

Section 25136-2 is adopted to read:

§ 25136-2. Sales Factor. Sales Other than Sales of Tangible Personal Property in this State.

(a) In General. Sales other than those described under Revenue and Taxation Code Sections 25135 and 25136, subdivision (a), are in this state if the taxpayer's market for the sales is in this state.

(b) General Definitions.

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(4) "Intangible property" includes, but is not limited to, patents, copyrights, trademarks, service marks, trade names, licenses, plans, specifications, blueprints, processes, techniques, formulas, designs, layouts, patterns, drawings, manuals, trade secrets, stock, contract rights including broadcasting rights, and other similar intangible assets.

(A) A "marketing intangible" includes, but is not limited to, the license of a copyright, service mark, trademark, or trade name where the value lies predominantly in the marketing of the intangible property in connection with goods, services or other items.

(B) A "non-marketing and manufacturing intangible" includes, but is not limited to, the license of a patent, a copyright, or trade secret to be used in a manufacturing or other non-marketing process, where the value of the intangible property lies predominately in its use in such process.

(C) A "mixed intangible" includes, but is not limited to, the license of a patent, a copyright, service mark, trademark, trade name, or trade secrets where the value lies both in the marketing of goods, services or other items as described in subparagraph (A) and in the manufacturing process or other non-marketing purpose as described in subparagraph (B).

(5) "Reasonably approximated" means that, considering all sources of information other than the terms of the contract and the taxpayer's books and records kept in the normal course of business, the location of the market for the benefit of the services or the location of the use of the intangible property is determined in a manner that is consistent with the activities of the customer to the extent such information is available to the taxpayer. Reasonable approximation shall be limited to the jurisdictions or geographic areas where the customer or purchaser, at the time of purchase, will receive the benefit of the services or use of the intangible property, to the extent such information is available to the taxpayer. If population is a reasonable approximation, the population used shall be the U.S. population as determined by the most recent U.S. census data. If it can be shown

by the taxpayer that the benefit of the service is being substantially received or intangible property is being materially used outside the U.S., then the populations of those other countries where the benefit of the service is being substantially received or the intangible property is being materially used shall be added to the U.S. population. Information that is specific in nature is preferred over information that is general in nature.

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(7) "The use of intangible property in this state" means the location where the intangible property is employed by the taxpayer's customer or licensee. In the case of the complete transfer of all property rights in stock of a corporation or interest in a pass-through entity, the location of the use of the stock of the corporation or interest in the pass-through entity is the location of the use of the underlying assets of the corporation or pass-through entity.

(8) "To the extent" means that if the customer of a service receives the benefit of a service or uses the intangible property in more than one state, the gross receipts from the performance of the service or the sale of intangible property are included in the numerator of the sales factor according to the portion of the benefit of the services received and/or the use of the intangible property in this state.

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(d) Sales from intangible property are assigned to this state to the extent the property is used in this state.

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(2) In the case of the licensing, leasing, rental or other use of intangible property as defined in subsection (b)(4), not including sales of intangible property provided for in paragraph (1), the location of the use of the intangible property in this state shall be determined as follows:

(A) Marketing Intangible.

1. 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, the royalties or other licensing fees paid by the licensee for such right(s) are attributable to this state to the extent that the fees are attributable to the sale or other provision of goods, services, or other items purchased or otherwise acquired by the ultimate customers in this state. The contract between the taxpayer and the licensee of the intangible property or the taxpayer's books and records kept in the normal course of business shall be presumed to

provide a method for determination of the ultimate customers in this state for the purchase of goods, services, or other items in connection with the use of the intangible property. This presumption may be overcome by the taxpayer or the Franchise Tax Board by showing, based on a preponderance of the evidence, that the ultimate customers in this state are not determinable under the contract or the taxpayer's books and records.

2. If the location of the use of the intangible property is not determinable under subparagraph 1 or the presumption under subparagraph 1 is overcome, the location of the use of the intangible property shall be reasonably approximated. To determine the customer's or licensee's use of marketing intangibles in this state, factors that may be considered include the number of licensed sites in each state, the volume of property manufactured, produced or sold pursuant to the arrangement at locations in this state, or other data that reflects the relative usage of the intangible property in this state.
3. Where the license of a marketing intangible property 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 taxpayer may be unable to develop information regarding the location of the ultimate use of the intangible property. If this is the case, then the taxpayer may attribute the receipt to this state based solely upon the percentage of this state's population as compared with the total population of the geographic area in which the licensee uses the intangible property to market its goods, services or other items. The population used shall be the U.S. population, unless it can be shown by the taxpayer that the intangible property is being used materially in other parts of the world. If the taxpayer can show that the intangible property is being used materially in other parts of the world, then only the populations of those other countries where the intangible is being materially used shall be added to the U.S. population.

(B) Non-marketing and manufacturing intangibles.

1. 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, the licensing fees paid by the licensee for such right(s) are attributable to this state to the extent that the use for which the fees are paid takes place in this state. The terms of the contract between the taxpayer and the licensee of the intangible property or the taxpayer's books and records kept in the normal course of business shall be presumed to provide a method for determination of the extent of the use of the intangible property in this state. This presumption may be overcome by the taxpayer or the Franchise Tax Board by showing, based on a preponderance of the evidence, that the

extent of the use for which the fees are paid are not determinable under the contract or the taxpayer's books and records.

2. If the location of the use of the intangible property cannot be determined under subparagraph 1 or the presumption in subparagraph 1 is overcome, then the location of the use of the intangible property shall be reasonably approximated.
3. If the location of the use of the intangible property for which the fees are paid cannot be determined under subparagraphs 1 or 2, it shall be presumed that the use of the intangible property takes place in this state if the licensee's billing address is in this state.

(C) Mixed intangibles.

1. Where a license of intangible property includes both a license of a marketing intangible and a license of a non-marketing or manufacturing intangible, and the fees to be paid in each instance are separately stated in the licensing contract, the Franchise Tax Board will accept such separate statement for purposes of this section if it is reasonable. If the Franchise Tax Board determines that the separate statement is not reasonable, then the Franchise Tax Board may assign the fees using a reasonable method that accurately reflects the licensing of a marketing intangible and the licensing of a non-marketing or manufacturing intangible.
2. Where the fees to be paid in each instance are not separately stated in the contract, it shall be presumed that the licensing fees are paid entirely for the license of a marketing intangible except to the extent that the taxpayer or the Franchise Tax Board can reasonably establish otherwise. This presumption may be overcome, by a preponderance of the evidence, by the taxpayer or the Franchise Tax Board, that the licensing fees are paid for both the licensing of a marketing intangible and the licensing of a non-marketing or manufacturing intangible, and the extent to which the fees represent the marketing intangible and the non-marketing or manufacturing intangible.

(D) Examples.

1. Intangible Property – Marketing Intangible, subsection (d)(2)(A)1. Crayon Corp and Dealer Corp enter into a license agreement whereby Dealer Corp as licensee is permitted to use trademarks that are owned by Crayon Corp in connection with Dealer Corp's sale of certain products to retail customers. Under the contract, Dealer Corp is required to pay Crayon Corp a licensing fee that is a fixed percentage of the total volume of monthly sales made by Dealer Corp of products using the Crayon Corp trademarks. Under the agreement, Dealer Corp

is permitted to sell the products at multiple store locations, including store locations that are both within and without this state. The licensing fees that are paid by Dealer Corp are broken out on a per-store basis. The licensing fees paid to Crayon Corp by Dealer Corp represent fees from the licensing of a marketing intangible and the fees that are derived from the individual sales at stores in this state constitute sales in this state.

2. Intangible Property – Marketing Intangible, subsection (d)(2)(A)2. Moniker Corp enters into a license agreement with Sports Corp where Sports Corp is granted the right to use trademarks owned by Moniker Corp to brand sports equipment that is to be manufactured by Sports Corp or an unrelated entity, and to sell the manufactured product to unrelated companies that make retail sales in a specified geographic region. Although the trademarks in question will be affixed to the tangible property to be manufactured, the license agreement confers a license of a marketing intangible. Neither the contract between the taxpayer and the licensee nor the taxpayer's books and records provide a method for determination of this state's customers of equipment manufactured with Moniker Corp's trademarks. The component of the licensing fee that constitutes sales of Moniker Corp in this state is reasonably approximated by multiplying the amount of the fee by the percentage of this state's population over the total population in the specified geographic region in which the retail sales are made.
3. Intangible Property - Marketing Intangible, Wholesale, subsection (d)(2)(A)3. Cartoon Corp enters into a license agreement with Wholesale Corp where Wholesale Corp is granted the right to use Cartoon Corp's cartoon characters in the design and manufacture of tee shirts and sweatshirts which will be sold to various retailers who will in turn sell them to members of the public. Cartoon Corp is unable to develop information regarding the location of the ultimate customer of the products designed and manufactured in connection with Cartoon Corp's cartoon characters. Cartoon Corp shall assign the licensing fee by multiplying the fee by the percentage of this state's population over the total population in the geographic area in which Cartoon Corp markets its goods, services or other items.
4. Intangible Property – Non-marketing and Manufacturing Intangible, subsection (d)(2)(B)1. Formula Corp and Appliance Corp enter into a license agreement whereby Appliance Corp is permitted to use a patent owned by Formula Corp to manufacture and sell appliances at stores owned by Appliance Corp within a certain geographic region. The license agreement specifies that Appliance Corp is to pay Formula Corp a royalty equal to a fixed percentage of the gross receipts from the products sold. The contract does not specify any

other fees. The appliances are manufactured and sold in this state and several other states. Given these facts, it is presumed that the licensing fees are paid for the license of a manufacturing intangible. Since Formula Corp can demonstrate the percentage of manufacturing by Appliance Corp that takes place in this state using the patent, that percentage of the total licensing fee paid to Formula Corp under the contract will constitute Formula Corp's sales in this state.

5. Intangible Property – Non-marketing and Manufacturing Intangible, subsection (d)(2)(B)2. Mechanical Corp enters into a license agreement with Spa Corp where Spa Corp is granted the right to use the patents owned by Mechanical Corp to manufacture mechanically operated spa covers for spas that Spa Corp manufactures. Neither the terms of the contract nor the taxpayer's books and records indicate the extent of the use of the patent in this state. However, there is public information that Spa Corp has three manufacturing locations in this state and an additional six manufacturing locations in various other states. Mechanical Corp may reasonably approximate the location of the use of the intangible property and assign 33% of the licensing fees to this state.
6. Intangible Property - Non-marketing and Manufacturing Intangible, subsection (d)(2)(B)3. Same facts as Example 5 except that Spa Corp is a small, privately held manufacturing corporation that has no publicly available information as to its manufacturing locations, Mechanical Corp shall assign all of the licensing fees to this state if Spa Corp's billing address is in this state.
7. Intangible Property - Mixed Intangible, subsection (d)(2)(C)1. Axel Corp enters into a two-year license agreement with Biker Corp in which Biker Corp 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 scooters are manufactured outside this state, but the taxpayer is granted the right to sell the scooters in a geographic area in which this state's population constitutes 25% of the total population in the geographic area during the period in question. The license agreement 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 agreement constitutes both the license of a marketing intangible and the license of a non-marketing intangible. Assuming that the separately stated fees are reasonable, the Franchise Tax Board will: (1) attribute no part of the licensing fee paid for the non-marketing intangible to this state, and

(2) attribute 25% of the licensing fee paid for the marketing intangible to this state.

8. Intangible Property – Mixed Intangible, subsection (d)(2)(C)2. Same facts as Example 7, except that the licensing agreement requires an upfront licensing fee to be paid by Biker Corp to Axel Corp but does not specify which percentage of the fee is derived from Biker Corp's right to use Axel Corp's patented technology. Unless either the taxpayer or the Franchise Tax Board reasonably establishes otherwise, it is presumed that the licensing fees are paid entirely for the license of a marketing intangible. In such cases, it will be presumed that 25% of the licensing fee constitutes sales in this state.

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