrivals (in the case of the transportation of people), or pickups and deliveries (in the case of the transportation of tangible personal property), associated with such services. Therefore, the receipts assigned to this state shall be determined by multiplying the taxpayer's total receipts from such services by the percentage of the total departures (or pickups) and arrivals (or deliveries) that take place in this state relative to the departures (or pickups) and arrivals (or deliveries) that take place everywhere. Transportation and delivery services to which this section, 4.b.iii(C), applies include, without limitation, such services as provided by cars, buses, trains, and trucks, and with respect to a taxpayer that provides transportation and delivery services by both air and means other than air, all of such transportation services. These rules supersede the rules set forth for motor carriers courier and package delivery services to the extent of any inconsistency. The rules set forth in this section, 4.b.iii(C), do not apply to transportation and delivery services as provided through the means of pipelines, which are governed by industry-specific alternative apportionment rules.~~

~~2. For purposes of this section, 4.b.iii(C),~~

~~i. The location of a "pickup" shall be the location at which an item of tangible personal property is transferred from the customer or the customer's designee for transportation and subsequent delivery; and~~

~~ii. The location of a "delivery" shall be the location at which an item of tangible personal property that has been transported is transferred to the customer or the customer's designee.~~

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iv. Examples.

c. Services Delivered to the Customer or on Behalf of the Customer, or Delivered Electronically Through the Customer.

i. In General.

Where the service provided by the taxpayer is not an in-person service within the meaning of 4.b or a professional service within the meaning of 4.d, and the service is delivered to or on behalf of the customer, or delivered electronically through the customer, the sale is in [state] if and to the extent that the service is delivered in [state]. For purposes of this section, 4.c., a service that is delivered "to" a customer is a service in which the customer and not a third party is the recipient of the service. A service that is delivered "on behalf of" a customer is one in which a customer contracts for a service but one or more third parties, rather than the customer, is the recipient of the service, such as fulfillment services (*see* 4.c.ii(A))or the direct or indirect delivery of advertising to the customer's intended audience (see 4.c.ii(C)). A service that is delivered electronically "through" a customer is a service that is delivered electronically to a customer for purposes of resale and subsequent electronic delivery in substantially identical form to an end user or other third-party recipient. Except in the instance of a service that is delivered through a customer (where the service must be delivered electronically), a service is included within the meaning of this regulation, irrespective of the method of delivery, e.g., whether such service is delivered by a physical means or through an electronic transmission.

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ii. Assignment of Sales.

The assignment of a sale to a state or states in the instance of a service that is delivered to the customer or on behalf of the customer, or delivered electronically through the customer, depends upon the method of delivery of the service and the nature of the customer. Separate rules of assignment apply to services delivered by physical means and services delivered by electronic transmission. (For purposes of this section, 4.c, a service delivered by an electronic transmission shall not be considered a delivery by a physical means). In any instance where, applying the rules set forth in this section, 4.c, the rule of assignment depends on whether the customer is an individual or a business customer, and the taxpayer acting in good faith cannot reasonably determine whether the customer is an individual or business customer, the taxpayer shall treat the customer as a business customer. In any instance where the state to which the sale is to be assigned can be determined or reasonably approximated, but the taxpayer is not taxable in such state, the sale that would otherwise be assigned to such state shall be excluded

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from the numerator and denominator of the taxpayer's sales factor. *See* 1.f.ii.

(A) Delivery to or on Behalf of a Customer by Physical Means, Whether to an Individual or Business Customer. Services delivered to a customer or on behalf of a customer through a physical means include, for example, product delivery services where property is delivered to the customer or to a third party on behalf of the customer; the delivery of brochures, fliers or other direct mail services; the delivery of advertising or advertising-related services to the customer's intended audience in the form of a physical medium; and the sale of custom software (e.g., where software is developed for a specific customer in a case where the transaction is properly treated as a service transaction for purposes of corporate taxation) where the taxpayer installs the custom software at the customer's site. The rules in this subsection 4.c.ii(A) apply whether the taxpayer's customer is an individual customer or a business customer.

Comment [A4]: Ben Miller has questioned whether the physical delivery section should be moved or restructured. The group is holding this issue in abeyance for the time being.

1. Rule of Determination. In assigning the sale of a service delivered to a customer or on behalf of a customer through a physical means, a taxpayer must first attempt to determine the state or states where such services are delivered. Where the taxpayer is able to determine the state or states where the service is delivered, it shall assign the sale to such state or states.

2. Rule of Reasonable Approximation. Where the taxpayer cannot determine the state or states where the service is actually delivered, but has sufficient information regarding the place of delivery from which it can reasonably approximate the state or states where the service is delivered, it shall reasonably approximate such state or states.

3. Examples

(B) Delivery to a Customer by Electronic Transmission. Services delivered by electronic transmission include, without limitation, services that are transmitted through the means of wire, lines, cable, fiber optics, electronic signals, satellite transmission, audio or radio waves, or other similar means, whether or not the service provider owns, leases or otherwise controls the transmission equipment. In the case of the delivery of a service by electronic transmission to a customer, the following rules apply.

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1. Services Delivered By Electronic Transmission to an Individual Customer.

    a. Rule of Determination. In the case of the delivery of a service to an individual customer by electronic transmission, the service is delivered in [state] if and to the extent that the taxpayer's customer receives the service in [state]. If the taxpayer can determine the state or states where the service is received, it shall assign the sale to such state or states.

    b. Rules of Reasonable Approximation. If the taxpayer cannot determine the state or states where the customer actually receives the service, but has sufficient information regarding the place of receipt from which it can reasonably approximate the state or states where the service is received, it shall reasonably approximate such state or states. Where a taxpayer does not have sufficient information from which it can determine or reasonably approximate the state or states in which the service is received, it shall reasonably approximate such state or states using the customer's billing address.

2. Services Delivered By Electronic Transmission to a Business Customer

    a. Rule of Determination. In the case of the delivery of a service to a business customer by electronic transmission, the service is delivered in [state] if and to the extent that the taxpayer's customer receives the service in [state]. If the taxpayer can determine the state or states where the service is received, it shall assign the sale to such state or states. For purposes of this section, 4.c.ii(B)2, it is intended that the state or states where the service is received reflect the location at which the service is directly used by the employees or designees of the customer.

    b. Rule of Reasonable Approximation. If the taxpayer cannot determine the state or states where the customer actually receives the service, but has sufficient information regarding the place of receipt from which it can reasonably approximate the state or states where the service is received, it shall reasonably approximate such state or states.

    c. Secondary Rule of Reasonable Approximation. In the case of the delivery of a service to a business customer by electronic transmission where a taxpayer does not have sufficient information from which it can determine or

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reasonably approximate the state or states in which the service is received, such state or states shall be reasonably approximated as set forth in this regulation. In such cases, unless the taxpayer can apply the safe harbor set forth in 4.c.ii(B)2.d the taxpayer shall reasonably approximate the state or states in which the service is received as follows: first, by assigning the sale to the state where the contract of sale is principally managed by the customer; second, if the state where the customer principally manages the contract is not reasonably determinable, by assigning the sale to the customer's place of order; and third, if the customer's place of order is not reasonably determinable, by assigning the sale using the customer's billing address; provided, however, that in any instance in which the taxpayer derives more than 5% of its sales of services from a customer, the taxpayer is required to identify the state in which the contract of sale is principally managed by that customer.

d. Safe Harbor. In the case of the delivery of a service to a business customer by electronic transmission a taxpayer may not be able to determine, or reasonably approximate under 4.c.ii(B)2.b, the state or states in which the service is received. In these cases, the taxpayer may, in lieu of the rule stated at 4.c.ii(B)2.c, apply the safe harbor stated in this section, 4.c.ii(B)2.d. Under this safe harbor, a taxpayer may assign its sales to a particular customer based upon the customer's billing address in any taxable year in which the taxpayer (1) engages in substantially similar service transactions with more than 250 customers, whether business or individual, and (2) does not derive more than 5% of its sales of services from such customer. This safe harbor applies only for purposes of 4.c.ii(B)2, to services delivered by electronic transmission to a business customer, and not otherwise.

3. Examples.

(C) Services Delivered Electronically Through or on Behalf of an Individual or Business Customer. A service delivered electronically "on behalf of" the customer is one in which a customer contracts for a service to be delivered electronically but one or more third parties, rather than the customer, is the recipient of the service, such as the direct or indirect delivery of advertising on behalf of a customer to the customer's intended audience. A service delivered electronically "through" a customer to third-party recipients is a service that is delivered electronically to a customer for purposes of resale and

Comment [A5]: See Comment A12, p. 24, regarding "License of a Marketing Intangible": If the recommended final sentence is added, this portion should be edited to conform.

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subsequent electronic delivery in substantially identical form to end users or other third-party recipients.

1. Rule of Determination. In the case of the delivery of a service by electronic transmission, where the service is delivered electronically to end users or other third-party recipients through or on behalf of the customer, the service is delivered in [state] if and to the extent that the end users or other third-party recipients are in [state]. For example, in the case of the direct or indirect delivery of advertising on behalf of a customer to the customer's intended audience by electronic means, the service is delivered in [state] to the extent that the audience for such advertising is in [state]. In the case of the delivery of a service to a customer that acts as an intermediary in reselling the service in substantially identical form to third-party recipients, the service is delivered in [state] to the extent that the end users or other third-party recipients receive such services in [state]. The rules in this subsection 4.c.ii(C) apply whether the taxpayer's customer is an individual customer or a business customer and whether the end users or other third-party recipients to which the services are delivered through or on behalf of the customer are individuals or businesses.

2. Rule of Reasonable Approximation. If the taxpayer cannot determine the state or states where the services are actually delivered to the end users or other third-party recipients either through or on behalf of the customer, but has sufficient information regarding the place of delivery from which it can reasonably approximate the state or states where the services are delivered, it shall reasonably approximate such state or states.

3. Select Secondary Rules of Reasonable Approximation.

    i. Where a taxpayer's service is the direct or indirect electronic delivery of advertising on behalf of its customer to the customer's intended audience, if the taxpayer lacks sufficient information regarding the location of the audience from which it can determine or reasonably approximate such location, the taxpayer shall reasonably approximate the audience in a state for such advertising using the following secondary rules of reasonable approximation. Where a taxpayer is delivering advertising directly or indirectly to a known list of subscribers, the taxpayer shall reasonably approximate the audience for advertising in a state using a percentage that reflects the ratio of the state's subscribers in the specific geographic area in which the advertising is delivered relative to the total subscribers

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in such area. For a taxpayer with less information about its audience, the taxpayer shall reasonably approximate the audience in a state using the percentage that reflects the ratio of the state's population in the specific geographic area in which the advertising is delivered relative to the total population in such area.

ii. Where a taxpayer's service is the delivery of a service to a customer that then acts as the taxpayer's intermediary in reselling such service to end users or other third-party recipients, if the taxpayer lacks sufficient information regarding the location of the end users or other third-party recipients from which it can determine or reasonably approximate such location, the taxpayer shall reasonably approximate the extent to which the service is received in a state by using the percentage that reflects the ratio of the state's population in the specific geographic area in which the taxpayer's intermediary resells such services, relative to the total population in such area.

4. Examples

d. Professional Services.

i. In General.

Except as otherwise provided in 4.d.ii, professional services are services that require specialized knowledge and in some cases require a professional certification, license or degree. Professional services include, without limitation, management services, bank and financial services, financial custodial services, investment and brokerage services, fiduciary services, tax preparation, payroll and accounting services, lending and credit card services, legal services, consulting services, video production services, graphic and other design services, engineering services, and architectural services.

ii. Overlap with Other Categories of Services.

(A) Certain services that fall within the definition of "professional services" set forth in 4.d.i are nevertheless treated as "in-person services" within the meaning of 4.b, and are assigned under the rules of 4.b. Specifically, professional services that are physically provided in person by the taxpayer such as carpentry, certain medical and dental services or child care services, where the customer or the customer's real or tangible property upon which the services are provided is in the same location as the service provider at the time the services are performed, are "in-person

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services" and are assigned as such, notwithstanding that they may also be considered to be "professional services". However, professional services where the service is of an intellectual or intangible nature, such as legal, accounting, financial and consulting services, are assigned as professional services under the rules of section 4.d.iii, notwithstanding the fact that such services may involve some amount of in-person contact.

(B) Professional services may in some cases include the transmission of one or more documents or other communications by mail or by electronic means. However, in such cases, despite this transmission, the assignment rules that apply are those set forth in this section, 4.d.iii, and not those set forth in 4.c, pertaining to services delivered to a customer or through or on behalf of a customer.

iii. Assignment of Sales.

In the case of a professional service, it is generally possible to characterize the location of delivery in multiple ways by emphasizing different elements of the service provided, no one of which will consistently represent the market for the services. Therefore, for purposes of consistent application of the market sourcing rule stated in [UDITPA],~~,~~ the Commissioner has concluded that the location of delivery in the case of professional services is not susceptible to a general rule of determination, and must be reasonably approximated. The assignment of a sale of a professional service depends in many cases upon whether the customer is an individual or business customer. In any instance in which the taxpayer, acting in good faith, cannot reasonably determine whether the customer is an individual or business customer, the taxpayer shall treat the customer as a business customer. For purposes of assigning the sale of a professional service, a taxpayer's customer is the person who contracts for such service, irrespective of whether another person pays for or also benefits from the taxpayer's services. ~~Except as provided in 4.d.iiiii(D) (mutual fund sales), i~~In any instance in which the taxpayer is not taxable in the state to which a sale shall be assigned, the sale shall be excluded from the numerator and denominator of the taxpayer's sales factor. *See* 1.f.ii

Comment [A6]: The work group has questioned whether or not to keep this rearticulation of the throwout rule.

(A) General Rule. Sales of professional services other than those services described in 4.d.iii(B) (architectural and engineering services), 4.d.iii(C) (services provided by a financial institution) and 4.d. iii(D) (certain services provided to RICs)), are assigned in accordance with this section 4.d.iii(A).

1. Professional Services Delivered to Individual Customers. Except as otherwise provided in this section, 4.d, in any

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instance in which the service provided is a professional service and the taxpayer's customer is an individual customer, the state or states in which the service is delivered shall be reasonably approximated as set forth in this section, 4.d.iii(A)1. In particular, the taxpayer shall assign the sale to the customer's state of primary residence, or, if the taxpayer cannot reasonably identify the customer's state of primary residence, to the state of the customer's billing address; provided, however, in any instance in which the taxpayer derives more than 5% of its sales of services from an individual customer, the taxpayer is required to identify the customer's state of primary residence and must assign the receipts from the service or services provided to that customer to that state.

2. Professional Services Delivered to Business Customers. Except as otherwise provided in this section, 4.d, in any instance in which the service provided is a professional service and the taxpayer's customer is a business customer, the state or states in which the service is delivered shall be reasonably approximated as set forth in this section, 4.d.iii(A)2. In particular, unless the taxpayer may use the safe harbor set forth at 4.d.iii(A)3, the taxpayer shall assign the sale as follows: first, by assigning the receipts to the state where the contract of sale is principally managed by the customer; second, if such place of customer management is not reasonably determinable, to the customer's place of order; and third, if such customer place of order is not reasonably determinable, to the customer's billing address; provided, however, in any instance in which the taxpayer derives more than 5% of its sales of services from a customer, the taxpayer is required to identify the state in which the contract of sale is principally managed by the customer.

3. Safe Harbor; Large Volume of Transactions. Notwithstanding the rules set forth in 4.d.iii(A)1 and 2, a taxpayer may assign its sales to a particular customer based on the customer's billing address in any taxable year in which the taxpayer (1) engages in substantially similar service transactions with more than 250 customers, whether individual or business, and (2) does not derive more than 5% of its sales of services from such customer. This safe harbor applies only for purposes of 4.d.iii(A), and not otherwise.

(B) Architectural and Engineering Services with respect to Real or Tangible Personal Property. Architectural and engineering services with respect to real or tangible personal property are professional services within the meaning of this section, 4.d.

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However, unlike in the case of the general rule that applies to professional services, (1) the sale of such an architectural service is assigned to a state or states if and to the extent that the services are with respect to real estate improvements located, or expected to be located, in such state or states; and (2) the sale of such an engineering service is assigned to a state or states if and to the extent that the services are with respect to tangible or real property located in such state or states, including real estate improvements located in, or expected to be located in, such state or states. These rules apply whether or not the customer is an individual or business customer. In any instance in which architectural or engineering services are not described in this section 4.d.iii(B), the sale of such services shall be assigned under the general rule for professional services. *See* 4.d.iii(A).

(C) Services provided by a Financial Institution. The apportionment rules that apply to financial institutions are set forth at [Financial institutions special apportionment regulation or statute]. That [statute] includes specific rules to determine a financial institution's sales factor. However, [the statute] also provides that receipts from sales, other than sales of tangible personal property, including service transactions, that are not otherwise apportioned under [the financial institutions statute], are to be assigned pursuant to [UDITPA]. In any instance in which a financial institution performs services that are to be assigned pursuant to [UDITPA], including, for example, financial custodial services, those services shall be considered professional services within the meaning of this section, 4.d, and shall be assigned according to the general rule for professional service transactions as set forth at 4.d.ii(A).

Comment [A7]: Note that this provision is specific to language contained in the MTC financial institutions statute. However, not all states have adopted the statute, and those that have may not incorporate or apply it in its original form.

~~(D) Mutual Fund Sales. Mutual fund sales within the meaning of this regulation, 830 CMR 63.38.1, generally are sales of professional services for purposes of 830 CMR 63.38.1(9)(d)4.d. *See* 830 CMR 63.38.1(2) (definition of mutual fund sales). However, the rules to assign mutual fund sales made by a mutual fund service corporation are those set forth in 830 CMR 63.38.7, and not those set forth in this regulation, 830 CMR 63.38.1. Also, in the case of mutual fund sales made by a taxpayer that is not a mutual fund service corporation, such mutual fund sales shall be assigned by applying the sourcing methodology described in 830 CMR 63.38.7(4)(c)4 to such sales. In these cases, consistent with the rules of M.G.L. c. 63, § 38(f) and 830 CMR 63.38.7, the mutual fund sales made by the taxpayer directly or indirectly to the RIC are included in the numerator and denominator of the taxpayer's sales factor irrespective as to whether the taxpayer is taxable in one or more of the states in which the RIC's shareholders are domiciled.~~

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iii. Examples.

5. *License or Lease of Intangible Property.*

a. General Rules.

i. The receipts from the license of intangible property are in [state] if and to the extent the intangible is used in [state]. In general, the term "use" shall be construed to refer to the location of the taxpayer's market for the use of the intangible property that is being licensed and is not to be construed to refer to the location of the property or payroll of the taxpayer as otherwise determined for corporate apportionment purposes pursuant to Article IV(10)-(14). The rules that apply to determine the location of the use of intangible property in the context of several specific types of licensing transactions are set forth at 5.b-e. For purposes of the rules set forth in this section, 5, a lease of intangible property is to be treated the same as a license of intangible property.

ii. In general, a license of intangible property that conveys all substantial rights in such property is treated as a sale of intangible property for tax purposes. *See* 6. Note, however, that for purposes of 5 and 6, a sale or exchange of intangible property is treated as a license of such property where the receipts from the sale or exchange derive from payments that are contingent on the productivity, use or disposition of the property.

iii. Intangible property licensed as part of the sale or lease of tangible property is treated under this regulation as the sale or lease of tangible property.

iv. In any instance in which the taxpayer is not taxable in the state to which the receipts from the license of intangible property are assigned, the receipts shall be excluded from the numerator and denominator of the taxpayer's sales factor. *See* 1.f.ii.

v. To the extent that the transfer of either a security, as defined in [section], or business "goodwill" or similar intangible value, including, without limitation, "going concern value" or "workforce in place," may be characterized as a license or lease of intangible property, receipts from such transaction shall be excluded from the numerator and the denominator of the taxpayer's sales factor.

b. License of a Marketing Intangible.
Where a license is granted for the right to use intangible property in connection with the sale, lease, license, or other marketing of goods, services, or other items (i.e., a marketing intangible), the royalties or other licensing fees paid by the licensee for such right are assigned to [state] to the extent that the fees are attributable to the sale or other

Comment [A8]: Members of the work group have expressed some concerns about how the rule would function in separate entity states; this is something to revisit later in the process.

Comment [A9]: Group members recommend we change this to "for purposes of allocation and apportionment," or otherwise specify it applies only to this regulation.

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provision of goods, services, or other items purchased or otherwise acquired by customers in [state]. Examples of a license of a marketing intangible include, without limitation, the license of a service mark, trademark, or trade name; certain copyrights; the license of a film, television or multimedia production or event for commercial distribution; and a franchise agreement. In each of these instances the license of the marketing intangible is intended to promote consumer sales. In the case of the license of a marketing intangible, where a taxpayer has actual evidence of the amount or proportion of its receipts that is attributable to [state], it shall assign such amount or proportion to [state]. In the absence of actual evidence of the amount or proportion of the licensee's receipts that are derived from [state] customers, the portion of the licensing fee to be assigned to [state] shall be reasonably approximated by multiplying the total fee by a percentage that reflects the ratio of the [state] population in the specific geographic area in which the licensee makes material use of the intangible property to regularly market its goods, services or other items relative to the total population in such area. Where the license of a marketing intangible is for the right to use the intangible property in connection with sales or other transfers at wholesale rather than directly to retail customers, the portion of the licensing fee to be assigned to [state] shall be reasonably approximated by multiplying the total fee by a percentage that reflects the ratio of the [state] population in the specific geographic area in which the licensee's goods, services, or other items are ultimately marketed using the intangible property relative to the total population of such area.

c. License of a Production Intangible.

Where a license is granted for the right to use intangible property other than in connection with the sale, lease, license, or other marketing of goods, services, or other items, and the license is to be used in a production capacity (a "production intangible"), the licensing fees paid by the licensee for such right are assigned to [state] to the extent that the use for which the fees are paid takes place in [state]. Examples of a license of a production intangible include, without limitation, the license of a patent, a copyright, or trade secrets to be used in a manufacturing process, where the value of the intangible lies predominately in its use in such process. In the case of a license of a production intangible, it shall be presumed that the use of the intangible property takes place in the state of the licensee's commercial domicile (where the licensee is a business) or the licensee's state of primary residence (where the licensee is an individual) unless the taxpayer or the Commissioner can reasonably establish the location(s) of actual use. Where the Commissioner can reasonably establish that the actual use of intangible property pursuant to a license of a production intangible takes place in part in [state], it shall be presumed that the entire use is in this state except to the extent that the taxpayer can demonstrate that the actual location of a portion of the use takes place outside [state].

Comment [A10]: Alternate proposed language:
"consumer"
"end user"
"consumer or end user"
"ultimate customer."

Comment [A11]: Consider adding "and materially"; would narrow the region of focus

Comment [A12]: Consider adding a final sentence to the effect that: "In the case of sales made in [to] a non-US jurisdiction it will be presumed that the marketing is not material unless the taxpayer shows otherwise."
A similar modification should be made with respect to the audience percentage rules set forth in the rule that pertains to "Services Delivered Electronically Through or on Behalf of an Individual or Business Customer."

Comment [A13]: There was a well-received suggestion to switch the structure to look first to use and then to presumption. *See* Proposed edit to section 5(c), License of a Production Intangible. The work group was split as to which approach it favored

Comment [A14]: Consider inserting a provision for separate-entity states clarifying that the presumption may not be used for related-party transactions.

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d. License of a Mixed Intangible.

Where a license of intangible property includes both a license of a marketing intangible and a license of a production intangible (a "mixed intangible") and the fees to be paid in each instance are separately and reasonably stated in the licensing contract, the Commissioner will accept such separate statement for purposes of this regulation ~~if it is reasonable~~. Where a license of intangible property includes both a license of a marketing intangible and a license of a production intangible and the fees to be paid in each instance are not separately and reasonably stated in the contract, it shall be presumed that the licensing fees are paid entirely for the license of the marketing intangible except to the extent that the taxpayer or the Commissioner can reasonably establish otherwise.

e. License of Intangible Property where Substance of Transaction Resembles a Sale of Goods or Services.

i. In general.

In some cases, the license of intangible property will resemble the sale of an electronically-delivered good or service rather than the license of a marketing intangible or a production intangible. In such cases, the receipts from the licensing transaction shall be assigned by applying the rules set forth in 4.c.ii(B) and (C), as if the transaction were a service delivered to an individual or business customer or delivered electronically through an individual or business customer, as applicable. Examples of transactions to be assigned under this section, 5.e include, without limitation, the license of database access, the license of access to information, the license of digital goods (*see* 7.b.), and the license of certain software (*e.g.*, where the transaction is not the license of pre-written software that is treated as the sale of tangible personal property, *see* 7.a).

ii. Sublicenses.

Pursuant to 5.e.i, the rules of 4.c.ii(C) may apply where a taxpayer licenses intangible property to a customer that in turn sublicenses the intangible property to end users as if the transaction were a service delivered electronically through a customer to end users. In particular, the rules set forth at 4.c.ii(C) that apply to services delivered electronically to a customer for purposes of resale and subsequent electronic delivery in substantially identical form to end users or other recipients may also apply with respect to licenses of intangible property for purposes of sublicense to end users, provided that for this purposes. the intangible property sublicensed to an end user shall not fail to be substantially identical to the property that was licensed to the sublicensor merely because the sublicense transfers a reduced bundle of rights with respect to such property (e.g., because the sublicensee's rights are limited to its own

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use of the property and do not include the ability to grant a further sublicense), or because such property is bundled with additional services or items of property.

f. Examples.

6. Sale of Intangible Property.

a. Assignment of Sales.

The assignment of a sale to a state or states in the instance of a sale or exchange of intangible property depends upon the nature of the intangible property sold. For purposes of this section, 6, a sale or exchange of intangible property includes a license of such property where the transaction is treated for tax purposes as a sale of all substantial rights in the property and the receipts from transaction are not contingent on the productivity, use or disposition of the property. For the rules that apply where the consideration for the transfer of rights is contingent on the productivity, use or disposition of the property, *see* 5.a and 6.a.iv.

i. Contract Right or Government License that Authorizes Business Activity in Specific Geographic Area.

In the case of a sale or exchange of intangible property where the property sold or exchanged is a contract right, government license or similar intangible property that authorizes the holder to conduct a business activity in a specific geographic area, the sale is assigned to a state if and to the extent that the intangible property is used or otherwise associated with the state. Where the intangible property is used in, or otherwise associated with, only this state the taxpayer shall assign the sale to [state]. Where the intangible property is used in or is otherwise associated with [state] and one or more other states, the taxpayer shall assign the sale to [state] to the extent that the intangible property is used in, or associated with, [state], through the means of a reasonable approximation.

ii. Agreement Not to Compete.

An agreement or covenant not to compete in a specified geographic area requires the contract party to refrain from conducting certain business activity in that specified area. In the case of an agreement or covenant not to compete the receipts are to be assigned to a state based upon the percentage that reflects the state's population in the U.S. geographic area specified in the contract relative to the total population in such area.

iii. Taxpayer Not Taxable in State of Assignment.

In any instance in which, pursuant to 6.a.i and ii, the state to which the sale is to be assigned can be determined or reasonably approximated, but where the taxpayer is not taxable in such state, the sale that would otherwise be assigned to such state shall be excluded from the numerator and denominator of the taxpayer's sales factor. *See* 1.f.ii.

iv. Sale that Resembles a License (Receipts are Contingent on Productivity, Use or Disposition of the Intangible Property).

In the case of a sale or exchange of intangible property where the receipts from the sale or exchange are contingent on the productivity, use or disposition of the property, the receipts from the sale shall be assigned by applying the rules set forth in 5 (pertaining to the license or lease of intangible property).

v. Sale that Resembles a Sale of Goods and Services.

In the case of a sale or exchange of intangible property where the substance of the transaction resembles a sale of goods or services and where the receipts from the sale or exchange do not derive from payments contingent on the productivity, use or disposition of the property, the receipts from the sale shall be assigned by applying the rules set forth in 5.e (relating to licenses of intangible property that resemble sales of goods and services). Examples of such transactions include those that are analogous to the license transactions cited as examples in 5.e.

vi. Excluded Sales.

The sale of a security as defined at [section] and the sale of business "goodwill" or similar intangible value, including, without limitation, "going concern value" and "workforce in place," shall be excluded from the numerator and denominator of a taxpayer's sales factor. . Also, except as otherwise provided in this regulation, the sale of intangible property that is not referenced in 6.a.i, ii, iv, or v, shall be excluded from the numerator and the denominator of the taxpayer's sales factor. The sale of intangible property that is not referenced in 6.a.i, ii, iv, or v, and that therefore is excluded from the numerator and denominator of the taxpayer's sales factor includes, without limitation, the sale of a partnership interest that is not otherwise a security within the meaning of [section].

b. Examples.

7. Special Rules.

a. Software Transactions.

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A license or sale of pre-written software for purposes other than commercial reproduction (or other exploitation of the intellectual property rights), when transferred on a tangible medium, is treated as the sale of tangible personal property, rather than as either the license or sale of intangible property or the performance of a service. In such cases, the receipts are in [state] as determined under the rules for the sale of tangible personal property set forth under Article IV. In all other cases, the receipts from a license or sale of software are to be assigned to [state] as determined otherwise under this regulation (e.g., depending on the facts, as the development and sale of custom software, *see* 4.c, as a license of a marketing intangible, *see* 5.b, as a license of a production intangible, *see* 5.c, as a license of intangible property where the substance of the transaction resembles a sale of goods or services, *see* 5.e, or as a sale of intangible property, *see* 6).

b. Sales or Licenses of Digital Goods or Services.

i. In general.

In the case of a sale or license of digital goods or services, including, among other things, the sale of various video, audio and software products or similar transactions, the receipts from the sale or license shall be assigned by applying the same rules as are set forth in 4.c.ii(B) or (C), as if the transaction were a service delivered to an individual or business customer or delivered through or on behalf of an individual or business customer. For purposes of the analysis, it is not relevant what the terms of the contractual relationship are or whether the sale or license might be characterized, depending upon the particular facts, as, for example, the sale or license of intangible property or the performance of a service. *See* 5.e. and (6)a.v.

ii. Telecommunications Companies.

In the case of a taxpayer that provides telecommunications or ancillary services and that is thereby subject to the provisions of [section], the sale or license of digital goods or services not otherwise assigned for apportionment purposes pursuant to that regulation shall be assigned pursuant to this section, 7.b.ii, by applying the rules set forth in 4.c.ii(B) or (C) as if the transaction were a service delivered to an individual or business customer or delivered through or on behalf of an individual or business customer. However, in applying such rules, if the taxpayer cannot determine the state or states where a customer receives the purchased product it may reasonably approximate this location using the customer's place of "primary use" of the purchased product, applying the definition of "primary use" set forth in [section].

c. Enforcement of Legal Rights.

Receipts attributable to the protection or enforcement of legal rights of a taxpayer through litigation, arbitration, or settlement of legal disputes or claims, including the filing and pursuit of claims under insurance contracts, shall be excluded from the numerator and denominator of the taxpayer's sales factor. For purposes of this rule, in the case of a settlement agreement, it shall not be relevant how the parties to the agreement characterize the payment made under the agreement.

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Examples

Examples Section 4.b.iv.

Assume in each of these examples that the taxpayer that provides the service is taxable in [state] and is to apportion its income pursuant to Article IV. Also, assume, where relevant, unless otherwise stated, that the taxpayer is taxable in each state other than [state] to which its sale or sales would be assigned, so that there is no requirement in such examples that such sale or sales be eliminated from the numerator and denominator of the taxpayer's sales factor. *See* 1.f.ii. Note that for purposes of the examples it is irrelevant whether the services are performed by an employee of the taxpayer or by an independent contractor acting on the taxpayer's behalf.

Example 1. Salon Corp has retail locations in [state] and in other states where it provides hair cutting services to individual and business customers, the latter of whom are paid for through the means of a company account. The sales of services provided at Salon Corp's in-state locations are in [state]. The sales of services provided at Salon Corp's locations outside [state], even when provided to state residents, are not in-state sales.

Example 2. Landscape Corp provides landscaping and gardening services in [state] and in neighboring states. Landscape Corp provides landscaping services at the in-state vacation home of an individual who is a resident of another state and who is located outside [state] at the time the services are performed. The sale of services provided at the in-state location is in [state].

Example 3. Same facts as in Example 2, except that Landscape Corp provides the landscaping services to Retail Corp, a corporation with retail locations in several states, and the services are with respect to such locations of Retail Corp that are in [state] and in other states. The sale of services provided to Retail Corp is in [state] to the extent the services are provided in [state].

Example 4. Camera Corp provides camera repair services at an in-state retail location to walk-in individual and business customers. In some cases, Camera Corp actually repairs a camera that is brought to its in-state location at a facility that is in another state. In such cases, the repaired camera is then returned to the customer at Camera Corp's in-state location. The sale of such services is in [state].

Example 5. Same facts as in Example 4, except that a customer located in [state] mails the camera directly to the out-of-state facility owned by Camera Corp to be fixed, and receives the repaired camera back in [state] by mail. The sale of the service is in [state].

Example 6. Teaching Corp provides seminars in [state] to individual and business customers. The seminars and the materials used in connection with the seminars are prepared outside the state, the teachers who teach the seminars include teachers that are resident outside the state, and the students who attend the seminars include

students that are resident outside the state. Because the seminars are taught in [state] the sales of the services are in [state].

Example 7. Bus Corp sells bus tickets to individual and business customers at bus depots located in [state] and in other states, and also through phone and Internet sales. The bus tickets are for travel to locations in [state] and to locations in other states. During the taxable year, Bus Corp sells 150,000 bus tickets. Each ticket has a departure location and an arrival location, for a total of 300,000 departure and arrival locations. Of these bus tickets, 25,000 have a departure location in [state] and 20,000 have an arrival location in [state]. The sale of such transportation services shall be assigned by multiplying Bus Corp's total revenues from such services by the percentage of Bus Corp's total departures and arrivals that take place in [state] relative to Bus Corp's total number of departures and arrivals. Therefore, Bus Corp must determine the amount of its ticket sales that are to be assigned to [state] by multiplying its total such sales by a fraction equal to 45,000 divided by 300,000, or .15. For purposes of the analysis it is irrelevant where and how the bus tickets are sold or whether the customer is an individual or business customer.

Examples Section 4.c.ii(A)(3)

Assume in each of these examples that the taxpayer that provides the service is taxable in [state] and is to apportion its income pursuant to Article IV. Also, assume, where relevant, unless otherwise stated, that the taxpayer is taxable in each state other than [state] to which its sale or sales would be assigned, so that there is no requirement in such examples that such sale or sales must be eliminated from the numerator and denominator of the taxpayer's sales factor. *See* 1.f.ii.

Example 1. Direct Mail Corp, a corporation based outside [state], provides direct mail services to its customer, Business Corp. Business Corp transacts with Direct Mail Corp to deliver printed fliers to a list of customers that is provided to it by Business Corp. Some of Business Corp's customers are in [state] and some of those customers are in other states. Direct Mail Corp will use the postal service to deliver the printed fliers to Business Corp's customers. The sale of Direct Mail Corp's services to Business Corp is assigned to [state] to the extent that the services are delivered on behalf of Business Corp to [state] customers (i.e., to the extent that the fliers are delivered on behalf of Business Corp to Business Corp's intended audience in [state]).

Example 2. Ad Corp is a corporation based outside [state] that provides advertising and advertising-related services in [state] and in neighboring states. Ad Corp enters into a contract at a location outside [state] with an individual customer who is not a [state] resident to design advertisements for billboards to be displayed in [state], and to design fliers to be mailed to [state] residents. All of the design work is performed outside [state]. The sale of the design services is in [state] because the service is physically delivered on behalf of the customer to the customer's intended audience in [state].

Example 3. Same facts as example 2, except that the contract is with a business customer that is based outside [state]. The sale of the design services is in [state]

because the services are physically delivered on behalf of the customer to the customer's intended audience in [state].

Example 4. Fulfillment Corp, a corporation based outside [state], provides product delivery fulfillment services in [state] and in neighboring states to Sales Corp, a corporation located outside [state] that sells tangible personal property through a mail order catalog and over the Internet to customers. In some cases when a customer purchases tangible personal property from Sales Corp to be delivered in [state], Fulfillment Corp will, pursuant to its contract with Sales Corp, deliver that property from its fulfillment warehouse located outside [state]. The sale of the fulfillment services of Fulfillment Corp to Sales Corp is assigned to [state] to the extent that Fulfillment Corp's deliveries on behalf of Sales Corp are to recipients in [state].

Example 5. Software Corp, a software development corporation, enters into a contract with a business customer, Buyer Corp, which is physically located in [state], to develop custom software to be used in Buyer Corp's business. Software Corp develops the custom software outside [state], and then physically installs the software on Buyer Corp's computer hardware located in [state]. The development and sale of the custom software is properly characterized as a service transaction, and the sale is assigned to [state] because the software is physically delivered to the customer in [state].

Example 6. Same facts as Example 5, except that Buyer Corp has offices in [state] and several other states, but is commercially domiciled outside [state] and orders the software from a location outside [state]. The receipts from the development and sale of the custom software service are assigned to [state] because the software is physically delivered to the customer in [state].

Examples Section 4.c.ii(B)(3)

Assume in each of these examples that the taxpayer that provides the service is taxable in [state] and is to apportion its income pursuant to Article IV. Also, assume, where relevant, unless otherwise stated, that the taxpayer is taxable in each state other than [state] to which its sale or sales would be assigned, so that there is no requirement in such examples that such sale or sales must be eliminated from the numerator and denominator of the taxpayer's sales factor. *See* 1.f.ii. Further, assume where relevant, unless otherwise stated, that the safe harbor set forth at 4.c.ii(B)2.d does not apply.

Example 1. Support Corp, a corporation that is based outside [state], provides software support and diagnostic services to individual and business customers that have previously purchased certain software from third-party vendors. These individual and business customers are located in [state] and other states. Support Corp supplies its services on a case by case basis when directly contacted by its customer. Support Corp generally provides these services through the Internet but sometimes provides these services by phone. In all cases, Support Corp verifies the customer's account information before providing any service. Using the information that Support Corp verifies before performing a service, Support Corp can determine where its services are received, and therefore must assign its sales to these locations. The sales made to Support Corp's individual and business customers are in [state] to the extent that Support Corp's services are received in [state]. *See* 4.c.ii(B)1 and 2.

Example 2. Online Corp, a corporation based outside [state], provides web-based services through the means of the Internet to individual customers who are resident in [state] and in other states. These customers access Online Corp's web services primarily in their states of residence, and sometimes, while traveling, in other states. For a substantial portion of its sales, either Online Corp can determine the state or states where such services are received, or, where it cannot determine such state or states, it has sufficient information regarding the place of receipt to reasonably approximate such state or states. However, Online Corp cannot determine or reasonably approximate the state or states of receipt for all of such sales. Assuming that Online Corp reasonably believes, based on all available information, that the geographic distribution of the sales for which it cannot determine or reasonably approximate the location of the receipt of its services generally tracks those for which it does have this information, Online Corp must assign to [state] the sales for which it does not know the customers' location in the same proportion as those sales for which it has this information. *See* 1.e.ii.

Example 3. Same facts as in Example 2, except that Online Corp reasonably believes that the geographic distribution of the sales for which it cannot determine or reasonably approximate the location of the receipt of its web-based services do not generally track the sales for which it does have this information. Online Corp must assign the sales of its services for which it lacks information as provided to its individual customers using the customers' billing addresses. *See* 4.c.ii(B)1.b.

Example 4. Same facts as in Example 3, except that Online Corp is not taxable in one state to which some of its sales would be otherwise assigned. The sales that would be otherwise assigned to that state are to be excluded from the numerator and denominator of Online Corp's sales factor. *See* 4.c.ii(B); 1.f.ii.

Example 5. Net Corp, a corporation based outside [state], provides web-based services to a business customer, Business Corp, a company with offices in [state] and two neighboring states. Particular employees of Business Corp access the services from computers in each Business Corp office. Assume that Net Corp determines that Business Corp employees in [state] were responsible for 75% of Business Corp's use of Net Corp's services, and Business Corp employees in other states were responsible for 25% of Business Corp's use of Net Corp's services. In such case, 75% of the sale is received in [state], and therefore 75% of the sale is in [state]. *See* 4.c.ii(B)2.a. Assume alternatively that Net Corp lacks sufficient information regarding the location or locations where Business Corp's employees used the services to determine or reasonably approximate such location or locations. Under these circumstances, if Net Corp derives 5% or less of its sales from Business Corp, Net Corp must assign the sale under 4.c.ii(B)2.c to the state where Business Corp principally managed the contract, or if that state is not reasonably determinable, to the state where Business Corp placed the order for the services, or if that state is not reasonably determinable, to the state of Business Corp's billing address. If Net Corp derives more than 5% of its sales of services from Business Corp, Net Corp is required to identify the state in which its contract of sale is principally managed by Business Corp and must assign the receipts to that state.

Example 6. Net Corp, a corporation based outside [state], provides web-based services through the means of the Internet to more than 250 individual and business

customers in [state] and in other states. Assume that for each customer Net Corp cannot determine the state or states where its web services are actually received, and lacks sufficient information regarding the place of receipt to reasonably approximate such state or states. Also assume that Net Corp does not derive more than 5% of its sales of services from any single customer. Net Corp may apply the safe harbor stated in 4.c.ii(B)2.d, and may assign its sales using each customer's billing address. If Net Corp is not taxable in one or more states to which some of its sales would be otherwise assigned, it must exclude those sales from the numerator and denominator of its sales factor. *See* 1.f.ii.

Examples Section 4.c.ii(C)(4)

Assume in each of these examples that the taxpayer that provides the service is taxable in [state] and is to apportion its income pursuant to Article IV. Also, assume, where relevant, unless otherwise stated, that the taxpayer is taxable in each state other than [state] to which its sale or sales would be assigned, so that there is no requirement in such examples that such sale or sales must be eliminated from the numerator and denominator of the taxpayer's sales factor. *See* 1.f.ii.

Example 1. Cable TV Corp, a corporation that is based outside of [state], has two revenue streams. First, Cable TV Corp sells advertising time to business customers pursuant to which the business customers' advertisements will run as commercials during Cable TV Corp's televised programming. Some of these business customers, though not all of them, have a physical presence in [state]. Second, Cable TV Corp sells monthly subscriptions to individual customers in [state] and in other states. Cable TV Corp's sale of advertising time to its business customers is assigned to [state] to the extent that the audience for Cable TV Corp's televised programming during which the advertisements run is in [state]. *See* 4.c.ii(C)1. If Cable TV Corp is unable to determine the actual location of its audience for the programming, and lacks sufficient information regarding audience location to reasonably approximate such location, Cable TV Corp must approximate its [state] audience using the percentage that reflects the ratio of its [state] subscribers in the geographic area in which Cable TV Corp's televised programming featuring such advertisements is delivered relative to its total number of subscribers in such area. *See* 4.c.ii(C)3.i. To the extent that Cable TV Corp's sales of monthly subscriptions represent the sale of a service, such sales are properly assigned to [state] in any case in which the programming is received by a customer in [state]. *See* 4.c.ii(B)1. In any case in which Cable TV Corp cannot determine the actual location where the programming is received, and lacks sufficient information regarding the location of receipt to reasonably approximate such location, such sales of Cable TV Corp's monthly subscriptions are assigned to [state] where its customer's billing address is in [state]. *See* 4.c.ii(B)1.b. Note that whether and to the extent that the monthly subscription fee represents a fee for a service or for a license of intangible property does not affect the analysis or result as to the state or states to which the sales are properly assigned. *See* 5.e.

Example 2. Network Corp, a corporation that is based outside of [state], sells advertising time to business customers pursuant to which the customers' advertisements will run as commercials during Network Corp's televised programming as distributed by unrelated cable television and satellite television transmission companies. Network Corp's sale of advertising time to its business customers is

assigned to [state] to the extent that the audience for Network Corp's televised programming during which the advertisements will run is in [state]. *See* 4.c.ii(C)1. If Network Corp cannot determine the actual location of the audience for its programming during which the advertisements will run, and lacks sufficient information regarding audience location to reasonably approximate such location, Network Corp must approximate the amount of the sales that constitutes [state] sales by multiplying the amount of such sales by a percentage that reflects the ratio of the [state] population in the specific geographic area in which the televised programming containing the advertising is run relative to the total population in such area. *See* 4.c.ii(C)3.i. In any case in which Network Corp's sales would be assigned to a state in which Network Corp is not taxable, such sales shall be excluded from the numerator and denominator of Network Corp's sales factor. *See* 1.f.ii.

Example 3. Web Corp, a corporation that is based outside [state], provides Internet content to viewers in [state] and other states. Web Corp sells advertising space to business customers pursuant to which the customers' advertisements will appear in connection with Web Corp's Internet content. Web Corp receives a fee for running the advertisements that is determined by reference to the number of times the advertisement is viewed or clicked upon by the viewers of its website. Web Corp's sale of advertising space to its business customers is assigned to [state] to the extent that the viewers of the Internet content are in [state], as measured by viewings or clicks. *See* 4.c.ii(C)1. If Web Corp is unable to determine the actual location of its viewers, and lacks sufficient information regarding the location of its viewers to reasonably approximate such location, Web Corp must approximate the amount of its [state] sales by multiplying the amount of such sales by a percentage that reflects the [state] population in the specific geographic area in which the content containing the advertising is delivered relative to the total population in such area. *See* 4.c.ii(C)3.i. In any case in which Web Corp's sales would be assigned to a state in which Web Corp is not taxable, such sales shall be excluded from the numerator and denominator of Web Corp's sales factor. *See* 1.f.ii.

Example 4. Retail Corp, a corporation that is based outside of [state], sells tangible property through its retail stores located in [state] and other states, and through a mail order catalog. Answer Co, a corporation that operates call centers in multiple states, contracts with Retail Corp to answer telephone calls from individuals placing orders for products found in Retail Corp's catalogs. In this case, the phone answering services of Answer Co are being delivered to Retail Corp's customers and prospective customers. Therefore, Answer Co is delivering a service electronically to Retail Corp's customers or prospective customers on behalf of Retail Corp, and must assign the proceeds from this service to the state or states from which the phone calls are placed by such customers or prospective customers. If Answer Co cannot determine the actual locations from which phone calls are placed, and lacks sufficient information regarding the locations to reasonably approximate such locations, Answer Co must approximate the amount of its [state] sales by multiplying the amount of its fee from Retail Corp by a percentage that reflects the [state] population in the specific geographic area from which the calls are placed relative to the total population in such area. *See* 4.c.i; 4.c.ii(C). Answer Co's sales shall also be excluded from the numerator and denominator of its sales factor in any case in which such sales would be assigned to a state in which Answer Co is not taxable. *See* 1.f.ii.

Example 5. Web Corp, a corporation that is based outside of [state], sells tangible property to customers via its Internet website. Design Co designed and maintains Web Corp's website, including making changes to the site based on customer feedback received through the site. Design Co's services are delivered to Web Corp, the proceeds from which are assigned pursuant to 4.c.ii(B). The fact that Web Corp's customers and prospective customers incidentally benefit from Design Co's services, and may even interact with Design Co in the course of providing feedback, does not transform the service into one delivered "on behalf of" Web Corp to Web Corp's customers and prospective customers.

Example 6. Wholesale Corp, a corporation that is based outside [state], develops an Internet-based information database outside [state] and enters into a contract with Retail Corp whereby Retail Corp will market and sell access to this database to end users. Depending on the facts, the provision of database access may be either the sale of a service or the license of intangible property or may have elements of both. Assume that on the particular facts applicable in this example Wholesale Corp is selling database access in transactions properly characterized as involving the performance of a service. When an end user purchases access to Wholesale Corp's database from Retail Corp, Retail Corp in turn compensates Wholesale Corp in connection with that transaction. In this case, Wholesale Corp's services are being delivered through Retail Corp to the end user. Wholesale Corp must assign its sales to Retail Corp to the state or states in which the end users receive access to Wholesale Corp's database. If Wholesale Corp cannot determine the state or states where the end users actually receive access to Wholesale Corp's database, and lacks sufficient information regarding the location from which the end users access the database to reasonably approximate such location, Wholesale Corp must approximate the extent to which its services are received by end users in [state] by using a percentage that reflects the ratio of the [state] population in the specific geographic area in which Retail Corp regularly markets and sells Wholesale Corp's database relative to the total population in such area. *See* 4.c.ii(C)3.ii. Note that it does not matter for purposes of the analysis whether Wholesale Corp's sale of database access constitutes a service or a license of intangible property, or some combination of both. *See* 5.e. In any case in which Wholesale Corp's sales would be assigned to a state in which Wholesale Corp is not taxable, such sales shall be excluded from the numerator and denominator of Wholesale Corp's sales factor. *See* 1.f.ii.

Examples Section 4.d.(4)

Unless otherwise stated, assume in each of these examples, where relevant: (a) that the taxpayer that provides the service is taxable in [state] and is to apportion its income pursuant to Article IV; (b) that the taxpayer is taxable in each state other than [state] to which its sale or sales would be assigned, so that there is no requirement in such examples that such sale or sales must be excluded from the numerator and denominator of the taxpayer's sales factor, *see* 1.f.ii; and (c) that the safe harbor set forth at 4.ii(A)3 does not apply~~; and (d) that the taxpayer's service at issue is not provided directly or indirectly to a RIC, *see* 4.d.iii(D)~~.

Example 1. Broker Corp provides securities brokerage services to individual customers who are resident in [state] and in other states. Assume that Broker Corp knows the state of primary residence for many of its customers, and where it does not know this state of primary residence, it knows the customer's billing address. Also

assume that Broker Corp does not derive more than 5% of its sales of services from any one individual customer. Where Broker Corp knows its customer's state of primary residence, it shall assign the sale to that state. Where Broker Corp does not know its customer's state of primary residence, but rather knows the customer's billing address, it shall assign the sale to that state. *See* 4.d.iii(A)1.

Example 2. Same facts as in Example 1, except that Broker Corp has several individual customers from whom it derives, in each instance, more than 5% of its sales of services. Sales to customers from whom Broker Corp derives 5% or less of its sales of services shall be assigned as described in example 1. For each customer from whom it derives more than 5% of its sales of services, Broker Corp is required to determine the customer's state of primary residence and must assign the receipts from the services provided to that customer to that state. In any case in which a 5% customer's state of primary residence is [state], a sale made to that customer must be assigned to [state]; in any case in which a 5% customer's state of primary residence is not [state] a sale made to that customer is not assigned to [state]. Where a sale is assigned to a state other than [state], if the state of assignment (i.e., the state of primary residence of the individual customer) is a state in which Broker Corp is not taxable, receipts from the sales shall be excluded from the numerator and denominator of Broker Corp's sales factor. *See* 4.d.iii(A); 1.f.ii.

Example 3. Architecture Corp provides building design services as to buildings located, or expected to be located, in [state] to individual customers who are resident in [state] and other states, and to business customers that are based in [state] and other states. Architecture Corp's sales are assigned to [state] because the locations of the buildings to which its design services relate are in [state], or are expected to be in [state]. For purposes of assigning these sales, it is not relevant where, in the case of an individual customer, the customer primarily resides or is billed for such services, and it is not relevant where, in the case of a business customer, the customer principally manages the contract, placed the order for the services or is billed for such services. Further, such sales are assigned to [state] even if Architecture Corp's designs are either physically delivered to its customer in paper form in a state other than [state] or are electronically delivered to its customer in a state other than [state]. *See* 4.d.iii(B).

Example 4. Law Corp provides legal services to individual clients who are resident in [state] and in other states. In some cases, Law Corp may prepare one or more legal documents for its client as a result of these services and/or the legal work may be related to litigation or a legal matter that is ongoing in a state other than where the client is resident. Assume that Law Corp knows the state of primary residence for many of its clients, and where it does not know this state of primary residence, it knows the client's billing address. Also assume that Law Corp does not derive more than 5% of its sales of services from any one individual client. Where Law Corp knows its client's state of primary residence, it shall assign the sale to that state. Where Law Corp does not know its client's state of primary residence, but rather knows the client's billing address, it shall assign the sale to that state. For purposes of the analysis it is irrelevant whether the legal documents relating to the service are mailed or otherwise delivered to a location in another state, or the litigation or other legal matter that is the underlying predicate for the services is in another state. *See* 4.d.ii(B) and iii(A)1.

Example 5. Same facts as in Example 4, except that Law Corp provides legal services to several individual clients who it knows have a primary residence in a state where Law Corp is not taxable. Receipts from these services shall be excluded from the numerator and denominator of Law Corp's sales factor even if the billing address of one or more of these clients is in a state in which Law Corp is taxable, including [state]. *See* 4.d.iii(A)1; 1.f.ii.

Example 6. Law Corp provides legal services to several multistate business clients. In each case, Law Corp knows the state in which the agreement for legal services that governs the client relationship is principally managed by the client. In one case, the agreement is principally managed in [state]; in the other cases, the agreement is principally managed in a state other than [state]. Where the agreement for legal services is principally managed by the client in [state] the sale of the services shall be assigned to [state]; in the other cases, the sale is not assigned to [state]. In the case of the sale that is assigned to [state], the sale shall be so assigned even if (1) the legal documents relating to the service are mailed or otherwise delivered to a location in another state, or (2) the litigation or other legal matter that is the underlying predicate for the services is in another state. *See* 4.d.ii(B) and iii(A)2.

Example 7. Same facts as in example 6, except that Law Corp is not taxable in one of the states other than [state] in which Law Corp's agreement for legal services that governs the client relationship is principally managed by the business client. Receipts from these latter services shall be excluded from the numerator and denominator of Law Corp's sales factor. *See* 4.d.iii, iii(A)2; 1.f.ii.

Example 8. Consulting Corp, a company that provides consulting services to law firms and other customers, is hired by Law Corp in connection with legal representation that Law Corp provides to Client Co. Specifically, Consulting Corp is hired to provide expert testimony at a trial being conducted by Law Corp on behalf of Client Co. Client Co pays for Consulting Corp's services directly. Assuming that Consulting Corp knows that its agreement with Law Co is principally managed by Law Corp in [state], the sale of Consulting Corp's services shall be assigned to [state]. It is not relevant for purposes of the analysis that Client Co is the ultimate beneficiary of Consulting Corp's services, or that Client Co pays for Consulting Corp's services directly. *See* 830 4.d.iii(A)2.

Example 9.[1] Bank Corp provides financial custodial services to 100 individual customers who are resident in [state] and in other states, including the safekeeping of some of its customers' financial assets. Assume for purposes of this example that Bank Corp knows the state of primary residence for many of its customers, and where it does not know this state of primary residence, it knows the customer's billing address. Also assume that Bank Corp does not derive more than 5% of its sales of all of its services from any single customer. Note that because Bank Corp does not have more than 250 customers, it may not apply the safe harbor for professional services stated in 4.d.iii(A)3. Where Bank Corp knows its customer's state of primary residence, it must assign the sale to that state. Where Bank Corp does not know its customer's state of primary residence, but rather knows the customer's billing address, it must assign the sale to that state. Bank Corp's sales are assigned to [state] if the customer's state of

[1] See Rule re: Financial Institutions, p. 22.

primary residence (or billing address, in cases where it does not know the customer's state of primary residence) is in [state], even if Bank Corp's financial custodial work, including the safekeeping of the customer's financial assets, takes place in a state other than [state]. *See* 4.d.iii(A)1, (C).

Example 10.[2] Same facts as Example 9, except that Bank Corp has more than 250 customers, individual or business. Bank Corp may apply the safe harbor for professional services stated in 4.d.iii(A)3, and may assign its sales to a state or states using each customer's billing address. ~~If Bank Corp is not taxable in one or more states to which some of its sales would be assigned, it must exclude the sales that would be assigned to those states from the numerator and denominator of its sales factor. *See* 4.d.iii, iii(C); 1.f.ii.~~

Example 11.[3] Same facts as Example 10, except that Bank Corp derives more than 5% of its sales from a single individual customer. As to the sales made to this customer, Bank Corp is required to determine the individual customer's state of primary residence and must assign the receipts from the service or services provided to that customer to that state. *See* 4.d.iii(A)1, iii(C). Sales to all other customers are assigned as described in Example 10.

Example 12. Advisor Corp, a corporation that provides investment advisory services, provides such advisory services to Investment Co. Investment Co is a multistate business client of Advisor Corp that uses Advisor Corp's services in connection with investment accounts that it manages for individual clients, who are the ultimate beneficiaries of Advisor Corp's services. Assume that Investment Co's individual clients are persons that are resident in numerous states, which may or may not include [state]. Assuming that Advisor Corp knows that its agreement with Investment Co is principally managed by Investment Co in [state], the sale of Advisor Corp's services shall be assigned to [state]. It is not relevant for purposes of the analysis that the ultimate beneficiaries of Advisor Corp's services may be Investment Co's clients, who are residents of numerous states. *See* 4.d.iii(A)2.

~~Example 13. Same facts as Example 12, except that in addition to providing investment advisory services to Investment Co, Advisor Corp also provides its advisory services to Mutual Fund Co, a regulated investment company with shareholders that are resident in numerous states, including this state. Advisor Corp is not a mutual fund service corporation; however Advisor Corp's services provided to Mutual Fund Co. constitute mutual fund sales within the meaning of this regulation. Advisor Corp's mutual fund sales to Mutual Fund Co shall be assigned to this state to the extent that Mutual Fund Co's shareholders of record are domiciled in this state. *See* 4.d.iii(D). However, unlike in the rule set forth generally in this regulation, there shall be no exclusion of such sales from the numerator and denominator of Advisor Corp's sales factor in any case in which such shareholders of record are domiciled in a state in which Advisor Corp is not taxable. In contrast to its mutual fund sales made to Mutual Fund Co, Advisor Corp's advisory services provided to Investment Co are assigned as stated in Example 12, and its sales to Investment Co shall be excluded from the numerator and~~

[2] See Rule re: Financial Institutions, p. 22.
[3] See Rule re: Financial Institutions, p. 22.

~~denominator of Advisor Corp's sales factor if such sales would be assigned to a state in which Advisor Corp is not taxable. *See* 4.d.iii, iii(A)2.~~

Example 14. Advisor Corp provides investment advisory services to Investment Fund LP, a partnership that invests in securities and other assets. Assuming that Advisor Corp knows that its agreement with Investment Fund LP is principally managed by Investment Fund LP in [state], the sale of Advisor Corp's services shall be assigned to [state]. *See* 4.d.iii(A)2. Note that, ~~unlike in the case of mutual fund sales (*see* 4.d.iii(D)),~~ it is not relevant for purposes of the analysis that the partners in Investment Fund LP are residents of numerous states~~.~~

Example 15. Design Corp is a corporation based outside [state] that provides graphic design and similar services in [state] and in neighboring states. Design Corp enters into a contract at a location outside [state] with an individual customer to design fliers for the customer. Assume that Design Corp does not know the individual customer's state of primary residence and does not derive more than 5% of its sales of services from the individual customer. All of the design work is performed outside [state]. The sale is in [state] if the customer's billing address is in [state]. *See* 4.d.iii(A)1.

Examples Section 5.f.

Assume in each of these examples that the taxpayer that licenses the intangible property is taxable in [state] and is to apportion its income pursuant to Article IV. Also, assume, where relevant, unless otherwise stated, that the taxpayer is taxable in each state other than [state] to which its sale or sales would be assigned, so that there is no requirement in such examples that such sale or sales must be eliminated from the numerator and denominator of the taxpayer's sales factor. *See* 1.f.ii.

Example 1. Crayon Corp and Dealer Co enter into a license contract under which Dealer Co as licensee is permitted to use trademarks that are owned by Crayon Corp in connection with Dealer Co's sale of certain products to retail customers. Under the contract, Dealer Co is required to pay Crayon Corp a licensing fee that is a fixed percentage of the total volume of monthly sales made by Dealer Co of products using the Crayon Corp trademarks. Under the contract, Dealer Co is permitted to sell the products at multiple store locations, including store locations that are both within and without [state]. Further, the licensing fees that are paid by Dealer Co are broken out on a per-store basis. The licensing fees paid to Crayon Corp by Dealer Co represent fees from the license of a marketing intangible. The portion of the fees to be assigned to [state] shall be determined by multiplying the fees by a percentage that reflects the ratio of Dealer Co's receipts that are derived from its [state] stores relative to Dealer Co's total receipts. *See* 5.b.

Example 2. Program Corp, a corporation that is based outside [state], licenses programming that it owns to licensees, such as cable networks, that in turn will offer the programming to their customers on television or other media outlets in [state] and in all other U.S. states. Each of these licensing contracts constitutes the license of a marketing intangible. For each licensee, assuming that Program Corp lacks evidence of the actual number of viewers of the programming in [state], the component of the licensing fee paid to Program Corp by the licensee that constitutes Program Corp's [state] sales is

determined by multiplying the amount of the licensing fee by a percentage that reflects the ratio of the [state] audience of the licensee for the programming relative to the licensee's total U.S. audience for the programming. *See* 5.b. If Program Corp is not taxable in any state in which the licensee's audience is located, the sales that would be assigned to such state shall be excluded from the numerator and denominator of Program Corp's sales factor. *See* 1.f.ii. Note that the analysis and result as to the state or states to which sales are properly assigned would be the same to the extent that the substance of Program Corp's licensing transactions may be determined to resemble a sale of goods or services, instead of the license of a marketing intangible. *See* 5.e.

Example 3. Moniker Corp enters into a license contract with Wholesale Co. Pursuant to the contract Wholesale Co is granted the right to use trademarks owned by Moniker Corp to brand sports equipment that is to be manufactured by Wholesale Co or an unrelated entity, and to sell the manufactured equipment to unrelated companies that will ultimately market the equipment to consumers in a specific geographic region, including a foreign country. The license agreement confers a license of a marketing intangible, even though the trademarks in question will be affixed to property to be manufactured. In addition, the license of the marketing intangible is for the right to use the intangible property in connection with sales to be made at wholesale rather than directly to retail customers. The component of the licensing fee that constitutes the [state] sales of Moniker Corp is determined by multiplying the amount of the fee by a percentage that reflects the ratio of the [state] population in the specific geographic region relative to the total population in such region. *See* 5.b. If Moniker Corp is not taxable in any state (including a foreign country) in which Wholesale Co's ultimate consumers are located, the sales that would be assigned to such state shall be excluded from the numerator and denominator of Moniker Corp's sales factor. *See* 1.f.ii.

Example 4. Formula, Inc and Appliance Co enter into a license contract under which Appliance Co is permitted to use a patent owned by Formula, Inc to manufacture appliances. The license contract specifies that Appliance Co is to pay Formula, Inc a royalty that is a fixed percentage of the gross receipts from the products that are later sold. The contract does not specify any other fees. The appliances are both manufactured and sold in [state] and several other states. Assume the licensing fees are paid for the license of a production intangible, even though the royalty is to be paid based upon the sales of a manufactured product (i.e., the license is not one that includes a marketing intangible). Because the Commissioner can reasonably establish that the actual use of the intangible property takes place in part in [state], the royalty is assigned based to the location of such use rather than to location of the licensee's commercial domicile, in accordance with 5.c. It is presumed that the entire use is in [state] except to the extent that the taxpayer can demonstrate that the actual location of some or all of the use takes place outside [state]. Assuming that Formula, Inc can demonstrate the percentage of manufacturing that takes place in [state] using the patent relative to such manufacturing in other states, that percentage of the total licensing fee paid to Formula, Inc under the contract will constitute Formula, Inc's [state] sales. *See* 5.c.

Example 5. Axel Corp enters into a license agreement with Biker Co in which Biker Co is granted the right to produce motor scooters using patented technology owned by Axel Corp, and also to sell such scooters by marketing the fact that the scooters were manufactured using the special technology. The contract is a license of both a marketing and production intangible, i.e., a mixed intangible. The scooters are

manufactured outside [state]. Assume that Axel Corp lacks actual information regarding the proportion of Biker Co's receipts that are derived from [state] customers. Also assume that Biker Co is granted the right to sell the scooters in a U.S. geographic region in which the [state] population constitutes 25% of the total population during the period in question. The licensing contract requires an upfront licensing fee to be paid by Biker Co to Axel Corp and does not specify what percentage of the fee derives from Biker Co's right to use Axel Corp's patented technology. Because the fees for the license of the marketing and production intangible are not separately and reasonably stated in the contract, it is presumed that the licensing fees are paid entirely for the license of a marketing intangible, unless either the taxpayer or Commissioner reasonably establishes otherwise. Assuming that neither party establishes otherwise, 25% of the licensing fee constitutes [state] sales. *See* 5.b and d.

Example 6. Same facts as Example 5, except that the license contract specifies separate fees to be paid for the right to produce the motor scooters and for the right to sell the scooters by marketing the fact that the scooters were manufactured using the special technology. The licensing contract constitutes both the license of a marketing intangible and the license of a production intangible. Assuming that the separately stated fees are reasonable, the Commissioner will: (1) assign no part of the licensing fee paid for the production intangible to [state], and (2) assign 25% of the licensing fee paid for the marketing intangible to [state]. *See* 5.d.

Example 7. Better Burger Corp, which is based outside [state], enters into franchise contracts with franchisees who agree to operate Better Burger restaurants as franchisees in various states. Several of the Better Burger Corp franchises are in [state]. In each case, the franchise contract between the individual and Better Burger provides that the franchisee is to pay Better Burger Corp an upfront fee for the receipt of the franchise and monthly franchise fees, which cover, among other things, the right to use the Better Burger name and service marks, food processes and cooking know-how, as well as fees for management services. The upfront fees for the receipt of the [state] franchises constitute fees paid for the licensing of a marketing intangible. These fees constitute [state] sales because the franchises are for the right to make [state] sales. The monthly franchise fees paid by [state] franchisees constitute fees paid for (1) the license of marketing intangibles (the Better Burger name and service marks), (2) the license of production intangibles (food processes and know-how) and (3) personal services (management fees). The fees paid for the license of the marketing intangibles and the production intangibles constitute [state] sales because in each case the use of the intangibles is to take place in [state]. *See* 5.b-c. The fees paid for the personal services are to be assigned pursuant to 4.

Example 8. Online Corp, a corporation based outside [state], licenses an information database through the means of the Internet to individual customers that are resident in [state] and in other states. These customers access Online Corp's information database primarily in their states of residence, and sometimes, while traveling, in other states. The license is a license of intangible property that resembles a sale of goods or services and shall be assigned in accordance with 5.e. If Online Corp can determine or reasonably approximate the state or states where its database is accessed, then it must do so. Assuming that Online Corp cannot determine or reasonably approximate the location where its database is accessed, Online Corp must assign the sales made to the individual customers using the customers' billing addresses to the extent known.

Assume for purposes of this example that Online Corp knows the billing address for each of its customers. In this case, Online Corp's sales made to its individual customers are in [state] in any case in which the customer's billing address is in [state]. *See* 4.c.ii(B)1.

Example 9. Net Corp, a corporation based outside [state], licenses an information database through the means of the Internet to a business customer, Business Corp, a company with offices in [state] and two neighboring states. The license is a license of intangible property that resembles a sale of goods or services and shall be assigned in accordance with 5.e. Assume that Net Corp cannot determine where its database is accessed but reasonably approximates that 75% of Business Corp's database access took place in [state], and 25% of Business Corp's database access took place in other states. In such case, 75% of the receipts from database access is in [state]. Assume alternatively that Net Corp lacks sufficient information regarding the location where its database is accessed to reasonably approximate such location. Under these circumstances, if Net Corp derives 5% or less of its receipts from database access from Business Corp, Net Corp must assign the sale under 4.c.ii(B)2 to the state where Business Corp principally managed the contract, or if that state is not reasonably determinable to the state where Business Corp placed the order for the services, or if that state is not reasonably determinable to the state of Business Corp's billing address. If Net Corp derives more than 5% of its receipts from database access from Business Corp, Net Corp is required to identify the state in which its contract of sale is principally managed by Business Corp and must assign the receipts to that state. *See* 4.c.ii(B)2.

Example 10. Net Corp, a corporation based outside [state], licenses an information database through the means of the Internet to more than 250 individual and business customers in [state] and in other states. The license is a license of intangible property that resembles a sale of goods or services and shall be assigned in accordance with 5.e. Assume that Net Corp cannot determine or reasonably approximate the location where its information database is accessed. Also assume that Net Corp does not derive more than 5% of its sales of database access from any single customer. Net Corp may apply the safe harbor stated in 4.c.ii(B)2.d, and may assign its sales to a state or states using each customer's billing address. If Net Corp is not taxable in one or more states to which some of its sales would be otherwise assigned, it must exclude those sales from the numerator and denominator of its sales factor. *See* 1.f.ii.

Example 11. Web Corp, a corporation based outside of [state], licenses an Internet-based information database to business customers who then sublicense the database to individual end users that are resident in [state] and in other states. These end users access Web Corp's information database primarily in their states of residence, and sometimes, while traveling, in other states. Web Corp's license of the database to its customers includes the right to sublicense the database to end users, while the sublicenses provide that the rights to access and use the database are limited to the end users' own use and prohibit the individual end users from further sublicensing the database. Web Corp receives a fee from each customer based upon the number of sublicenses issued to end users. The license is a license of intangible property that resembles a sale of goods or services and shall be assigned by applying the rules set forth in 4.c.ii(C). *See* 5.e. If Web Corp can determine or reasonably approximate the state or states where its database is accessed by end users, then it must do so. Assuming that Web Corp lacks sufficient information from which it can determine or

reasonably approximate the location where its database is accessed by end users, Web Corp must approximate the extent to which its database is accessed in [state] using a percentage that represents the ratio of the [state] population in the specific geographic area in which Web Corp's customer sublicenses the database access relative to the total population in such area. *See* 4.c.ii(C)3.ii.

Examples Section 6.b.

Assume in each of these examples that the taxpayer that provides the service is taxable in [state] and is to apportion its income pursuant to Article IV. Also, assume, where relevant, unless otherwise stated, that the taxpayer is taxable in each state other than [state] to which some of its sales would be assigned, so that there is no requirement in such examples that such sales to other states must be excluded from the taxpayer's numerator and denominator. *See* 1.f.ii.

Example 1. Airline Corp, a corporation based outside [state], sells its rights to use several gates at an airport located in [state] to Buyer Corp, a corporation that is based outside [state]. The contract of sale is negotiated and signed outside of [state]. The sale is in [state] because the intangible property sold is a contract right that authorizes the holder to conduct a business activity solely in [state]. *See* 6.a.i.

Example 2. Wireless Corp, a corporation based outside [state], sells a license issued by the Federal Communications Commission (FCC) to operate wireless telecommunications services in a designated area in [state] to Buyer Corp, a corporation that is based outside [state]. The contract of sale is negotiated and signed outside of [state]. The sale is in [state] because the intangible property sold is a government license that authorizes the holder to conduct business activity solely in [state]. *See id.*

Example 3. Same facts as in Example 2 except that Wireless Corp sells to Buyer Corp an FCC license to operate wireless telecommunications services in a designated area in [state] and an adjacent state. Wireless Corp must attempt to reasonably approximate the extent to which the intangible property is used in or associated with [state]. For purposes of making this reasonable approximation, Wireless Corp may rely upon credible data that identifies the percentage of persons that use wireless telecommunications in the two states covered by the license. *See id.*

Example 4. Same facts as in Example 3 except that Wireless Corp is not taxable in the adjacent state in which the FCC license authorizes it to operate wireless telecommunications services. The receipts paid to Wireless Corp that would be assigned to the adjacent state must be excluded from the numerator and denominator of Wireless Corp's sales factor. *See* 6.a.i.; 1.f.ii.

Example 5. Sports League Corp, a corporation that is based outside [state], sells the rights to broadcast the sporting events played by the teams in its league in all 50 U.S. states to Network Corp. Although the games played by Sports League Corp will be broadcast in all 50 states, the games are of greater interest in the northeast region of the country, including [state]. Because the intangible property sold is a contract right that authorizes the holder to conduct a business activity in a specified geographic area,

Sports League Corp must attempt to reasonably approximate the extent to which the intangible property is used in or associated with [state]. For purposes of making this reasonable approximation, Sports League Corp may rely upon audience measurement information that identifies the percentage of the audience for its sporting events in [state] and the other states. *See* 6.a.i.

Example 6. Same facts as in Example 5, except that Sports League Corp is not taxable in one state. The receipts paid to Sports League Corp that would be assigned to that state must be excluded from the numerator and denominator of Sports League Corp's sales factor. *See* 6.a.i.; 1.f.ii.

Example 7. Business Corp, a corporation based outside [state] engaged in business activities in [state] and other states, enters into a covenant not to compete with Competition Corp, a corporation that is based outside [state], in exchange for a fee. The agreement requires Business Corp to refrain from engaging in certain business activity in [state] and other states. The component of the fee that constitutes a sale in [state] is determined by multiplying the amount of the fee by a fraction represented by the percentage of the [state] population over the total population in the specified geographic region. *See* 6.a.ii. In any case in which a portion of the fee would be assigned to a state in which Business Corp is not taxable, such portion shall be excluded from the numerator and denominator of Business Corp's sales factor. *See* 1.f.ii.

Example 8. Business Corp, a corporation that is commercially domiciled in [state], sells all of its assets including its business goodwill, to a business customer that is based in [state]. The sale of the goodwill shall be excluded from the numerator and denominator of Business Corp's sales factor. *See* 6.a.vi.

Example 9. Inventor Corp, a corporation that is based outside [state], sells patented technology that it has developed to Buyer Corp, a business customer that is based in [state]. Assume that the sale is not one in which the receipts derive from payments that are contingent on the productivity, use or disposition of the property. *See* 6.a.iv. Inventor Corp understands that Buyer Corp is likely to use the patented technology in [state], but the patented technology can be used anywhere (i.e., the rights sold are not rights that authorize the holder to conduct a business activity in a specific geographic area). The sale of the patented technology shall be excluded from the numerator and denominator of Inventor Corp's sales factor. *See* 6.a.vi.

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