

EXPOSURE DRAFT

The Rhode Island Division of Taxation is releasing this draft regulation to provide taxpayers and practitioners with an opportunity to review anticipated regulatory changes related to the implementation of mandatory combined reporting in Rhode Island. Mandatory combined reporting, enacted by law in June 2014, represents a sweeping change to the structure of Rhode Island's corporate income tax system, and takes effect for tax years beginning on or after January 1, 2015. This Exposure Draft anticipates the implementation of new apportionment rules associated with the introduction of mandatory combined reporting. Among other things, the new apportionment rules will provide taxpayers and practitioners with guidance related to single sales factor apportionment and market-based sourcing under Rhode Island's new corporate income tax regime.

Please submit comments on this Exposure Draft on or before **September 21, 2015** to:

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State of Rhode Island and Providence Plantations

**Rhode Island Division of Taxation
(Department of Revenue)**

Corporate Income Tax:

Apportionment of Net Income

Regulation CT 15-04

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State of Rhode Island and Providence Plantations
Rhode Island Department of Revenue
Division of Taxation

Public Notice of Proposed Rule-Making

Pursuant to the provisions of 42-35-3(a)(1) of the General Laws of Rhode Island, and in accordance with the Administrative Procedures Act Chapter 42-35 of the General Laws, the Division of Taxation hereby gives notice of its intent to amend a regulation regarding Apportionment of Net Income for Business Corporation Tax.

The purpose of this rule making is to implement Rhode Island General Laws (RIGL) Sections 44-11-13 through 44-11-15. This amendment provides guidance regarding Apportionment of Net Income for Business Corporation Tax. There is also a change in style and format. This regulation shall take effect **MONTH XX, 2015** and shall amend and supersede regulation CT 04-04; further identified by ERLID Number 2875 promulgated January 1, 2004.

The proposed regulation and concise summary of non-technical requirements and proposed new rules are available for public inspection at www.tax.ri.gov, in person at The Rhode Island Division of Taxation, or requested by e-mail at mcanole@tax.ri.gov or by calling Michael Canole at (401) 574-8729.

In the development of the proposed regulation, consideration was given to: (1) alternative approaches; (2) overlap or duplication with other statutory and regulatory provisions; and (3) whether the regulation, in and of itself, would have significant economic impact on small business. No alternative approach, duplication, or overlap was identified based upon available information.

All interested parties are invited to submit written or oral comments concerning the proposed regulations by **MONTH XX, 2015** to Michael Canole, Rhode Island Division of Taxation, One Capitol Hill, Providence, RI – telephone number (401) 574-8729 or via e-mail at mcanole@tax.ri.gov. A public hearing to consider the proposed regulation will be held on **DAY, MONTH XX, 2015 at 9:30 a.m.** at the Rhode Island Division of Taxation, One Capitol Hill, Providence, RI, at which time and place all persons interested therein will be heard. The room is accessible to the disabled and interpreter services for the hearing impaired will be provided if requested 48 hours prior to the hearing. Requests for this service can be made in writing to Michael Canole at Rhode Island Division of Taxation, One Capitol Hill, Providence, RI 02908 or by calling 401 574-8729.

**Rhode Island Department of Revenue
Division of Taxation**

Concise summary of all non-technical requirements pursuant to RIGL Section 42-35-3(a)(1) for Rules and Regulation regarding Nexus for Business Corporation Tax.

The purpose of this rule making is to implement Rhode Island General Laws (RIGL) Sections 44-11-13 through 44-11-15. This amendment provides guidance regarding Apportionment of Net Income for Business Corporation Tax. There is also a change in style and format.

This regulation shall take effect **MONTH XX, 2015 and shall amend and supersede regulation CT 04-04 further identified by ERLID Number 2875 promulgated January 1, 2004.**

State Of Rhode Island – Division Of Taxation

Business Corporation Tax

Regulation CT 04-04

Allocation of Income and Net Worth

For the purposes of this regulation, the following definitions apply:

1. The term "arithmetical mean" shall mean the sum of the factors available to the taxpayer divided by the number of fractions used:

EXAMPLE: If there are three denominators and only two numerators in the three factors, the taxpayer would still be able to divide by three.

2. The term "gross receipts from sales" shall mean the gross amount of the sale of inventory sold in the ordinary course of business less any appropriate returns and allowances for such sales

as recorded by the taxpayer for federal income tax purposes.

In the case of a taxpayer who qualifies to apportion (Regulation CT 88-01), its net income shall

be apportioned to the state by means of an allocation fraction computed as a simple arithmetical mean of three fractions:

The first of these fractions shall represent that part held or owned within this state of the average

net book value of the total tangible property (real estate and tangible personal property) held or

owned by the taxpayer during the taxable year without deduction on account of any encumbrances thereon. Rented property shall be valued at eight times the annual net rental rate

paid less annual sub-rentals received.

Inclusions in property factor:

1. ——— Inventory

2. ——— Depreciable Assets

3. ~~Leasehold Improvements~~
4. ~~Land~~
5. ~~Construction in progress to the extent shown as a capital asset on the books of the taxpayer~~
6. ~~Rental Property~~

~~The second of these fractions shall represent that part of the taxpayer's total receipts from sales or other sources during the taxable year which is attributable to the taxpayer's activities or transactions within this state during the taxable year, meaning and including within such part as being thus attributable receipts from:~~

- a. ~~gross sales of its tangible personal property (inventory sold in the ordinary course of business) where shipments are made to points within this state;~~
- b. ~~gross income from services performed within this state;~~
- c. ~~gross income from rentals from property situated within the state;~~
- d. ~~net income from the sale of real and personal property, other than inventory sold in the ordinary course of business as described in (a) above, or other capital assets located in the state;~~
- e. ~~net income from the sale or other disposition of securities or financial obligations;~~ and
- f. ~~gross income from all other receipts within this state.~~

~~Inclusion in receipts factor:~~

1. ~~Gross receipts defined above as gross receipts from sales.~~
2. ~~Dividends less exclusions for Rhode Island purposes, such as dividends received from shares of stock of any payee liable for taxes as outlined in Chapters 11, 13 and 14 of the Rhode Island General Laws and dividends excluded for federal tax purposes~~
3. ~~Interest less exclusions for Rhode Island purposes, such as interest on certain obligations of the U.S. and its possessions or interest on obligations of Rhode Island Public Service Corporations.~~

- ~~4. Rent.~~
- ~~5. Royalties.~~
- ~~6. Net capital gain as reported for federal tax purposes.~~
- ~~7. Net ordinary gain as reported for federal tax purposes.~~
- ~~8. Other income.~~
- ~~9. Income exempt for federal taxation but taxable for Rhode Island purposes, such as income from obligations from other states.~~

~~THE GROSS RECEIPTS FACTOR CANNOT BE LESS THAN 0%~~

~~The third fraction shall represent that part of the total wages, salaries and other compensation to officers, employees and agents paid or incurred by the taxpayer during the taxable year which is attributable to services performed in connection with the taxpayer's activities or transactions within this state during the taxable year.~~

~~MANUFACTURERS~~

~~In the case of manufacturers whose principal business is described in Sector 31, 32, or 33 of the North American Industry Classification System as adopted by the United States Office of Management and Budget and as revised from time to time, may, in lieu of apportioning its net income to this state based on the allocation fraction described in section 44-11-14(a), elect for any year to apportion its net income to this state on the following allocation fraction:~~

~~For the tax year beginning on or after January 1, 2004, but before January 1, 2005, thirty percent (30%) of the property factor, thirty percent (30%) of the payroll factor and forty percent (40%) of the receipts factor may be used.~~

~~For tax years beginning on or after January 1, 2005, twenty-five percent (25%) of the property factor, twenty-five percent (25%) of the payroll factor and fifty percent (50%) of the receipts factor may be used.~~

MOTOR CARRIERS

In the case of motor carriers, the following method is used to determine the numerator of each factor.

1. ~~Property Factor:~~

~~Consists of the average net book value of situs assets plus a portion of the net book value of the line-haul vehicles. In determining the net book value of line-haul vehicles, compare Rhode Island pick up and delivery equipment to pick up and delivery equipment everywhere to arrive at a percentage due to Rhode Island for line-haul equipment. For a motor carrier who does not have a Rhode Island facility, but who regularly picks up and delivers in Rhode Island, delivery equipment will be apportioned to Rhode Island upon its Rhode Island activities. Rental property shall be valued at eight times the annual net rental paid less annual sub-rentals received.~~

2. ~~Receipts Factor:~~

~~Average of the inbound/outbound Rhode Island receipts plus all other receipts attributable to Rhode Island.~~

3. ~~Salaries and Wages Factor:~~

~~Consists of the situs wages plus a portion of the line-haul wages. Rhode Island line-haul wages are determined by the percentage of activity in Rhode Island.~~

~~For a motor carrier who does not have a Rhode Island facility, but who regularly picks up and delivers in Rhode Island, drivers' wages will be apportioned to Rhode Island based upon its Rhode Island activities.~~

AIRLINES

In the case of airlines, the following method is used to determine the numerator of each factor:

1. Property Factor:

Situs assets shall be included based on the average net book value. Flight aircraft shall be included based on the following ratio: mileage of aircraft, by type, flown in this state compared to total aircraft mileage flown everywhere, multiplied by the net book value of flight aircraft everywhere.

Rental property shall be valued at eight times the annual net rental paid less annual subrentals received.

2. Receipts Factor:

Passenger revenue and freight revenue shall be allocated to Rhode Island based on the ratio of departures of flight aircraft, by type, from locations in this state compared to total departures everywhere, multiplied by total passenger revenue everywhere.

All other receipts attributable to Rhode Island shall also be included in the numerator.

3. Salaries and Wages Factor:

Situs wages shall be included plus a portion of flight payroll. Flight payroll shall be included based on the following ratio: mileage of aircraft, by type, flown in this state compared to total

SPECIALTY RECEIPTS

For those taxpayers whose Rhode Island receipts includes sums from the exercise of various legal rights such as patents, copyrights, royalties, franchises, licenses, etc. which are used, broadcast or copied (in any media) such receipts shall be included in the numerator of the gross

~~receipts factor and the total of such receipts shall be included in the denominator. A patent is used in Rhode Island to the extent that it is employed in fabrication, manufacturing, production or other processing in Rhode Island or to the extent that a patented product is produced in Rhode Island.~~

~~A copyright is used in Rhode Island to the extent that printing or other publication originated therein.~~

~~Broadcast media is used in Rhode Island to the extent that the Rhode Island target audience is determinable as a part of the total audience. If the Rhode Island target audience is not determinable, then the entire receipts from the Rhode Island source are includible in the numerator of the gross receipts factor.~~

~~R. GARY CLARK
TAX ADMINISTRATOR~~

~~THIS REGULATION AMENDS AND SUPERCEDES REGULATION CT 04-04 PROMULGATED JANUARY 1, 2004.~~

STATE OF RHODE ISLAND – DIVISION OF TAXATION
BUSINESS CORPORATION TAX

APPORTIONMENT OF NET INCOME

REGULATION CT 15-04

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Rule 1. Purpose

These rules and regulations implement RIGL § 44-11-13 through § 44-11-15. These sections allow for apportionment of net income for businesses within and partially within the state.

Rule 2. Authority

These rules and regulations are promulgated pursuant to RIGL § 44-11-13 through § 44-11-15, and RIGL § 44-1-4, which authorizes the Rhode Island tax administrator to make rules and regulations, as the administrator may deem necessary for the proper administration and enforcement of the tax laws of this state. The rules and regulations have been prepared in accordance with the requirements in RIGL § 42-35-1 et seq. of the Rhode Island Administrative Procedures Act.

Rule 3. Application

These rules and regulations shall be liberally construed so as to permit the Division of Taxation the authority to effectuate the purpose of RIGL § 44-11-13 through § 44-11-15 and other applicable state laws and regulations. This Regulation explains apportionment for corporations, pass-through entities, sole proprietorships, and other business types as required. All examples in this Regulation are provided solely for the purpose of illustrating basic concepts that are set forth in the Rules herein, and may not introduce all relevant considerations. Such examples shall not serve as precedents in administrative hearings or other legal proceedings, and are not intended to cover all possible situations.

Rule 4. Severability

If any provision of these rules and regulations, or the application thereof to any person or circumstance, is held invalid by a court of competent jurisdiction, the validity of the remainder of the rules and regulations shall not be affected thereby.

Rule 5. Definitions

The term "Allocation" is used interchangeably with the term "Apportionment" and shall have the same meaning and effect.

"Apportionment" means the formula used to determine the amount of income that is attributable to Rhode Island by a combined group or any other taxpayer.

"Arithmetical mean" means the sum of the factors available to the taxpayer divided by the number of fractions used.

"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 United States 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 receipts from such sales.

“C corporation” means a corporation organized under subchapter C of the Internal Revenue Code, as defined in Section 1504 of that subchapter. For the purposes of this Regulation, the term includes those entities treated as C corporations for federal tax purposes.

“Combined group” means a group of two or more corporations in which more than fifty percent (50%) of the voting stock of each member corporation is directly or indirectly owned by a common owner or owners, either corporate or non-corporate, or by one or more of the member corporations, and that are engaged in a unitary business.

“Common ownership” means more than fifty percent (50%) of the voting control of each member of the group is directly or indirectly owned by a common owner or owners, either corporate or non-corporate, whether or not the owner or owners are members of the combined group.

“Corporation” has the meaning set forth in RIGL § 44-11-1(4), and for purposes of mandatory unitary combined reporting under the Rhode Island General Laws, includes an LLC, partnership, or other entity electing to be taxed as a corporation for federal tax purposes. Although a partnership or other pass-through entity may not always be considered a corporation includible in the combined group on an entity basis as a member, when a partnership or other pass-through entity is directly or indirectly held by a corporation, the business conducted by such a partnership or pass-through entity is considered the business of the corporation to the extent of the corporation’s distributive share of the partnership or pass-through entity net income.

“Cost of performance sourcing” means the sourcing method used for gross receipts from transactions other than sales of tangible personal property under the three-factor apportionment formula set forth in Rule 9 of this Regulation.

“Division of Taxation” means the Rhode Island Department of Revenue, Division of Taxation. The Division of Taxation may also be referred to as the “Division” or the “Tax Division.”

“Documentary evidence” means journals, books of account, invoices, expense reports, or other records maintained in the regular course of business, or any other records required to be maintained for legal or accounting purposes.

“Income-producing activity” means, for each separate item of income, the transactions and activity directly engaged by the taxpayer for the ultimate purpose of obtaining profit or gain. For apportionment purposes, such activity does not include transactions and activities performed on behalf of a taxpayer, such as those conducted on the taxpayer’s behalf by an independent contractor. Income-producing activity includes, but is not limited to:

- (a) The rendering of personal services by employees or the utilization of tangible and intangible property by the taxpayer in performing a service;

- (b) The sale, rental, leasing, licensing the use of, or other use of real property; and
- (c) The rental, leasing, licensing the use of, or other use of tangible or intangible personal property.

“Individual customer” means any customer that is not a business customer.

“Intangible property” within the meaning of this Regulation 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 computer software.

“Market based sourcing” means the sourcing method used for gross receipts from transactions other than sales of tangible personal property under the single sales factor apportionment formula set forth in Rule 8 of this Regulation.

“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 seller, resulting in a contract with the seller.

“Single sales factor” means the apportionment fraction set forth in Rule 8 of this Regulation. The sales factor may also be referred to as the “receipts factor” or “gross receipts factor”.

“State where a contract of sale is principally managed by the customer,” means the primary location at which an employee or other representative of a customer serves as the primary contact person for the seller with respect to the implementation and day-to-day execution of a contract entered into by the seller with the customer.

“Taxpayer” means and includes any person subject to taxation under the Rhode Island General Laws. For tax years beginning on or after January 1, 2015, a combined group is included within the definition of taxpayer.

“Three-factor apportionment” means the apportionment formula set forth in Rule 9 of this Regulation. The three-factor apportionment formula takes into account the property factor, the payroll factor, and the sales factor of the trade or business of the taxpayer.

“Unitary business” means the activities of a group of two or more corporations under common ownership that are sufficiently interdependent, integrated or interrelated through their activities so as to provide mutual benefit and produce a significant sharing or exchange of value among them or a significant flow of value between the separate parts.

Rule 6. Appportionment – Generally

(a) **Purpose of Apportionment.** The purpose of apportionment is to determine the amount of income attributable to Rhode Island by any taxpayer under the Rhode Island General Laws (RIGL).

(b) **Business Income vs. Non-Business Income.** Rhode Island does not distinguish between business income and non-business income for formulary apportionment purposes.

(c) **Combined Group Members' Share of Tax.** The use of a combined report does not disregard the separate identities of the taxpayer members of the combined group. Each taxpayer member is responsible for tax based on its taxable income or loss apportioned to this state. Thus, only those members in a combined group that have corporate income tax nexus with Rhode Island shall be assessed a tax on the combined group's Rhode Island-apportioned net income. Any member in a combined group that lacks corporate income tax nexus with Rhode Island shall not be responsible for the tax assessed on the combined group.

(d) **Apportionment of Income Derived Entirely Within State.** In the case of any taxpayer, including a C corporation, deriving all its income from sources within this state, or engaging in activities or transactions wholly within this state for the purpose of profit or gain, or where said taxpayer does not have a regular place of business outside of this state other than a statutory office, one hundred (100%) percent of its net income shall be apportioned to this state.

(1) **Note.** For tax years beginning on or after January 1, 2015, any corporation that independently meets the criteria set forth in Rule 6(d) above, but which is also a member in a combined group subject to RIGL § 44-11 that derives income from sources both within and outside of this state for the purpose of profit or gain, shall be included in the combined group's combined return.

Examples.

(A) During the 2014 through 2016 tax years, Independent Man Corp., a Rhode Island C corporation unaffiliated with any other business entity, derives 100% of its income from the sale of yellow and green paper cups. For tax years 2014 through 2016, all of Independent Man Corp.'s income shall be apportioned to Rhode Island.

(B) For tax year 2017, Independent Man Corp. is acquired by Lemon, Inc. and becomes part of a combined group with multiple members, not all of whom derive income entirely from Rhode Island sources. A combined return must be filed with the Division of Taxation on behalf of the combined group. The combined group derives only a portion of its income from Rhode Island sources, but Independent Man Corp. continues to derive 100% of its income from sources within Rhode Island. The combined group's income will be apportioned to Rhode Island as set forth in Rule 6(e)(2) of this Regulation and Independent Man Corp.'s income and apportionment information must be included on a schedule attached to the combined group's combined return.

(e) **Apportionment of Income Derived Partially within State.**

(1) **Pre-2015.** For tax years beginning before January 1, 2015, all taxpayers that derive their income from sources both within and outside of this state for the purpose of profit or gain, shall apportion net income to this state by means of a three-factor apportionment formula, using sales (receipts), property, and payroll, as set forth in RIGL § 44-11-14(a), and as detailed in Rule 9 of this Regulation. In certain cases, a taxpayer may use a

special apportionment formula available under RIGL §§ 44-11-14.1 through 44-11-14.6, as detailed in Rule 10 of this Regulation.

Example:

During tax year 2013, Quahog Jewelry LLC and Netop Corp. are separate business entities engaged in the manufacture, design, and sale of expensive charm bracelets derived from Rhode Island seashells. Both companies sell their wares in Rhode Island and also more widely throughout the United States. Quahog Jewelry LLC operates a manufacturing facility in Massachusetts, whereas Netop Corp. manufactures all of its bracelets in Rhode Island. Both companies own retail locations in Rhode Island and nowhere else. Because both companies – one an LLC and the other a corporation – derive income from sources both within and outside of this State in a pre-2015 tax year, they must both apportion their income according to a three-factor apportionment formula on the basis of sales, property and payroll, consistent with Rules 9 and 10 of this Regulation.

(i) **Note.** For tax years beginning before January 1, 2015, the existence of a combined group shall be disregarded, and a combined group shall not be considered a taxpayer within the meaning of this Regulation.

(2) **2015 and Thereafter – C Corporations and Combined Groups.** For tax years beginning on or after January 1, 2015, all C corporations and combined groups deriving income from sources both within and outside of this state, or engaging in any activities or transactions both within and outside of this state for the purpose of profit or gain, including those C corporations that are members in a combined group and those that are not members in a combined group, shall apportion net income to this state by means of an allocation fraction. The fraction shall be computed by means of a simple arithmetical operation employing a single factor that represents total receipts from sales or other sources during the taxable year which is attributable to the taxpayer's activities or transactions within this state during the taxable year, as set forth in RIGL § 44-11-14 (b), and as detailed in Rule 8 of this Regulation. In limited cases, such C corporations may use a special apportionment formula available under RIGL §§ 44-11-14.1 through 44-11-14.6, and as detailed in Rule 11 of this Regulation.

(i) **Combined Group Tax Liability Determinations.** When a C corporation subject to tax under Chapter 44-11 of the Rhode Island General Laws is a member in a combined group, the corporation must determine the tax liability of the combined group and its own individual tax liability based upon the income and apportionment information of all members in the combined group, using a combined report as set forth in RIGL § 44-11-4.1, and subject to exclusions therein, if any.

(ii) **Federal Affiliated Groups.** An affiliated group of C corporations, as defined in section 1504 of the Internal Revenue Code, may elect to be treated as a combined group with respect to the combined reporting requirement imposed by RIGL § 44-11-4.1(a), as set forth in **Rule ** of Regulation CT-****, and subject to the statutory and regulatory conditions set forth therein.

(3) **2015 and Thereafter – Other Taxpayers.** For tax years beginning **on or after** January 1, 2015, any taxpayer that derives income from sources both within and outside of this state or engages in any activities or transactions both within and outside of this state for the purpose of profit or gain, but which is not:

- (i) a C corporation;
- (ii) a combined group with a C corporation member; or
- (iii) a member in a combined group with a C corporation member,

shall apportion net income to this state by means of a three-factor apportionment formula, using sales (receipts), property, and payroll, as set forth in RIGL § 44-11-14(a), and as detailed in Rule 9 of **this Regulation CT 15-04**. In the case of a combined group without a C corporation member, no combined report shall be filed on behalf of the combined group. In certain cases, a taxpayer subject to this provision may use a special apportionment formula available under RIGL §§ 44-11-14.1 through 44-11-14.6, and as detailed in Rule 10 of **this Regulation CT 15-04**.

Rule 7. Combined Reporting Requirement for Tax Years Beginning on or After January 1, 2015.

(a) **Commencement of Mandatory Unitary Combined Reporting.** For tax years beginning **on or after** January 1, 2015, a C corporation must report on its Rhode Island corporate income tax return not only its own income, but also the combined income of the other corporations that are members in its combined group. The C corporation must treat all such corporations and affiliates as if they comprise one, single unitary company, and combine all income into a single pool. Thus, each member in the combined group must include all receipts, i.e., total receipts or gross receipts, from sales or other sources, without regard to whether the member has corporate income tax nexus in this state. In calculating the single sales factor for a combined group, receipts between members included in the group must be eliminated.

(b) **Treatment of C Corporation’s Pass-Through Entity Income.** When a partnership or other pass-through entity does not elect to be taxed as a corporation for federal tax purposes and is directly or indirectly held by a corporation, including any member in a combined group, then the business conducted by the partnership or pass-through entity shall be considered the business of the corporation to the extent of the corporation’s distributive share of the partnership or pass-through entity income. Such distributive share shall be included in the net income calculations of the corporation and the combined group, and shall be apportioned to Rhode Island for corporate income tax purposes as set forth in this Regulation, consistent with the decision reached by the Rhode Island Supreme Court in *Homart Dev. Co. v. Norberg*, 529 A.2d 115 (R.I. 1987).

(c) **Single Sales Factor Apportionment.** For purposes of combined reporting, a C corporation must use the single sales factor apportionment formula, as described in Rule 8 of this Regulation. The purpose of apportionment in the context of combined reporting is to determine the combined group’s Rhode Island source income, which is taxable. In determining the combined group’s taxable income in this manner, the Division of Taxation is merely measuring the in-state activities of the combined group, and not imposing a tax on members in the combined group that lack nexus with Rhode Island or that are protected from Rhode Island taxation by Public Law 86-

272. After determining through such an apportionment formula the amount of a combined group's net income apportioned to Rhode Island, combined group net income is solely attributed to and tax is solely imposed on those members in the combined group that have corporate income tax nexus with Rhode Island.

(d) Members of the Combined Group with Different Accounting Periods:

(1) Mandatory Election of Uniform Accounting Period. If the taxable year of a member in a combined group differs from the taxable year of the combined group, the designated agent shall elect to determine the portion of that member's income to be included in one of the following ways:

- (i) a separate income statement prepared from the books and records for the months included in the group's taxable year; or
- (ii) including all of the income for the year that ends during the group's taxable year.

(2) Year-to-Year Consistency Requirement. The same method must be used for each member with a different accounting period. Once an election is made under this section, it is the only method that may be used from year to year with respect to members in the combined group, except upon prior written approval of the Tax Administrator.

Rule 8. Single Sales Factor Apportionment and Market Based Sourcing (*applicable to entities taxed as C corporations*)

(a) Applicability of Single Sales Factor Apportionment and Market Based Sourcing. This apportionment Rule applies to the following taxpayers for tax years beginning **on or after** January 1, 2015:

- (1) all C corporations deriving income from sources both within and outside of this state, or engaging in any activities or transactions both within and outside of this state for the purpose of profit or gain;
- (2) all members in a combined group that derives income from sources both within and outside of this state, or engages in any activities or transactions both within and outside of this state for the purpose of profit or gain, when such a combined group includes at least one C corporation member; and
- (3) all combined groups deriving income from sources both within and outside of this state, or engaging in any activities or transactions both within and outside of this state for the purpose of profit or gain, when such a combined group includes at least one C corporation member.

(b) Limited Availability of Special Apportionment Formulas. In limited cases, for tax years beginning **on or after** January 1, 2015, taxpayers may use a special apportionment formula available under RIGL §§ 44-11-14.1 through 44-11-14.6 and Rule 11 of this Regulation. In such situations, eligible entities shall nevertheless apportion income to Rhode Island according to the

provisions of this Rule to the extent that such apportionment is not inconsistent with the formula available under RIGL §§ 44-11-14.1 through 44-11-14.6 and Rule 11 of this Regulation.

(c) **C Corporation's Net Income Attributable to Rhode Island.** To arrive at a determination of the share of net income attributable to Rhode Island for an individual C corporation that is not a member in a combined group, the total reported net income of the C corporation is multiplied by the C corporation's apportionment percentage, referred to elsewhere in this Regulation as the corporation's sales factor. The apportionment percentage is determined as a fraction, the numerator of which is the total Rhode Island sales of the C corporation, determined as set forth in RIGL §44-11-14(b) and Rule 8(i) of this Regulation, and the denominator of which is the total sales everywhere of the C corporation.

(d) **Combined Group's Net Income Attributable to Rhode Island.** To arrive at a determination of a combined group's net income attributable to Rhode Island, the total reported combined group net income is multiplied by the apportionment percentage of the combined group, described elsewhere in this Regulation as the combined group's sales factor. The apportionment percentage is determined as a fraction, the numerator of which is the total Rhode Island sales of the combined group, determined as set forth in RIGL § 44-11-14(b) and Rule 8(i) of this Regulation, and the denominator of which is the total sales everywhere of the combined group.

(e) **Finnigan Method Requirement.** In calculating any sales factor for purposes of combined reporting as required by this Rule, Rhode Island employs the Finnigan Method. Thus a C corporation filing a combined return on behalf of a combined group must include all receipts attributable to Rhode Island for all members in the combined group, without regard to whether a member has corporate income tax nexus with this state. As long as one member in a combined group has corporate income tax nexus with Rhode Island and also engages in activities that exceed the protection of Public Law 86-272, then all members in the combined group, including those protected from state taxation by Public Law 86-272 and those that do not have nexus with Rhode Island, must be included when calculating the combined group's net income and apportionment factors. The Rhode Island receipts of a combined group member that lacks nexus with Rhode Island or that is protected from Rhode Island taxation by Public Law 86-272 must always be included in the numerator of an apportionment fraction on the combined return. For purposes of apportioning a combined group's net income to Rhode Island by means of such an apportionment fraction, the determination of what constitutes a Rhode Island sale or a Rhode Island receipt is governed by Rule 8(i) of this Regulation. The determination of what constitutes a Rhode Island sale or receipt for purposes of the combined group's apportionment calculation is unrelated to and unaffected by Constitutional and other federal limitations on the minimum activities necessary to establish nexus with this State.

(f) **Market-Based Sourcing Requirement.** When receipts from sales, other than sales of tangible personal property, contribute to the sales factor determination of a taxpayer subject to this Rule, the method for calculating receipts from such sales shall rely on the principle of market-based sourcing. Market-based sourcing treats receipts from transactions for other than tangible personal property, including services and intangible property, as sourced to a state if and to the extent that the corporation's market for the sales is in the state. In the case of sales of services, the sale is sourced to the state where the recipient of the service receives the benefit of the service. If the recipient receives less than the full benefit of the service in this State, then

receipts from the associated transaction shall be included in the numerator of the apportionment factor in proportion to the extent that the recipient receives the benefit in this State. In other cases involving sales that are not sales of tangible personal property, the market-based sourcing principle considers a sale or receipt to be within this state for purposes of apportionment as provided in this Rule. The Tax Administrator may promulgate regulations for specific industries. Examples of the market-based sourcing principle are provided in Rule 8(i)(8) of this Regulation.

(g) Sourcing for Sales of Tangible Personal Property. A sale of tangible personal property shall be attributed to the jurisdiction from which the property was shipped only if no member in the combined group has nexus for corporate income tax purposes with the state of destination. In addition, a sale of tangible personal property shipped to this state by a member in the combined group shall be assigned to this state if any member in the combined group has nexus for corporate income tax purposes in this state.

(h) Accuracy in Assigning Sales Factor Receipts and Maintaining Records. A taxpayer's method of assigning its receipts 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 receipts, including its underlying assumptions, and shall provide such records to the Division of Taxation upon request. A taxpayer's method of assigning its receipts, including the use of a method of approximation, where applicable, must reflect an attempt to obtain the most accurate assignment of receipts consistent with the regulatory standards set forth 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 on the applicable facts. In any case in which a taxpayer fails to properly assign receipts from a sale in accordance with the rules set forth in this Regulation, the Division of Taxation may adjust the assignment of such receipts in accordance with the applicable rules in this Regulation. In any case in which the Division of Taxation concludes that a taxpayer's customer's billing address was selected for tax avoidance purposes, the Division of Taxation may adjust the assignment of receipts from sales to such a customer in a manner consistent with the applicable rules in this Regulation. The Division of Taxation reserves the authority to review and adjust a taxpayer's assignment of receipts on a return to more accurately assign such receipts, consistent with the rules or standards in this Regulation.

(i) Activities and Transactions that Constitute Sales or Receipts within the State. Sales or receipts within this state means all gross receipts of the taxpayer in the State of Rhode Island including, but not limited to, receipts derived from the sale of tangible personal property and receipts derived from the sale of other than tangible personal property. Interest income, service charges, carrying charges or time-price differentials incidental to a sale must be included as sales in the state to which the sale is attributable, regardless of the place where the accounting records are located. Sales include federal and state excise taxes, including sales taxes, if those taxes are passed on to the buyer or included as part of the selling price of the product. Sales or receipts within this State include but are not limited to the following:

(1) Sales of tangible personal property in Rhode Island:

(i) Destination Sales. Sales are in Rhode Island if the property is delivered or shipped to a purchaser in Rhode Island regardless of the F.O.B. point or other condition of sale.

Tangible property is deemed to have been shipped or delivered to a purchaser within Rhode Island if:

- (A) The property is delivered directly by the vendor to the possession and control of the purchaser or its representative within Rhode Island unless the vendor can substantiate that no use is made of the property in Rhode Island other than immediate transshipment;
 - (B) The property is delivered to the possession and control of the purchaser by the vendor or by a common carrier outside Rhode Island, if the property is immediately transshipped to Rhode Island;
 - (C) The property is diverted to a purchaser in Rhode Island while en route to a third party consignee in another state. For example, the ABC Corp is a produce grower in state A and begins shipment of produce to customer in state B. While en route the shipment is diverted to Rhode Island where ABC Corp has corporate income tax nexus. This would be classified as a Rhode Island sale; or
 - (D) The third party recipient of the tangible personal property is located in Rhode Island, even if the property is ordered from outside the state. For example, Big Car Dealer, Inc. located in State A sells a red sports car to a Rhode Island customer. However, Big Car Dealer, Inc. doesn't have a red sports car in stock. Big Car Dealer, Inc. contacts another dealership in state A which does have such a model in stock and directs the other dealership to deliver the car directly to the customer in Rhode Island. This would be classified as a Rhode Island sale, assuming Big Car Dealer has corporate income tax nexus in Rhode Island.
- (2) **Throwback sales.** Where tangible personal property is delivered or shipped from Rhode Island to a purchaser outside of Rhode Island and the vendor does not have corporate income tax nexus in that other state, such sale is sourced to Rhode Island.

Example:

123 Inc., a C-corporation, with branches and inventory in Rhode Island, has its head office and factory located in State A. 123 Inc. receives an order from a customer located in State B. 123 Inc. fills the order by shipping merchandise to the customer in State B from stocks of inventory located in Rhode Island. 123 Inc. does not have corporate income tax nexus with State B. Because 123 Inc. has corporate income tax nexus in Rhode Island and not in State B, this sale is attributed to Rhode Island for purposes of apportionment.

- (3) **Sales related to manufacturing and selling, sales related to purchasing and reselling, and sales related to goods or products.** Sales include gross sales, less returns and allowances. Sales also include all service charges, carrying charges, and other non-interest charges incidental to sales.

Examples:

- (A) Taxpayer Corp. has an inventory warehouse in Massachusetts and sells \$100,000 of product to a purchaser with stores in various states, including Rhode Island. The order was placed by the purchaser through its central purchasing department in Delaware. \$25,000 of the order was shipped to the store in Rhode Island. Taxpayer Corp. will include this \$25,000 in the numerator of its sales factor.
- (B) XYZ Inc., a C-corporation with inventory in State A, sold 100,000 units of its product to a customer having branch stores in several states, including Rhode Island. The order was placed by the customer's central purchasing department in State B, and 25,000 units of the product were shipped by XYZ, Inc. directly to the customer's branch store in Rhode Island. Since XYZ, Inc. shipped 25,000 units of product to a customer's location in Rhode Island, that sale is sourced to Rhode Island for purposes of XYZ, Inc.'s apportionment factor.

(4) **Cost-plus contracts.** Sales include entire reimbursed cost plus the fee.

(5) **Lease or rental of real or tangible personal property located in Rhode Island.** Sales include the gross receipts from renting, leasing, or licensing the use of real or tangible personal property within the state, except in cases in which the lease, rental, or license of the asset is treated as the sale or other disposition of a capital asset used in a seller's trade or business, in which case sales include only the gain from the disposition of the property. Sales are attributable to Rhode Island if and to the extent that the property is located in Rhode Island.

(6) **Capitalized leases.** Property located in Rhode Island subject to a capitalized lease for federal income tax purposes is treated as a capitalized lease for Rhode Island tax purposes. Any income or gain realized from a capitalized lease transaction is includable for Rhode Island purposes to the extent that the income or gain from such transaction is included in the federal gross income of the seller.

(7) **Sale, exchange, or other disposition of fixed assets located in Rhode Island.** In the case of the sale, exchange or other disposition of a fixed asset used in a seller's trade or business, such as property, plant or equipment, sales are measured by the gain from such transaction. Gain from the disposition of a fixed asset shall include, but is not limited to, the deemed gain from a transaction that is treated as a sale of a seller's assets and that results in recognition of income.

(8) **Sales other than sales of tangible personal property.** Receipts from sales, other than sales of tangible personal property, are in Rhode Island within the meaning of this regulation if and to the extent that the seller's market for the sales is in Rhode Island. For purposes of this Rule 8(i)(8), sales other than sales of tangible personal property are classified broadly into four categories: (i) Sale of a Service; (ii) License or Lease of Intangible Property; (iii) Sale of Intangible Property; and (iv) Special Rules. To facilitate determinations of what activities and transactions constitute a sale or receipt within Rhode Island, the four broad categories of sales other than sales of tangible personal property are further broken down into subcategories, as set forth below in this Rule 8(i)(8).

(A) **General Principle of Application; Rules of Reasonable Approximation.** The various sales assignment rules set forth in Rules 8(i)(8)(B) through 8(i)(8)(E) are

intended to 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. The provisions that set forth rules of reasonable approximation apply where the state or states of assignment cannot be determined. In some instances, a reasonable approximation must be made in accordance with specific rules of approximation prescribed by this Regulation. 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.

(B) Sale of a Service. Rhode Island sales of services are determined according to the principle of market-based sourcing and include gross receipts from the performance of services including commissions, fees, management charges, and similar items. The receipts from a sale of a service are in Rhode Island if and to the extent that the recipient of the service receives the benefit of the service in Rhode Island. The rules to determine the location where the recipient receives the benefit of the service in the context of several specific types of service transactions are set forth below in Rules 8(i)(8)(B)(i) through 8(i)(8)(B)(iii). In any instance where, applying the applicable rules set forth below in this Rule 8(i)(8)(B) pertaining to sales of services, a taxpayer can ascertain the state or states of assignment of a substantial portion of its receipts from sales of substantially similar services (“assigned receipts”), 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 receipts, it shall include receipts from those sales which it believes tracks the geographic distribution of the assigned receipts in its sales factor in the same proportion as its assigned receipts. 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.

(i) In-Person Services. Except as otherwise provided in this Rule, in-person services are services that are physically provided in person by the service provider, 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 service provider 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 Rule 8(i)(8)(B)(iii), although they may involve some amount of in-person contact, are not treated as in-person services within the meaning of this Rule.

(a) **Assignment of Receipts.** Except as otherwise provided in this Rule, where the service provided by the service provider is an in-person service, the benefit of the service is received at the location where the service is received. Therefore, the receipts from a sale are in Rhode Island if and to the extent the customer receives the in-person service in Rhode Island. In assigning its receipts from sales of in-person services, a taxpayer shall first attempt to determine the location where a service is received, as follows:

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

II. Where the service is performed with respect to the customer's real estate in Rhode Island 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 Rhode Island, the benefit of the service is received in Rhode Island.

III. 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 Rhode Island or outside Rhode Island, the benefit of the service is received in Rhode Island if such property is shipped or delivered to the customer in Rhode Island.

In any instance in which the state or states where the benefit of a service is actually received cannot be determined, but the taxpayer has sufficient information from which it can reasonably approximate the state or states where the benefit of the service is received, the taxpayer shall reasonably approximate such state or states.

(b) **Examples.**

Example 1. Salon Corp has retail locations in Rhode Island 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 receipts from sales of services provided at Salon Corp's in-state locations are in Rhode Island. The receipts from sales of services provided at Salon Corp's

locations outside Rhode Island, even when provided to state residents, are not receipts from in-state sales.

Example 2. Landscape Corp provides landscaping and gardening services in Rhode Island 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 Rhode Island at the time the services are performed. The receipts from sale of services provided at the in-state location are in Rhode Island.

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 Rhode Island and in other states. The receipts from the sale of services provided to Retail Corp are in Rhode Island to the extent the services are provided in Rhode Island.

For additional examples demonstrating the assignment of receipts for in-person services under this section, please see the corresponding section of the Appendix (Rule 15) to this Regulation.

(ii) Services Delivered to the Customer or on Behalf of the Customer, or Delivered Electronically through the Customer. Where the service provided by the service provider is not an in-person service within the meaning of Rule 8(i)(8)(B)(i) or a professional service within the meaning of Rule 8(i)(8)(B)(iii), and the service is delivered to or on behalf of the customer, or delivered electronically through the customer, the benefit of the service is received in Rhode Island if and to the extent that the service is delivered in Rhode Island. For purposes of this Rule, 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, or the direct or indirect delivery of advertising to the customer’s intended audience. 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.

(a) Assignment of Receipts. The assignment of receipts from 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 Rule 8(i)(8)(B)(ii), 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 Rule, 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.

I. 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 apply whether the taxpayer's customer is an individual customer or a business customer.

A. Rule of Determination. In assigning the receipts of a 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 receipts to such state or states.

B. 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.

C. Examples.

Example 1. Direct Mail Corp, a corporation based outside Rhode Island, 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 Rhode Island 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 receipts from the sale of Direct Mail Corp's services to Business Corp are assigned to Rhode Island to the extent that the services are delivered on behalf of Business Corp to Rhode Island customers

(i.e., to the extent that the fliers are delivered on behalf of Business Corp to Business Corp's intended audience in Rhode Island).

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

Example 3. Same facts as example 2, except that the contract is with a business customer that is based outside Rhode Island. The receipts from the sale of the design services are in Rhode Island because the services are physically delivered on behalf of the customer to the customer's intended audience in Rhode Island.

For additional examples demonstrating the assignment under this section of receipts for services delivered to or on behalf of a customer by physical means, whether to an individual or business customer, please see the corresponding section of the Appendix (Rule 15) to this Regulation.

II. 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.

A. Services Delivered by Electronic Transmission to an Individual Customer.

(i) **Rule of Determination.** In the case of the delivery of a service to an individual customer by electronic transmission, the service is delivered in Rhode Island if and to the extent that the service provider's customer receives the service in Rhode Island. If the taxpayer can determine

the state or states where the service is received, it shall assign the receipts from that sale to such state or states.

(ii) **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 benefit of 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 benefit of the service is received, it shall reasonably approximate such state or states using the customer's billing address.

B. Services Delivered by Electronic Transmission to a Business Customer.

(i) **Rule of Determination.** In the case of the delivery of a service to a business customer by electronic transmission, the service is delivered in Rhode Island if and to the extent that the service provider's customer receives the service in Rhode Island. If the taxpayer can determine the state or states where the service is received, it shall assign the receipts from that sale to such state or states. For purposes of this Rule, 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.

(ii) **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 benefit of the service is received, it shall reasonably approximate such state or states.

(iii) **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 reasonably approximate the state or states in which the benefit of 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 immediately below in subsection (iv), the taxpayer shall reasonably approximate the state or states in which

the benefit of the service is received as follows: first, by assigning the receipts from 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 receipts from 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 receipts from the sale using the customer's billing address; provided, however, that in any instance in which the taxpayer derives more than 5% of its receipts from 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.

(iv) **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 the preceding subsection (ii), the state or states in which the benefit of the service is received. In these cases, the taxpayer may, in lieu of the rule stated in the immediately preceding subsection (iii), apply the safe harbor stated in this Rule. Under this safe harbor, a taxpayer may assign receipts from sales to a particular customer based upon the customer's billing address in any taxable year in which the service provider (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 receipts from sales of services from such customer. This safe harbor applies only to services delivered by electronic transmission to a business customer, and not otherwise.

C. Examples.

Example 1. Support Corp, a corporation that is based outside Rhode Island, 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 Rhode Island 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 receipts to these locations. The receipts from sales made to Support Corp's individual and business customers are in Rhode Island to the extent that Support Corp's services are received in Rhode Island.

Example 2. Online Corp, a corporation based outside Rhode Island, provides web-based services through the means of the Internet to individual customers who are resident in Rhode Island 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 receipts from the sale of services, Online Corp can either 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 receipts from 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 Rhode Island the receipts from sales for which it does not know the customers' location in the same proportion as those receipts for which it has this information.

Example 3. Same facts as in Example 2, except that Online Corp reasonably believes that the geographic distribution of the receipts from 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 receipts from sales of its services for which it lacks information as provided to its individual customers using the customers' billing addresses.

For additional examples demonstrating the assignment under this section of receipts for services delivered to a customer by electronic transmission, please see the corresponding section of the Appendix (Rule 15) to this Regulation.

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

A. 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 benefit of the service is received in Rhode Island if and to the extent that the end users or other third-party recipients are in Rhode Island. 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 benefit of the service is received in Rhode Island to the extent that the audience for such advertising is in Rhode Island. 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 benefit of the service is received in Rhode Island to the extent that the end users or other third-party recipients receive such services in Rhode Island. The rules in this subsection apply whether the service provider’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.

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

C. Select Secondary Rules of Reasonable Approximation

(i) Where a service provider’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 service provider 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 in such area. For a taxpayer with less information about the service provider's 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 service provider's service is the delivery of a service to a customer that then acts as the service provider'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 service provider's intermediary resells such services, relative to the total population in such area.

(iii) Where a service provider's service is the delivery of a service other than advertising to a party that then acts as the service provider'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 service provider's intermediary resells such services, relative to the total population in such area.

(iv) When using the secondary reasonable approximation methods provided above, the relevant specific geographic area of service reception shall only include the areas where the service was substantially and materially delivered or resold. Unless the taxpayer demonstrates the contrary, it will be presumed that the area where the service was substantially and materially delivered or resold does not include areas outside the United States.

D. Examples.

Example 1. Cable TV Corp, a corporation that is based outside of Rhode Island, 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 Rhode Island. Second, Cable TV Corp sells monthly subscriptions to individual customers in Rhode Island and in other states. The receipts from Cable TV Corp's sale of advertising time to its business customers are assigned to Rhode Island to the extent that the audience for Cable TV Corp's televised programming during which the advertisements run is in Rhode Island. 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 Rhode Island audience using the percentage that reflects the ratio of its Rhode Island 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. To the extent that Cable TV Corp's sales of monthly subscriptions represent the sale of a service, the receipts from such sales are properly assigned to Rhode Island in any case in which the programming is received by a customer in Rhode Island. 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, the receipts from such sales of Cable TV Corp's monthly subscriptions are assigned to Rhode Island where its customer's billing address is in Rhode Island. 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 receipts are properly assigned.

Example 2. Network Corp, a corporation that is based outside of Rhode Island, 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. The receipts from Network Corp's sale of advertising time to its business customers are assigned to Rhode Island to the extent that the audience for Network Corp's televised programming during which the advertisements will run is in Rhode Island. 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 receipts from sales of advertising that constitute Rhode Island sales by multiplying the amount of advertising receipts by a percentage that reflects the ratio of the Rhode Island population in the specific geographic area in which the televised programming containing the advertising is run relative to the total population in such area.

For additional examples demonstrating the assignment under this section of receipts for services delivered electronically through or on behalf of an individual or business customer, please see the corresponding section of the Appendix (Rule 15) to this Regulation.

(iii) **Professional Services.** Except as otherwise provided in Rule 8(i)(8)(B)(iii)(a), 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.

(a) **Overlap with Other Categories of Services.** Certain services that fall within the definition of “professional services” set forth in Rule 8(i)(8)(B)(iii) are nevertheless treated as “in-person services” within the meaning of Rule 8(i)(8)(B)(i), and are assigned under the rules of that subsection. Specifically, professional services that are physically provided in person by the service provider 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 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 as set forth in Rule 8(i)(8)(B)(iii)(b), notwithstanding the fact that such services may involve some amount of in-person contact. 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 the transmission, the assignment rules that apply are those set forth in Rule 8(i)(8)(B)(iii), and not those set forth in Rule 8(i)(8)(B)(ii), pertaining to services delivered to a customer or through or on behalf of a customer.

(b) **Assignment of Receipts.** In the case of a professional service, it is generally possible to characterize the location where the benefit of the service is received 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-based sourcing principle, the Division of Taxation has concluded that the location where the benefit of the service is received in the case of professional services is not susceptible to a general rule of determination, and must be reasonably approximated. The assignment of receipts from 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 receipts from a sale of a professional service, a service provider's customer is the person who contracts for such service, irrespective of whether another person pays for or also benefits from the service provider's services.

I. General Rule. Unless provided otherwise by the Rhode Island General Laws or by this Regulation, receipts from sales of professional services shall be assigned in accordance with this Rule 8(i)(8)(B)(iii)(I), as follows:

A. Professional Services Delivered to Individual Customers.

Except as otherwise provided in this Rule 8(i)(8)(B)(iii), in any instance in which the service provided is a professional service and the service provider's customer is an individual customer, the state or states in which the benefit of the service is received shall be reasonably approximated as set forth in this Rule 8(i)(8)(B)(iii)(I)(A). In particular, the taxpayer shall assign the receipts from a 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, that in any instance in which the service provider derives more than 5% of its receipts from 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.

B. Professional Services Delivered to Business Customers.

Except as otherwise provided in this Rule 8(i)(8)(B)(iii), in any instance in which the service is a professional service and the service provider's customer is a business customer, the state or states in which the benefit of the service is received shall be reasonably approximated as set forth in this Rule 8(i)(8)(B)(iii)(I)(B). In particular, unless the taxpayer may use the safe harbor set forth at Rule 8(i)(8)(B)(iii)(I)(C), the taxpayer shall assign the receipts from 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 service provider derives more than 5% of its receipts from 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.

C. Safe Harbor; Large Volume of Transactions.

Notwithstanding the rules set forth in subsections 8(i)(8)(B)(iii)(I)(A) and 8(i)(8)(B)(iii)(I)(B), a taxpayer may assign receipts from sales to a particular customer based on the customer's billing address in any taxable year in which the service provider (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 receipts from sales of services from such customer. This safe harbor applies only for purposes of Rule 8(i)(8)(B)(iii)(I), and not otherwise.

II. 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 Rule 8(i)(8)(B)(iii). However, unlike in the case of the general rule that applies to professional services, (1) the receipts from a sale of such an architectural service are 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 receipts from a sale of such an engineering service are 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 Rule 8(i)(8)(B)(iii)(II), the receipts from a sale of such services shall be assigned under the general rule for professional services.

III. Legal Services. Legal services are professional services within the meaning of this section. As an exception to the general rules for assignment of such receipts, however, receipts for the sale of professional services involving the initiation, defense or maintenance of a judicial or administrative proceeding within this state shall be assigned to this state.

IV. Examples.

Example 1. Architecture Corp provides building design services as to buildings located, or expected to be located, in Rhode Island to individual customers who are resident in Rhode Island and other states,

and to business customers that are based in Rhode Island and other states. The receipts from Architecture Corp's sales are assigned to Rhode Island because the locations of the buildings to which its design services relate are in Rhode Island, or are expected to be in Rhode Island. For purposes of assigning these receipts, 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 receipts are assigned to Rhode Island even if Architecture Corp's designs are either physically delivered to its customer in paper form in a state other than Rhode Island or are electronically delivered to its customer in a state other than Rhode Island.

Example 2. Law Corp provides legal services to individual clients who are resident in Rhode Island 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 receipts from sales of services from any one individual client. Where Law Corp knows its client's state of primary residence, it shall assign the receipts 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 receipts 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.

Example 3. 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 Rhode Island; in the other cases, the agreement is principally managed in a state other than Rhode Island. Where the agreement for legal services is principally managed by the client in Rhode Island, the receipts from sale of the services shall be assigned to Rhode Island; in the other cases, the receipts are not assigned to Rhode Island. In the case of receipts that are assigned to Rhode Island, the receipts 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.

For additional examples demonstrating the assignment under this section of receipts for professional services, please see the corresponding section of the Appendix (Rule 15) to this Regulation.

(C) License or Lease of Intangible Property. The gross receipts from the license of intangible property are in Rhode Island if and to the extent the intangible property is used in Rhode Island. 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 below in Rules 8(i)(8)(C)(i) through 8(i)(8)(C)(iv). For purposes of the rules set forth in this subsection 8(i)(8)(C), a lease of intangible property is to be treated the same as a license of intangible property. In general, a license of intangible property that conveys all substantial rights in such property is treated as a sale of intangible property for purposes of this Regulation. Note, however, that for purposes of Rules 8(i)(8)(C) and 8(i)(8)(D), 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. 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. To the extent that the transfer of a security 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.

(i) 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 Rhode Island 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 consumers or other ultimate customers in Rhode Island. 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 Rhode Island, it shall assign such amount or proportion to Rhode Island. In the absence of actual evidence of the amount or proportion of the licensee's receipts that are derived from Rhode Island customers, the portion of the licensing fee to be assigned to Rhode Island shall be reasonably approximated by multiplying the total fee by a percentage that reflects the ratio of the Rhode Island 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 Rhode Island shall be reasonably approximated by multiplying the total fee by a percentage that reflects the ratio of the

Rhode Island population in the specific geographic area in which the licensee's goods, services, or other items are ultimately and materially marketed using the intangible property relative to the total population of such area. In the case of sales made to a jurisdiction outside the United States, it will be presumed that the licensing is not material unless the taxpayer shows otherwise.

(ii) **License of a Production Intangible.** A license 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 to be used in a production capacity is a “production intangible.” 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. The licensing fees paid by the licensee for such right are assigned to Rhode Island to the extent that the use for which the fees are paid takes place in Rhode Island. Where the Division of Taxation can reasonably establish that the actual use of intangible property pursuant to a license of a production intangible takes place in part in Rhode Island, 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 Rhode Island. In the case of a license of a production intangible where the actual use is unknown, 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).

(iii) **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 Division of Taxation will accept such separate statement for purposes of this Regulation. 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 Division of Taxation can reasonably establish otherwise.

(iv) **License of Intangible Property where Substance of Transaction Resembles a Sale of Goods or Services.** 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 Rules 8(i)(8)(B)(ii)(a)(II) and 8(i)(8)(B)(ii)(a)(III), 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 Rule 8(i)(8)(C)(iv) include, without limitation, the license of database access, the license of access to information, the license of digital goods, 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).

(a) **Sublicenses.** Pursuant to Rule 8(i)(8)(C)(iv), the rules of subsection 8(i)(8)(B)(ii)(a)(III) may apply where a holder of intangible property 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 subsection 8(i)(8)(B)(ii)(a)(III) 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 these 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 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.

(v) **Examples.**

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 Rhode Island. 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 Rhode Island shall be determined by multiplying the fees by a percentage that reflects the ratio of Dealer Co's receipts that are derived from its Rhode Island stores relative to Dealer Co's total receipts.

Example 2. Program Corp, a corporation that is based outside Rhode Island, 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 Rhode Island 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 Rhode Island, the component of the licensing fee paid to Program Corp by the licensee that constitutes Program Corp's Rhode Island receipts is determined by multiplying the amount of the licensing fee by a percentage that reflects the ratio of the Rhode Island audience of the licensee for

the programming relative to the licensee's total U.S. audience for the programming. Note that the analysis and result as to the state or states to which receipts 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.

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 Rhode Island receipts of Moniker Corp is determined by multiplying the amount of the fee by a percentage that reflects the ratio of the Rhode Island population in the specific geographic region relative to the total population in such region.

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 Rhode Island 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 Division of Taxation can reasonably establish that the actual use of the intangible property takes place in part in Rhode Island, the royalty is assigned based to the location of such use rather than to location of the licensee's commercial domicile. It is presumed that the entire use is in Rhode Island except to the extent that the taxpayer can demonstrate that the actual location of some or all of the use takes place outside Rhode Island. Assuming that Formula, Inc can demonstrate the percentage of manufacturing that takes place in Rhode Island 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 Rhode Island receipts.

For additional examples demonstrating the assignment under this section of receipts for the license or lease of intangible property, please see the corresponding section of the Appendix (Rule 15) to this Regulation.

(D) Sale of Intangible Property. The assignment of gross receipts from 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 Rule 8(i)(8)(D), 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 the 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 Rule 8(i)(8)(C).

(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 receipts from the sale are assigned to a state if and to the extent that the intangible property is used or is authorized to be used within the state. Where the intangible property is used or may be used only in Rhode Island the taxpayer shall assign the receipts from the sale to Rhode Island. Where the intangible property is used or is authorized to be used in Rhode Island and one or more other states, the taxpayer shall assign the receipts from the sale to Rhode Island to the extent that the intangible property is used in or authorized for use in Rhode Island, through the means of a reasonable approximation.

(ii) 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 Rule 8(i)(8)(C) (pertaining to the license or lease of intangible property).

(iii) 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 Rule 8(i)(8)(C)(iv) (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 Rule 8(i)(8)(C)(iv).

(iv) Examples.

Example 1. Sports League Corp, a corporation that is based outside Rhode Island, 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 Rhode Island. 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

may be used in Rhode Island. 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 Rhode Island and the other states.

Example 2. Business Corp, a corporation based outside Rhode Island engaged in business activities in Rhode Island and other states, enters into a covenant not to compete with Competition Corp, a corporation that is based outside Rhode Island, in exchange for a fee. The agreement requires Business Corp to refrain from engaging in certain business activity in Rhode Island and other states. The component of the fee that constitutes receipts from a sale in Rhode Island is determined by multiplying the amount of the fee by a fraction represented by the percentage of the Rhode Island population over the total population in the specified geographic region.

(E) Special Rules.

(i) **Software Transactions.** 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 gross receipts are in Rhode Island as determined under the rules for the sale of tangible personal property. In all other cases, the receipts from a license or sale of software are to be assigned to Rhode Island as determined otherwise under this regulation (e.g., depending on the facts, as the development and sale of custom software, see Rule 8(i)(8)(B)(ii), as a license of a marketing intangible, see Rule 8(i)(8)(C)(i), as a license of a production intangible, see Rule 8(i)(8)(C)(ii), as a license of intangible property where the substance of the transaction resembles a sale of goods or services, see Rule 8(i)(8)(C)(iv), or as a sale of intangible property, see Rule 8(i)(8)(D)).

(ii) **Sales or Licenses of Digital Goods or Services.** 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 gross receipts from the sale or license shall be assigned by applying the same rules as are set forth in Rules 8(i)(8)(B)(ii)(a)(II) or 8(i)(8)(B)(ii)(a)(III), 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.

(9) **Dividends.** Sales include dividends, such as dividends received from shares of stock of any payee liable for taxes as outlined in Chapters 44-11, 44-13 and 44-14, and dividends excluded for federal tax purposes, less exclusion for Rhode Island purposes.

(10) **Interest.** Sales include interest, such as interest on certain obligations of the United States and its possessions or interests on obligations of Rhode Island Public Service Corporations, less exclusions for Rhode Island purposes.

(i) Exclusion of Receipts from Sales Factor. Gross receipts do not include, for example, such items as:

- (1) Transactions solely between affiliates that are members in the same combined group;
- (2) Repayment, maturity, or redemption of the principal of a loan, bond, or mutual fund or certificate of deposit or similar marketable instrument;
- (3) The principal amount received under a repurchase agreement or other transaction properly characterized as a loan;
- (4) Proceeds from issuance of the taxpayer's own stock or from the sale of treasury stock;
- (5) Damages and other amounts received as the result of litigation;
- (6) Property acquired by an agent on behalf of another;
- (7) Tax refunds and other benefit recoveries, unless such refunds or benefit recoveries are claimed as deductions;
- (8) Pension reversions;
- (9) Contributions to capital other than sales of securities by securities dealers;
- (10) Income from forgiveness of indebtedness; or
- (11) Amounts realized from exchanges of inventory that are not recognized by the Internal Revenue Code.

Rule 9. Three-Factor Apportionment Using Sales, Property and Payroll

(a) **Applicability of Three-Factor Apportionment.** This apportionment Rule applies to the following taxpayers, unless the taxpayer is eligible to use a special apportionment formula available under RIGL §§ 44-11-14.1 through 44-11-14.6 and Rule 10 or 11 of this Regulation:

(1) **2015 and Thereafter.** For tax years beginning **on or after** January 1, 2015, any taxpayer that derives income from sources both within and outside of this state or engages in any activities or transactions both within and outside of this state for the purpose of profit or gain, **but which is not:**

- (i) a C corporation,
- (ii) a combined group with a C corporation member, or
- (iii) a member in a combined group with a C corporation member.

(2) **Pre-2015.** For tax years beginning **before** January 1, 2015, all taxpayers that derive their income from sources both within and outside of this state for the purpose of profit or gain.

(i) **Note:** With respect to the corporate income tax responsibilities of C corporations for tax years beginning **on or after** January 1, 2015, such taxpayers must refer to and comply with Rule 8 of this Regulation.

(b) **Three-Factor Apportionment – Formula.** For all taxpayers to whom this Rule applies, income shall be apportioned to this state by means of an apportionment formula to be computed as a simple arithmetical mean of three (3) fractions, as follows:

(1) **Property.** The first fraction shall represent that part held or owned within this state of the average net book value of the total tangible property (real estate and tangible personal property) held or owned by the taxpayer during the taxable year, without deduction on account of any encumbrance thereon. Included in this property factor are the following:

- (i) Inventory,
- (ii) Depreciable Assets,
- (iii) Leasehold improvements,
- (iv) Land,
- (v) Construction in progress to the extent shown as a capital asset on the books of the corporation, and
- (vi) Rental property (capitalized times 8).

(2) **Sales.** The second fraction shall represent that part of the taxpayer's total receipts from sales or other sources during the taxable year which is attributable to the taxpayer's activities or transactions within this state during the taxable year. Under the three-factor apportionment formula applicable in this rule, taxpayers determining sales attributable to Rhode Island for transactions other than sales of tangible personal property shall adhere to cost of performance sourcing principles, and not the market-based sourcing principles that apply in the context of single sales factor apportionment. Under cost of performance sourcing principles, gross receipts from transactions other than sales of tangible personal property are attributed to this state if the income-producing activity which gave rise to the receipts is performed wholly within this state. Also, gross receipts are attributed to this state if, with respect to a particular item of income, the income-producing activity is performed within and without this state but the greater portion of the income-producing activity is performed within this state, based on costs of performance. In all cases where a three-factor apportionment formula applies, the sales fraction shall continue to be determined in the same manner that applied in Rhode Island prior to the introduction of mandatory unitary combined reporting. Taxpayers' receipts from sales include, but are not limited to, receipts from the following:

- (i) Gross sales of tangible personal property (inventory sold in the ordinary course of business) where:
 - (A) Shipments are made to points within this state; or

(B) Shipments are made from an office, store, warehouse, factory or other place of storage in this state and the selling entity does not have corporate income tax nexus in the state of delivery.

- (ii) Gross income from services performed within this state;
- (iii) Gross income from rentals from property situated within this state;
- (iv) Net income from the sale of real and personal property, other than inventory sold in the ordinary course of business as described in paragraph (1) of this subdivision, or other capital assets located in the state;
- (v) Net income from the sale or other disposition of securities or financial obligations;
- (vi) Gross income from all other receipts within this state;
- (vii) Dividends less exclusions for Rhode Island purposes, such as dividends received from shares of stock of any payee liable for taxes as outlined in Chapters 44-11, 44-13 and 44-14 of Rhode Island General Laws and dividends excluded for federal tax purposes;
- (viii) Interest less exclusion for Rhode Island purposes, such as interest on certain obligations of the United States and its possessions or interest on obligations of Rhode Island Public Service Corporations;
- (ix) Rent
- (x) Royalties;
- (xi) Net Capital Gain as reported for federal tax purposes;
- (xii) Net Ordinary Gain as reported for federal tax purposes;
- (xiii) Other Income; and
- (xiv) Income exempt from federal taxation but taxable for Rhode Island purposes, such as income from obligations from other states.

(3) **Payroll.** The third fraction shall represent that part of the total wages, salaries, and other compensation to officers, employees, and agents paid or incurred by the taxpayer during the taxable year which is attributable to services performed in connection with the taxpayer's activities or transactions within this state during the taxable year.

Rule 10. Special Apportionment Formulas – Pre-2015

(a) **Applicability of Special Apportionment Formulas – Pre-2015.** For tax years beginning **before** January 1, 2015, special apportionment rules, as set forth in subsections (b) through (j) of this Rule, shall apply to the categories of taxpayers listed below when such taxpayers derive their income from sources both within and outside of this state for the purpose of profit or gain:

- (1) Manufacturers;
- (2) Motor carriers;
- (3) Airlines;
- (4) Taxpayers with specialty receipts;
- (5) Taxpayers with qualified USFDA manufacturing facilities in Rhode Island;
- (6) Regulated investment companies and securities brokerage services;
- (7) Credit card banks;
- (8) Retirement and pension plans;
- (9) Sellers of international investment management services.

In all such cases, apportionment fractions shall be determined in the same manner that applied in Rhode Island prior to the introduction of mandatory unitary combined reporting. **For tax years beginning on or after January 1, 2015, refer to Rule 11 of this Regulation.**

(b) Manufacturers (tax years beginning before January 1, 2015).

(1) Manufacturers who maintain a principal business as described in Sector 31, 32 or 33 of the North American Industry Classification System as adopted by the United States Office of Management and Budget as revised from time to time, may, in lieu of apportioning net income to this state based on the apportionment fraction described in RIGL § 44-11-14(a), elect for any year to apportion net income to this state based upon the following apportionment fraction:

- (i) For the tax year beginning on or after January 1, 2004, but before January 1, 2005, thirty percent (30%) of the property factor, thirty percent (30%) of the payroll factor and forty percent (40%) of the receipts factor may be used;
- (ii) For the tax year beginning on or after January 1, 2005, twenty-five percent (25%) of the property factor, twenty-five percent (25%) of the payroll factor and fifty percent (50%) of the receipts factor may be used.

(c) Motor carriers (tax years beginning before January 1, 2015).

(1) In the case of motor carriers, the following method is used to determine the numerator of each factor:

(i) Property Factor:

(A) Consists of the average net book value of situs assets plus a portion of the net book value of the line-haul vehicles. In determining the net book value of line-haul vehicles, compare Rhode Island pickup and delivery equipment to pickup and delivery equipment everywhere to arrive at a percentage due to Rhode Island for line-haul equipment.

(B) For a motor carrier who does not have a Rhode Island facility, but who regularly picks up and delivers in Rhode Island, delivery equipment will be apportioned to Rhode Island based upon its Rhode Island activities.

(C) Rental property shall be valued at eight times the annual net rental paid less annual sub-rentals received.

(ii) **Receipts Factor:** Average of the inbound/outbound Rhode Island receipts plus all other receipts attributable to Rhode Island.

(iii) **Salaries and Wages Factor:**

(A) Consists of the situs wages plus a portion of the line-haul wages. Rhode Island line-haul wages are determined by the percentage of activity in Rhode Island.

(B) For a motor carrier who does not have a Rhode Island facility, but who regularly picks up and delivers in Rhode Island, drivers' wages will be apportioned to Rhode Island based upon its Rhode Island activities.

(d) **Airlines (tax years beginning before January 1, 2015).**

(1) In the case of airlines, the following method is used to determine the numerator of each factor:

(i) **Property Factor:**

(A) Situs assets shall be included based on the average net book value. Flight aircraft shall be included based on the following ratio: mileage of aircraft, by type, flown in this state compared to total aircraft mileage flown everywhere, multiplied by the net book value of flight aircraft everywhere.

(B) Rental property shall be valued at eight times the annual net rental paid less annual sub rentals received.

(ii) **Receipts Factor:**

(A) Passenger revenue and freight revenue shall be allocated to Rhode Island based on the ratio of departures of flight aircraft, by type, from locations in this state compared to total departures everywhere, multiplied by total passenger revenue everywhere

(B) All other receipts attributable to Rhode Island shall also be included in the numerator.

(iii) **Salaries and Wages Factor:**

(A) Situs wages shall be included plus a portion of flight payroll. Flight payroll shall be included based on the following ratio: mileage of aircraft, by type, flown in this state compared to total aircraft mileage flown everywhere, multiplied by the total flight payroll everywhere.

(e) Taxpayers with specialty receipts (tax years beginning before January 1, 2015).

(1) For those taxpayers whose Rhode Island receipts include sums from the exercise of various legal rights such as patents, copyrights, royalties, franchises, licenses, etc. which are used, broadcast, or copied (in any media), such receipts shall be included in the numerator of the gross receipts factor and the total of such receipts shall be included in the denominator. A patent is used in Rhode Island to the extent that it is employed in fabrication, manufacturing, production or other processing in Rhode Island or to the extent that a patented product is produced in Rhode Island.

(2) A copyright is used in Rhode Island to the extent that printing or other publication originated therein.

(3) Broadcast media is used in Rhode Island to the extent that the Rhode Island target audience is determinable as a part of the total audience. If the Rhode Island audience is not determinable, then the entire receipts from the Rhode Island source are includible in the numerator of the gross receipts.

(4) In all cases, 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 tax administrator upon request.

(f) Taxpayers with qualified USFDA manufacturing facilities in Rhode Island (tax years beginning before January 1, 2015).

(1) A taxpayer with a Rhode Island facility which is both certified and registered by the United States Food and Drug Administration (USFDA) and is considered manufacturing as defined by the US Standard Industrial Classification Code(s)(SIC Code) 283, and 384 shall follow the three-factor apportionment formula as described in Rule 9 of this Regulation, except that the taxpayer may exclude certain values from the apportionment fraction, as follows:

- (i) From the numerator of the property fraction, the taxpayer may exclude the amount, if any, by which the net book value of qualified property in the tax year for which an exclusion is claimed under this provision exceeds the net book value of qualified property in the preceding tax year. For the purposes of this provision, "qualified property" means real estate and tangible personal property used solely and exclusively in all of the taxpayer's certified Rhode Island facilities.

- (ii) From the numerator of the wages/payroll fraction, the taxpayer may exclude the amount, if any, by which total qualified payroll expenses of the taxpayer in the tax year for which an exclusion is claimed under this provision exceeds the total qualified payroll expenses of the taxpayer in the immediately preceding tax year. For purposes of this provision, "qualified payroll" means the total amount of salaries, wages and other compensation paid to employees and to officers, except officers who have a direct or indirect ownership interest in the taxpayer in excess of five percent (5%) or who are substantial creditors of the taxpayer, which is attributable solely and exclusively to services performed in connection with the taxpayer's activities or transactions at all of the taxpayer's certified Rhode Island facilities.
- (iii) In the event that a facility is certified during the taxpayer's tax year or in the event that a facility ceases to be certified during the taxpayer's tax year, the taxpayer shall prorate the amounts determined under subsections (f)(1)(i) and (f)(1)(ii) of this Rule.
- (iv) The taxpayer shall attach to the return for each tax year for which an exclusion is claimed under this provision detailed calculations substantiating each exclusion and proof that the taxpayer has satisfied the conditions relating to registration and certification by USFDA contained in this section.

(g) Regulated investment companies and securities brokerage services (tax years beginning before January 1, 2015).

- (1) Any taxpayer located within the state which sells management, distribution or administration services (including without limitations, transfer agent, fund accounting, custody and other similar or related services) as described in this provision to or on behalf of a regulated investment company (as defined in the Internal Revenue Code of 1986, as amended) may elect the allocation and apportionment method for the taxpayer's net income provided for in this provision. The election, if made, shall be irrevocable for successive periods of five (5) years. All net income derived directly or indirectly from the sale of management, distribution, or administration services to or on behalf of regulated investment companies, including net income received directly or indirectly from trustees, and sponsors or participants of employee benefit plans which have accounts in a regulated investment company, shall be apportioned to Rhode Island only to the extent that shareholders of the regulated investment company are domiciled in Rhode Island as follows:
 - (i) Net income shall be multiplied by a fraction, the numerator of which shall be Rhode Island receipts from the services during the taxable year and the denominator of which shall be the total receipts everywhere from the services for the same taxable year.

- (ii) For purposes of this provision, Rhode Island receipts shall be determined by multiplying total receipts for the taxable year from each separate regulated investment company for which the services are performed by a fraction. The numerator of the fraction shall be the average of the number of shares owned by the regulated investment company's shareholders domiciled in this state at the beginning of and at the end of the regulated investment company's taxable year, and the denominator of the fraction shall be the average of the number of the shares owned by the regulated investment company shareholders everywhere at the beginning of and at the end of the regulated investment company's taxable year.
- (2) Any taxpayer which provides securities brokerage services and which operates within the state may elect the allocation and apportionment method for the taxpayer's net income provided for in this provision. The election, if made, shall be irrevocable for successive periods of five (5) years. All net income derived directly or indirectly from the sale of securities brokerage services by a taxpayer shall be apportioned to Rhode Island only to the extent that securities brokerage customers of the taxpayer are domiciled in Rhode Island. The portion of net income apportioned to Rhode Island shall be determined by multiplying the total net income from the sale of the services by a fraction determined in the following manner:
- (i) The numerator of the fraction shall be the brokerage commissions and total margin interest paid in respect of brokerage accounts owned by customers domiciled in Rhode Island for the taxpayer's taxable year; and
 - (ii) The denominator of the fraction shall be the brokerage commissions and total margin interest paid in respect of brokerage accounts owned by all of the taxpayer's customers for the same taxable year.
- (h) Credit card banks (tax years beginning before January 1, 2015).**

- (1) Any banking institution whose business activities are taxable within and outside of this state and whose activities are limited to those described in Section 2(c)(2)(F) of the Bank Holding Company Act (12 U.S.C. § 1841(c)(2)(F)) may elect the allocation and apportionment method for the taxpayer's net income provided for in this provision. The election, if made, shall be irrevocable for successive periods of five (5) years. All net income derived directly or indirectly from the banking institution shall be apportioned to Rhode Island only to the extent that customers of the taxpayer are domiciled in Rhode Island. The portion of net income apportioned to Rhode Island shall be determined by multiplying the total net income from the sale of the services by a fraction determined in the following manner:
- (i) The numerator of the fraction shall be the income derived from accounts owned by customers domiciled in Rhode Island for the banking institution's taxable year; and

- (ii) The denominator of the fraction shall be income derived from accounts owned by all of the banking institution's customers for the same taxable year.

(i) Retirement and pension plans (tax years beginning before January 1, 2015).

(1) Any taxpayer located within the state that sells management, distribution or administration services, including without limitations, transfer agent, fund accounting, custody and other similar or related services, as described in this provision to or on behalf of an employee retirement plan or pension plan may elect the allocation and apportionment method for the taxpayer's net income provided for in this provision. The election, if made, shall be irrevocable for successive periods of five (5) years. All net income derived directly and indirectly from the sale of the management, distribution, or administration services to or on behalf of a retirement plan or pension plan, including net income received directly or indirectly from trustees, sponsors or participants of such a retirement plan or pension plan, shall be apportioned to Rhode Island only to the extent that the beneficiaries or participants of a retirement plan or pension plan are domiciled in Rhode Island as follows:

- (i) Net income shall be multiplied by a fraction, the numerator of which shall be Rhode Island receipts from the services during the taxable year and the denominator of which shall be the total receipts everywhere from the services for the same taxable year.
- (ii) For the purposes of this provision, Rhode Island receipts shall be determined by multiplying total receipts for the taxable year from a retirement plan or pension plan for which the services are performed by a fraction. The numerator of the fraction shall be the average of the number of total beneficiaries or participants of each retirement plan or pension plan domiciled in this state at the beginning of and at the end of taxable year of the taxpayer, and the denominator of the fraction shall be the average of the number of total beneficiaries or participants of the retirement plan or pension plan everywhere at the beginning of and at the end of each taxable year of the taxpayer.

(j) Sellers of international investment management services (tax years beginning before January 1, 2015).

- (1) Any qualified taxpayer located within the state which sells international investment management services to non-U.S. persons or non-U.S. investment funds shall exclude from its net income any income derived directly or indirectly from the sale of international investment management services.
- (2) For purposes of this section, "non-U.S. persons" means any person who is not a citizen of the United States and who is domiciled outside of the United States during the entire

taxable year; "non-U.S. investment funds" means any collective investment fund the sole beneficiaries of which are non-U.S. persons.

- (3) For purposes of this section, "international investment management services" shall include, without limitation, investment advice, investment research, investment consulting, portfolio management, administration or distribution services (including, without limitation, transfer agent, fund accounting, customary and other similar or related services) rendered to or on behalf of non-U.S. persons and non-U.S. investment funds.
- (4) For purposes of this section, a "qualified taxpayer" is one which during the taxable year employs, or together with affiliated taxpayers with which it is eligible to file a consolidated tax return for federal income tax purposes, an average of not less than five hundred (500) full-time equivalent employees in the state.

Rule 11. Special Apportionment Formulas – 2015 and Thereafter

(a) **Applicability of Special Apportionment Formulas – 2015 and Thereafter.** For tax years beginning **on or after** January 1, 2015, taxpayers deriving income from sources both within and outside of this state, or engaging in any activities or transactions both within and outside of this state for the purpose of profit or gain, shall generally apportion income according to the manner prescribed in Rule 8, using single sales factor apportionment and the principle of market-based sourcing. Notwithstanding this general rule, certain categories of taxpayers or members in combined groups listed below remain eligible to apportion income to Rhode Island according to modified formulas of apportionment, as set forth in subsections (b) through (g) of this Rule:

- (1) Motor carriers;
- (2) Airlines;
- (3) Regulated investment companies and securities brokerage services;
- (4) Credit card banks;
- (5) Retirement and pension plans;
- (6) Sellers of international investment management services.

In all such cases, taxpayers and combined group members eligible to apportion income according to a modified formula shall remain obligated to comply with Rhode Island's mandatory unitary combined reporting regime. When a taxpayer or member in a combined group that is categorized in subsection (a)(1) through (a)(6) is a member in a combined group with other categories of taxpayers (whether such categories of taxpayers are listed in this Regulation or not), the modified formula used for determining the portion of the sales factor of the taxpayer or member categorized in subsection (a)(1) through (a)(6), as set forth in subsections (b) through (g) of this Rule, shall not apply to the combined group as a whole or to members in the combined group that are categorized differently.

(b) **Motor carriers (tax years beginning after January 1, 2015).**

(1) To arrive at a determination of the share of net income attributable to Rhode Island for a motor carrier, the motor carrier's net income is multiplied by the motor carrier's apportionment percentage. The apportionment percentage is determined as a fraction, the numerator of which is the motor carrier's total Rhode Island sales, and the denominator of which is the motor carrier's total worldwide sales.

(2) A motor carrier's Rhode Island sales consist of the average of the inbound/outbound Rhode Island receipts plus all other receipts attributable to Rhode Island.

(c) Airlines (tax years beginning after January 1, 2015).

(1) To arrive at a determination of the share of net income attributable to Rhode Island for an airline, passenger revenue and freight revenue shall be allocated to Rhode Island based on the ratio of departures of flight aircraft, by type, from locations in this state compared to total departures everywhere, multiplied by total passenger revenue everywhere. All other receipts attributable to Rhode Island shall also be included in the numerator.

(d) Regulated investment companies and securities brokerage services (tax years beginning after January 1, 2015).

(1) The method for determining the share of net income attributable to Rhode Island for any taxpayer located within the state which sells management, distribution or administration services (including without limitations, transfer agent, fund accounting, custody and other similar or related services) to or on behalf of a regulated investment company (as defined in the Internal Revenue Code of 1986, as amended) is the same as the method set forth in Rule 10(g)(1) of this Regulation.

(2) The method for determining the share of net income attributable to Rhode Island for any taxpayer which provides securities brokerage services and which operates within the state is the same as the method set forth in Rule 10(g)(2) of this Regulation.

(e) Credit card banks (tax years beginning after January 1, 2015).

(1) The method for determining the share of net income attributable to Rhode Island for any banking institution whose business activities are taxable within and outside of this state and whose activities are limited to those described in Section 2(c)(2)(F) of the Bank Holding Company Act (12 U.S.C. § 1841(c)(2)(F)) is the same as the method set forth in Rule 10(h)(1) of this Regulation.

(f) Retirement and pension plans (tax years beginning after January 1, 2015).

(1) The method for determining the share of net income attributable to Rhode Island for any taxpayer located within the state that sells management, distribution or administration services, including without limitations, transfer agent, fund accounting, custody and other

similar or related services to or on behalf of an employee retirement plan or pension plan is the same as the method set forth in Rule 10(i)(1) of this Regulation.

(g) Sellers of international investment management services (tax years beginning after January 1, 2015).

(1) Regarding qualified taxpayers located within the state which sell international investment management services to non-U.S. persons or non-U.S. investment funds, such taxpayers shall determine net income in accordance with the provisions of Rule 10(j).

Rule 12. Variation of Method of Apportioning Income

(a) Tax Administrator's Authority to Vary Methods of Apportionment. If at any time the Tax Administrator, on his or her own motion or acting upon a complaint by a taxpayer, determines that the methods of apportionment provided are inequitable either to the state or to the taxpayer, the tax administrator, after affording the taxpayer reasonable opportunity to be heard, may apply any other method of apportionment that is equitable and, if necessary, shall re-determine the tax.

(b) Disputes Regarding Applicable Methods of Apportionment. When a dispute arises between the Tax Administrator and a taxpayer with respect to the method of apportionment applied, both the taxpayer and the Tax Administrator shall be entitled to initiate an appeals process through an independent arbitrator. In all cases, the arbitrator shall be selected by the taxpayer from a list of independent arbitrators approved by the American Arbitration Association, and all costs and fees, including legal fees for all parties, shall be borne by the taxpayer, regardless of the outcome of the arbitration on the merits. For purposes of the independent appeals process described in this provision, the various methods of apportionment are set forth in Rules 8, 9, 10 and 11 of this Regulation. The independent appeals process described in this provision shall be available only for disputes where proper selection of the method of apportionment to be applied to the taxpayer, in any given year, is the sole issue in dispute. The independent appeals process is not intended to resolve disputes concerning composition of a combined group, determination of combined group net income, the actual determination of apportionment factors, or to any other matter arising before or after selection of the taxpayer's method of apportionment. The decision resulting from the independent appeals process shall not prohibit either party from pursuing any legal remedy otherwise available if the issue is not resolved as a result of the appeal process. The decision resulting from the independent appeals process can be used as evidence.

Rule 13. Record Keeping

All C corporations shall maintain documentary evidence of all market sourcing determinations. 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 receipts 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 receipts, including its underlying assumptions, and shall provide such records to the Division of Taxation upon request. Failure to keep such records may result in market sourcing determinations by the Tax Administrator. In any case in which a taxpayer fails to retain contemporaneous records that explain the determination and application of its method of assigning receipts, including its underlying assumptions, or fails to provide such records to the Division of Taxation upon request, the Division of Taxation may treat the taxpayer's assignment of receipts as unsubstantiated, and may adjust the assignment of such receipts in a manner consistent with the applicable rules in this Regulation. Such determinations by the Tax Administrator shall be presumptively valid. The burden shall be on the taxpayer to maintain necessary evidence supporting classification of all income and all information related to calculation of Rhode Island income.

Rule 14. Effective Date

The effective date of this regulation is **MONTH XX, 2015**. It supersedes and replaces regulation CT04-04 Corporate Tax – Allocation of Income and Net Worth, promulgated April 1, 2003 and CT88-01 Corporation Tax – Ability to Apportion Net Income, promulgated December 31, 1988.

Rule 15. Appendix – Additional Examples

(a) *Additional Examples – from Rule 8(i)(8)(B)(i)(b), sales of in-person services*

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 receipts from sale of such services are in Rhode Island.

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

Example 6. Teaching Corp provides seminars in Rhode Island 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 Rhode Island the receipts from sales of the services are in Rhode Island.

(b) *Additional Examples – from Rule 8(i)(8)(B)(ii)(a)(I)(C), sales of services delivered to or on behalf of a customer by physical means, whether to an individual or business customer.*

Example 4. Fulfillment Corp, a corporation based outside Rhode Island, provides product delivery fulfillment services in Rhode Island and in neighboring states to Sales Corp, a corporation located outside Rhode Island 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 Rhode Island, Fulfillment Corp will, pursuant to its contract with Sales Corp, deliver that property from its fulfillment warehouse located outside Rhode Island. The receipts from the sale of the fulfillment services of Fulfillment Corp to Sales Corp are assigned to Rhode Island to the extent that Fulfillment Corp's deliveries on behalf of Sales Corp are to recipients in Rhode Island.

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

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

- (c) *Additional Examples – from Rule 8(i)(8)(B)(ii)(a)(II)(C), sales of services delivered to a customer by electronic transmission.*

Example 4. Net Corp, a corporation based outside Rhode Island, provides web-based services to a business customer, Business Corp, a company with offices in Rhode Island 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 Rhode Island 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 receipts from the sale are received in Rhode Island. 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 receipts from sales to Business Corp, Net Corp must assign the receipts 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 sales of services to 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 5. Net Corp, a corporation based outside Rhode Island, provides web-based services through the means of the Internet to more than 250 individual and business customers in Rhode Island 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 receipts from sales of services to any single customer. Net Corp may apply the safe harbor provision and may assign its receipts using each customer's billing address.

- (d) *Additional Examples – from Rule 8(i)(8)(B)(ii)(a)(III)(D), sales of services delivered electronically through or on behalf of an individual or business customer.*

Example 3. Web Corp, a corporation that is based outside Rhode Island, provides Internet content to viewers in Rhode Island 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. The receipts from Web Corp's sale of advertising space to its business customers are assigned to Rhode Island to the extent that the viewers of the Internet content are in Rhode Island, as measured by viewings or clicks. 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 Rhode Island receipts by multiplying the amount of receipts from sales of advertising by a percentage that reflects the Rhode Island population in the specific geographic area in which the content containing the advertising is delivered relative to the total population in such area.

Example 4. Retail Corp, a corporation that is based outside of Rhode Island, sells tangible property through its retail stores located in Rhode Island 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 Rhode Island receipts by multiplying the amount of its fee from Retail Corp by a percentage that reflects the Rhode Island population in the specific geographic area from which the calls are placed relative to the total population in such area.

Example 5. Web Corp, a corporation that is based outside of Rhode Island, 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 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 Rhode Island, develops an Internet-based information database outside Rhode Island 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 receipts from 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 Rhode Island by using a percentage that reflects the ratio of the Rhode Island 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. 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.

(e) *Additional Examples – from Rule 8(i)(8)(B)(iii)(b)(IV), sales of professional services*

Example 4. 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 Rhode Island, the receipts from the sale of Consulting Corp's services shall be assigned to Rhode Island. 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.

Example 5. Design Corp is a corporation based outside Rhode Island that provides graphic design and similar services in Rhode Island and in neighboring states. Design Corp enters into a contract at a location outside Rhode Island 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 receipts from sales of services from the individual customer. All of the design work is performed outside Rhode Island.

Receipts from the sale are in Rhode Island if the customer's billing address is in Rhode Island.

(f) *Additional Examples – from Rule 8(i)(8)(C)(v), license or lease of intangible property*

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 Rhode Island. Assume that Axel Corp lacks actual information regarding the proportion of Biker Co.'s receipts that are derived from Rhode Island customers. Also assume that Biker Co is granted the right to sell the scooters in a U.S. geographic region in which the Rhode Island 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 Division of Taxation reasonably establishes otherwise. Assuming that neither party establishes otherwise, 25% of the licensing fee constitutes Rhode Island receipts.

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 Division of Taxation will: (1) assign no part of the licensing fee paid for the production intangible to Rhode Island, and (2) assign 25% of the licensing fee paid for the marketing intangible to Rhode Island.

Example 7. Super Burger Corp, which is based outside Rhode Island, enters into franchise contracts with franchisees who agree to operate Better Burger restaurants as franchisees in various states. Several of the Super Burger Corp franchises are in Rhode Island. In each case, the franchise contract between the individual and Super Burger provides that the franchisee is to pay Super 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 Super 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 Rhode Island franchises constitute fees paid for the licensing of a marketing intangible. These fees constitute Rhode Island receipts because the franchises are for the right to make Rhode Island sales. The monthly franchise fees paid by Rhode Island franchisees constitute fees paid for (1) the license of marketing intangibles (the Super 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 Rhode Island receipts because in each case the use of the intangibles is to take

place in Rhode Island. The fees paid for the personal services are to be assigned pursuant to the assignment rules associated with the sale of a service.

Example 8. Online Corp, a corporation based outside Rhode Island, licenses an information database through the means of the Internet to individual customers that are resident in Rhode Island 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. 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 receipts 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 receipts from sales made to its individual customers are in Rhode Island in any case in which the customer's billing address is in Rhode Island.

Example 9. Net Corp, a corporation based outside Rhode Island, licenses an information database through the means of the Internet to a business customer, Business Corp, a company with offices in Rhode Island and two neighboring states. The license is a license of intangible property that resembles a sale of goods or services. 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 Rhode Island, 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 Rhode Island. 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 receipts 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.

Example 10. Net Corp, a corporation based outside Rhode Island, licenses an information database through the means of the Internet to more than 250 individual and business customers in Rhode Island and in other states. The license is a license of intangible property that resembles a sale of goods or services. 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 receipts from sales of database access from any single customer. Net Corp may apply the safe harbor provision, and may assign its receipts to a state or states using each customer's billing address.

Example 11. Web Corp, a corporation based outside of Rhode Island, licenses an Internet-based information database to business customers who then sublicense the database to individual end users that are resident in Rhode Island 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. 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 Rhode Island using a percentage that represents the ratio of the Rhode Island population in the specific geographic area in which Web Corp's customer sublicenses the database access relative to the total population in such area.

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