Section 18 – No Receipts Rule

Examples

1. Taxpayer Bigbox Holdings, Inc. receives $100 million in dividends from domestic subsidiaries of Bigbox Retailing, Inc. and $100 million in “foreign-source” dividends from Bigbox Overseas Retailing, Ltd., a Canadian corporation, which is excluded from your state’s tax base. Bigbox Retailing’s apportionment factor in this state in the current year is 20% and was 18% in the prior year. Because the years in which Bigbox Retailing generated earning from which the dividends were paid cannot be reasonably determined, the average of the current and prior year’s apportionment factors (19%) must be used to apportion the domestic-source dividends.

1a. Same Facts, but Bigbox Holdings is not taxable in any other state or country in this year or the prior year. Accordingly, 81% ($81 million) of the taxpayer's domestic dividends are eliminated from the receipts factor under section 5 of this regulation. The taxpayer's gross receipts numerator in this state is 100% ($19 million/$19 million).

2. Taxpayer CB Holdings, Inc. is a Kansas corporation with one employee and one office in Dodge City, Kansas. During the tax year its gross income consisted entirely of a $160 million taxable dividend paid by CB REIT, Inc., a related party with its only office and employees in Dodge City.

CB REIT, Inc. was engaged exclusively in leasing retail properties directly to Crazy Bob Auto Parts, Inc., also a related party. CB REIT, Inc. had one employee and one office, also in Dodge City, Kansas during the tax year. $32 million of CB REIT's gross receipts were generated from leasing stores in this state, with the remainder of the $128 million in gross receipts derived from leasing retail properties equally distributed in States A, B, C, and D. CB Holdings, Inc. is taxable in this state and in states A, B, C, & D.

Although all of the taxpayer's dividend income is paid by CB REIT, under Subsection 1(a)(iii) of this regulation, $32 million of the taxpayer's receipts are assigned to this state because 20% of CB REIT's earnings were generated by the activities of Crazy Bob Auto Parts, Inc., a related party, in this state. The taxpayer's receipts factor in this state is $32million/$128 million.

2a. Same facts, except that taxpayer CB Holdings, Inc. is not taxable in states A, B, C and D, the other states in which CB REIT leases property. Under Section 5, $128 million of those receipts are eliminated from the receipts factor numerator and denominator, resulting in 100% of all remaining gross receipts ($32 million/$32 million) attributable to CB Holdings, Inc.'s gross receipts being assigned to this state.

2b. In the following year, CB Holdings, Inc. lends its excess capital to Crazy Bob Auto Parts, Inc., located in State Y, as an unsecured loan. As a result of that loan, CB Holdings, Inc. reports $40 million of interest income in addition to the $160 million of dividend income it received from CB REIT, Inc. Although CB Holdings, Inc. does not meet this state's definition of a financial institution, the receipts from lending activity ($40 million) will be included in the receipts factor pursuant to Subsection 1(c) and assigned to State Y as the location of the borrower.

Because CB Holdings, Inc. is only taxable in this state and state Y, this state's gross receipts numerator remains $32 million, as $128 million of the dividend income is still thrown out of the receipts factor denominator. The $40 million of loan income will be included in the receipts factor denominator of CB Holdings, Inc., resulting in a receipts factor in this state of $32million/$72 million, and $40million/$72 million in State Y.

3. Taxpayer Quick Sale Co. is a Maryland corporation formed by All States Nuclear Corp. with the intent of facilitating the disposition of its power plants located in three states. The stock was sold to Risky Investments for $500 million in cash, generated a capital gain of $100 million on the plant located in this state, and a capital loss of $25 million on each the two plants located elsewhere, for All States Nuclear Corp.

In the year preceding the sale, 30% of Quick Sale Co.'s apportionment factors were in this state. All States Nuclear Corp would include 30% of the capital gain ($30 million) for this state's receipts factor numerator and $100 million for the receipts factor denominator, but only if All States Nuclear had other apportionable "receipts" of $3 million or less in the year the gain was included in taxable income. Otherwise, neither the capital gain or capital losses would be included in the receipts factor numerator or denominator.

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In the year preceding the sale, 30% of Quick Sale Co.'s apportionment factors were in this state. All States Nuclear Corp would include 30% of the capital gain ($30 million) for this state's receipts factor numerator and $100 million for the receipts factor denominator, but only if All States Nuclear had other apportionable "receipts" of $3 million or less in the year the gain was included in taxable income. Otherwise, neither the capital gain or capital losses would be included in the receipts factor numerator or denominator.

3a. Same facts, but All States Nuclear Corp formed Quick Sale Corp. one day before its sale. In order to more clearly reflect the taxpayer’s business activity in this state, an alternative apportionment methodology must be used pursuant to Section 6 of this regulation and Compact Article IV, Section 18. Using the prior year’s apportionment percentages for All States Nuclear Corp could be a reasonable means of apportioning Quick Sale Corp’s gross receipts, since those gross receipts derived from the disposition of assets previously held by All State Nuclear Corp. A second alternative would be to sue the apportionment factors associated with the operations transferred to Quick Sale.

3b. Same facts, but the sale is structured as a IRC Sec. 338(h)(10) election and is deemed to be a sale of assets, not stock, under this state’s income tax conformity rules. Quick Sale Corp. is taxable in all three states in which it owned assets in the year of the sale; the capital gain would be apportioned based on the current year’s apportionment factors under Subsection 1(b).

4. Taxpayer Loan Participation Services, Inc. is a Delaware corporation formed by a related financial institution for the exclusive purpose of holding securitized loan portfolios in trust for unrelated parties in multiple countries. The taxpayer has no employees or property. The securitized loan portfolios consist of mortgage loans; 10% of those mortgage interests can be traced to real property in this state. Even though Loan Participation Services, Inc. would not be considered a financial institution under this state's laws, 10% of the portfolio's receipts derived from items including interest payments, late fees and origination fees are assignable to this state if this state has adopted the Multistate Tax Commission's model formula for the apportionment of financial institution income, or if the loan portfolio income would be assigned to this state under this state's apportionment formula for financial institutions.

5. Taxpayer IH Factoring, Inc. is a Delaware corporation with all twenty of its employees in Dover, Delaware. It exclusively purchases installment agreements (accounts receivable) from its parent corporation, Iron Horse Motorcycles, Inc., and re-sells those agreements (as securitized instruments) to institutional investors. IH Factoring would not be considered a financial institution under this state’s laws. Iron Horse Motorcycles has a 10% apportionment factor in this state, but 25% of its dealers’ purchase agreements sold to IH Factoring derive from loans to motorcycle customers in this state. 25% of IH Factoring Inc.’s gross receipts are assigned to this state.

Alternative Apportionment Example (for Section 3):

6. Taxpayer Windfall, Inc. is an indirectly wholly-owned subsidiary of ABC Manufacturing Company and its income is included on the water's edge unitary combined report filed by ABC Manufacturing Inc. and Combined Subsidiaries in this state; the numerator of the receipts factor for that group in this state is 3%. Windfall, Inc. has no property, payroll or receipts from transactions and activities undertaken in the regular course of its business. Windfall, Inc. receives $1 billion in settlement of ABC Manufacturing's long-standing patent infringement suit against a business competitor. Under Section 3(a) of this regulation, Windfall, Inc.'s receipts factor is 3%.

Alternative Apportionment Example (for Section 4):

7. Taxpayer Windfall, Inc. is included on the federal consolidated return of ABC Manufacturing Company and Consolidated Subsidiaries, and is required to file as a separate entity in this state. Windfall, Inc. has no property, payroll or receipts from transactions and activities undertaken in the regular course of its business. Windfall, Inc. receives a $1 billion settlement in connection with ABC Manufacturing Company's long-standing patent infringement suit. The federal consolidated group reported federal taxable income of $6 billion in the year the settlement amount was recognized. Its members with nexus in this state apportioned a combined total of $600 million to this state in that year. Under Section 4, Windfall, Inc.'s receipts factor numerator in this state is $100 million and its denominator is $1 billion.