GENERAL ASSEMBLY OF NORTH CAROLINA
SESSION 2003

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SENATE DRS75092-LAxz-1 (12/16)

Short Title:	Update Corporate Tax Apportionment Formula.	(Public)
Sponsors:	Senators Clodfelter; Dalton, Hartsell, Hoyle, and Kerr.	
Referred to:		

A BILL TO BE ENTITLED

AN ACT TO ADJUST THE APPORTIONMENT FORMULA SALES FACTOR FOR BROADCASTERS AND PUBLISHERS AND TO UPDATE THE APPORTIONMENT FORMULA PROPERTY FACTOR FOR ALL CORPORATIONS BY EXCLUDING OUTER-JURISDICTIONAL PROPERTY FROM THAT FACTOR.

The General Assembly of North Carolina enacts:

SECTION 1. G.S. 105-130.4 reads as rewritten:

"**§ 105-130.4. Allocation and apportionment of income for corporations.**

(a) As used in this section, unless the context otherwise requires:

(1) 'Business income' means all income that is apportionable under the United States Constitution.

(1a) Broadcasting. – Transmitting radio or television programming to viewers or listeners by an electronic or other signal conducted by radio waves, microwaves, wires, coaxial cables, fiber optics, satellite transmissions, or any other means of communication.

(2) 'Commercial domicile' means the principal place from which the trade or business of the taxpayer is directed or managed.

(3) 'Compensation' means wages, salaries, commissions and any other form of remuneration paid to employees for personal services.

(4) 'Excluded corporation' means any corporation engaged in business as a building or construction contractor, a securities dealer, or a loan company or a corporation that receives more than fifty percent (50%) of its ordinary gross income from intangible property.

(4a) General formula. – A fraction, the numerator of which is the property factor plus the payroll factor plus twice the sales factor, and the denominator of which is four. If the sales factor does not exist, the denominator of the fraction is the number of existing factors. If the sales factor exists but the payroll factor or the property factor does not exist, the denominator of the fraction is the number of existing factors plus one.

(5) 'Nonbusiness income' means all income other than business income.

(5a) Outer-jurisdictional property. – Tangible personal property that is not physically located in any state. The term includes orbiting satellites and undersea transmission cables.

(6) 'Public utility' means any corporation that is subject to control of one of more of the following entities: the North Carolina Utilities Commission, the Federal Communications Commission, the Interstate Commerce Commission, the Federal Power Commission, or the Federal Aviation Agency; and that owns or operates for public use any plant, equipment, property, franchise, or license for the transmission of communications, the transportation of goods or persons, or the production, storage, transmission, sale, delivery or furnishing of electricity, water, steam, oil, oil products, or gas. The term also includes a motor carrier of property whose principal business activity is transporting property by motor vehicle for hire over the public highways of this State. The term does not include a corporation engaged in the business of broadcasting radio or television programming.

(6a) Radio programming. – Any performance, event, or production broadcast on radio, including news, sporting events, plays, stories, and other literary, commercial, educational, or artistic works, through the use of an audio tape, disk, or any other format or medium. Each episode of a series is considered separately.

(7) 'Sales' means all gross receipts of the corporation except for the following receipts:

a. Receipts from a casual sale of property.

b. Receipts allocated under subsections (c) through (h) of this section.

c. Receipts exempt from taxation.

d. The portion of receipts realized from the sale or maturity of securities or other obligations that represents a return of principal.

(8) 'Casual sale of property' means the sale of any property which was not purchased, produced or acquired primarily for sale in the corporation's regular trade or business.

(9) 'State' means any state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, any territory or possession of the United States, and any foreign country or political subdivision thereof.

(9a) Television programming. – Any performance, event, or production broadcast on television, including news, sporting events, plays, stories,

<u>and other literary, commercial, educational, or artistic works, through the use of video tape, disk, or any other format or medium. Each episode of a series is considered separately.</u>

(b) A corporation having income from business activity which is taxable both within and without this State shall allocate and apportion its net income or net loss as provided in this section. For purposes of allocation and apportionment, a corporation is taxable in another state if (i) the corporation's business activity in that state subjects it to a net income tax or a tax measured by net income, or (ii) that state has jurisdiction based on the corporation's business activity in that state to subject the corporation to a tax measured by net income regardless whether that state exercises its jurisdiction. For purposes of this section, 'business activity' includes any activity by a corporation that would establish a taxable nexus pursuant to 15 United States Code section 381.

(c) Rents and royalties from real or tangible personal property, gains and losses, interest, dividends less the portion deductible under G.S. 105-130.7, patent and copyright royalties and other kinds of income, to the extent that they constitute nonbusiness income, less related expenses shall be allocated as provided in subsections (d) through (h) of this section.

(d) (1) Net rents and royalties from real property located in this State are allocable to this State.

(2) Net rents and royalties from tangible personal property are allocable to this State:

a. If and to the extent that the property is utilized in this State, or

b. In their entirety if the corporation's commercial domicile is in this State and the corporation is not organized under the laws of, or is not taxable in, the state in which the property is utilized.

(3) The extent of utilization of tangible personal property in a state is determined by multiplying the rents and royalties by a fraction, the numerator of which is the number of days of physical location of the property in the state during the rental or royalty period in the income year and the denominator of which is the number of days of physical location of the property everywhere during all rental or royalty periods in the income year. If the physical location of the property during the rental or royalty period is unknown or unascertainable by the corporation, tangible personal property is utilized in the state in which the property was located at the time the rental or royalty payer obtained possession.

(e) (1) Gains and losses from sales or other disposition of real property located in this State are allocable to this State.

(2) Gains and losses from sales or other disposition of tangible personal property are allocable to this State if

a. The property had a situs in this State at the time of the sale, or

b. The corporation's commercial domicile is in this State and the corporation is not taxable in the state in which the property has a situs.

(3) Gains and losses from sales or other disposition of intangible personal property are allocable to this State if the corporation's commercial domicile is in this State.

(f) Interest and net dividends are allocable to this State if the corporation's commercial domicile is in this State. For purposes of this section, the term 'net dividends' means gross dividend income received less related expenses and less that portion of the dividends deductible under G.S. 105-130.7.

(g) (1) Royalties or similar income received from the use of patents, copyrights, secret processes and other similar intangible property are allocable to this State:

a. If and to the extent that the patent, copyright, secret process or other similar intangible property is utilized in this State, or

b. If and to the extent that the patent, copyright, secret process or other similar intangible property is utilized in a state in which the taxpayer is not taxable and the taxpayer's commercial domicile is in this State.

(2) A patent, secret process or other similar intangible property is utilized in a state to the extent that it is employed in production, fabrication, manufacturing, processing, or other use in the state or to the extent that a patented product is produced in the state. If the basis of receipts from such intangible property does not permit allocation to states or if the accounting procedures do not reflect states of utilization, the intangible property is utilized in the state in which the taxpayer's commercial domicile is located.

(3) A copyright is utilized in a state to the extent that printing or other publication originates in the state. If the basis of receipts from copyright royalties does not permit allocation to states or if the accounting procedures do not reflect states of utilization, the copyright is utilized in the state in which the taxpayer's commercial domicile is located.

(h) The income less related expenses from any other nonbusiness activities or investments not otherwise specified in this section is allocable to this State if the business situs of the activities or investments are located in this State.

(i) <u>Most Corporations. – </u>All business income of ~~corporations other than public utilities and excluded corporations shall be apportioned to this State by multiplying the income by a fraction, the numerator of which is the property factor plus the payroll factor plus twice the sales factor, and the denominator of which is four. Provided, that where the sales factor does not exist, the denominator of the fraction shall be the number of existing factors and where the sales factor exists but the payroll factor or the property factor does not exist, the denominator of the fraction shall be the number of existing factors plus one.~~<u>corporations, other than those corporations that are required to</u>

apportion business income under one of the special formulas provided in subsections (m) through (s2) of this section, is apportioned to this State by multiplying the income by the general formula.

(j) (1) The property factor is a fraction, the numerator of which is the average value of the corporation's real and tangible personal property owned or rented and used in this State during the income year and the denominator of which is the average value of all the corporation's real and tangible personal property owned or rented and used during the income year. Neither the numerator nor the denominator includes outer-jurisdictional property.

(2) Property owned by the corporation is valued at its original cost. Property rented by the corporation is valued at eight times the net annual rental rate. Net annual rental rate is the annual rental rate paid by the corporation less any annual rental rate received by the corporation from subrentals except that subrentals shall not be deducted when they constitute business income. Any property under construction and any property the income from which constitutes nonbusiness income shall be excluded in the computation of the property factor.

(3) The average value of property shall be determined by averaging the values at the beginning and end of the income year, but in all cases the Secretary of Revenue may require the averaging of monthly or other periodic values during the income year if reasonably required to reflect properly the average value of the corporation's property. A corporation that ceases its operations in this State before the end of its income year because of its intention to dissolve or to relinquish its certificate of authority, or because of a merger, conversion, or consolidation, or for any other reason whatsoever shall use the real estate and tangible personal property values as of the first day of the income year and the last day of its operations in this State in determining the average value of property, but the Secretary may require averaging of monthly or other periodic values during the income year if reasonably required to reflect properly the average value of the corporation's property.

(k) (1) The payroll factor is a fraction, the numerator of which is the total amount paid in this State during the income year by the corporation as compensation, and the denominator of which is the total compensation paid everywhere during the income year. All compensation paid to general executive officers and all compensation paid in connection with nonbusiness income shall be excluded in computing the payroll factor. General executive officers shall include the chairman of the board, president, vice-presidents, secretary, treasurer, comptroller, and any other officers serving in similar capacities.

(2) Compensation is paid in this State if:

a. The individual's service is performed entirely within the State; or

b. The individual's service is performed both within and without the State, but the service performed without the State is incidental to the individual's service within the State; or

c. Some of the service is performed in this State and (i) the base of operations or, if there is no base of operations, the place from which the service is directed or controlled is in this State, or (ii) the base of operations or the place from which the service is directed or controlled is not in any state in which some part of the service is performed, but the individual's residence is in this State.

(l) (1) The sales factor is a fraction, the numerator of which is the total sales of the corporation in this State during the income year, and the denominator of which is the total sales of the corporation everywhere during the income year. Notwithstanding any other provision under this Part, the receipts from any casual sale of property shall be excluded from both the numerator and the denominator of the sales factor. Where a corporation is not taxable in another state on its business income but is taxable in another state only because of nonbusiness income, all sales shall be treated as having been made in this State.

(2) Sales of tangible personal property are in this State if the property is received in this State by the purchaser. In the case of delivery of goods by common carrier or by other means of transportation, including transportation by the purchaser, the place at which the goods are ultimately received after all transportation has been completed shall be considered as the place at which the goods are received by the purchaser. Direct delivery into this State by the taxpayer to a person or firm designated by a purchaser from within or without the State shall constitute delivery to the purchaser in this State.

(3) Other sales are in this State if:

a. The receipts are from real or tangible personal property located in this State; or

b. The receipts are from intangible property and are received from sources within this State; or

c. The receipts are from services and the income-producing activities are in this State.

(m) All business income of a railroad company shall be apportioned to this State by multiplying the income by a fraction, the numerator of which is the 'railway operating revenue' from business done within this State and the denominator of which is the "total railway operating revenue" from all business done by the company as shown by its records kept in accordance with the standard classification of accounts prescribed by the Interstate Commerce Commission.

'Railway operating revenue' from business done within this State shall mean 'railway operating revenue' from business wholly within this State, plus the equal mileage proportion within this State of each item of 'railway operating revenue' received from the interstate business of the company. 'Equal mileage proportion' shall mean the proportion which the distance of movement of property and passengers over lines in this State bears to the total distance of movement of property and passengers over lines of the company receiving such revenue. 'Interstate business' shall mean 'railway operating revenue' from the interstate transportation of persons or property into, out of, or through this State. If the Secretary of Revenue shall find, with respect to any particular company, that its accounting records are not kept so as to reflect with exact accuracy such division of revenue by State lines as to each transaction involving interstate revenue, the Secretary of Revenue may adopt such regulations, based upon averages, as will approximate with reasonable accuracy the proportion of interstate revenue actually earned upon lines in this State. Provided, that where a railroad is being operated by a partnership which is treated as a corporation for income tax purposes and pays a net income tax to this State, or if located in another state would be so treated and so pay as if located in this State, each partner's share of the net profits shall be considered as dividends paid by a corporation for purposes of this Part and shall be so treated for inclusion in gross income, deductibility, and separate allocation of dividend income.

(n) All business income of a telephone company shall be apportioned to this State by multiplying the income by a fraction, the numerator of which is gross operating revenue from local service in this State plus gross operating revenue from toll services performed wholly within this State plus the proportion of revenue from interstate toll services attributable to this State as shown by the records of the company plus the gross operating revenue in North Carolina from other service less the uncollectible revenue in this State, and the denominator of which is the total gross operating revenue from all business done by the company everywhere less total uncollectible revenue. Provided, that where a telephone company is required to keep its records in accordance with the standard classification of accounts prescribed by the Federal Communications Commission the amounts in such accounts shall be used in computing the apportionment fraction as provided in this subsection.

(o) All business income of a motor carrier of property shall be apportioned by multiplying the income by a fraction, the numerator of which is the number of vehicle miles in this State and the denominator of which is the total number of vehicle miles of the company everywhere. The words 'vehicle miles' shall mean miles traveled by vehicles owned or operated by the company hauling property for a charge or traveling on a scheduled route.

(p) All business income of a motor carrier of passengers shall be apportioned by multiplying the income by a fraction, the numerator of which is the number of vehicle miles in this State and the denominator of which is the total number of vehicle miles of the company everywhere. The words 'vehicle miles' shall mean miles traveled by vehicles owned or operated by the company carrying passengers for a fare or traveling on a scheduled route.

(q) All business income of a telegraph company shall be apportioned by multiplying the income by a fraction, the numerator of which is the property factor plus the payroll factor plus the sales factor and the denominator of which is three.

The property factor shall be as defined in subsection (j) of this section, the payroll factor shall be as defined in subsection (k) of this section, and the sales factor shall be as defined in subsection (l) of this section.

(r) All business income of an excluded corporation and of all other public utilities shall be apportioned by multiplying the income by the sales factor as determined under subsection (l) of this section.

(s) All business income of an air or water transportation corporation shall be apportioned by a fraction, the numerator of which is the corporation's revenue ton miles in this State and the denominator of which is the corporation's revenue ton miles everywhere. The term 'revenue ton mile' means one ton of passengers, freight, mail, or other cargo carried one mile. In making this computation, a passenger is considered to weigh two hundred pounds.

<u>(s1) Broadcasters. – All business income of a corporation engaged in the business of broadcasting radio or television programming is apportioned by multiplying the income by the general formula, after modifying the numerator of the sales factor in accordance with this section. The numerator includes all receipts from broadcasting radio and television programming multiplied by an audience factor. For radio broadcasts and for television broadcasts by a television station, the audience factor is the ratio of the corporation's North Carolina listening or viewing audience to the corporation's total listening or viewing audience. For television broadcasts by a cable television system, the audience factor is the ratio of the cable television system's subscribers located in this State to all the cable television system's subscribers. A corporation may use published rating or subscription statistics, as appropriate, to determine its audience factor.</u>

<u>(s2) Publishers. – All business income of a corporation engaged in the business of publishing, selling, licensing, or distributing newspapers, magazines, trade journals, books, or other publications is apportioned by multiplying the income by the general formula, after modifying the numerator of the sales factor in accordance with this section. The numerator includes all the corporation's receipts from advertising and from the sale, rental, or other use of its customer lists multiplied by a circulation factor. The circulation factor is the ratio of the corporation's North Carolina purchasers and subscribers of a publication to the corporation's total purchasers and subscribers of the publication. A purchaser or subscriber of a publication is the final recipient of the publication. A separate circulation factor applies to each publication. If advertising in a publication is included only in copies of the publication distributed to a limited geographic area, the circulation factor is determined on the basis of the circulation within the limited geographic area. A corporation may use rating statistics published by the Audit Bureau of Circulations or other comparable statistics to determine the circulation factor for a publication.</u>

(t) (1) If any corporation believes that the method of allocation or apportionment as administered by the Secretary has operated or will so operate as to subject it to taxation on a greater portion of its income than is reasonably attributable to business or earnings within the State, it may file with the Tax Review Board a petition setting forth the facts upon which its belief is based and its argument with respect to the application of the allocation formula. This petition shall be filed in such form and within such time as the Tax Review Board may prescribe. The Board shall grant a hearing on the petition. The time limitations set in G.S. 105-241.2 for the date of the hearing, notification to the taxpayer, and a decision following the hearing apply to a hearing held pursuant to this subsection. At least three members of the Tax Review Board shall attend any hearing pursuant to such petition. In such cases, the Tax Review Board's membership shall be augmented by the addition of the Secretary, who shall sit as a member of the Board with full power to participate in its deliberations and decisions with respect to petitions filed under the provisions of this subsection. An informal record containing in substance the evidence, contentions and arguments presented at the hearing shall be made. All members of the augmented Tax Review Board shall consider such evidence, contentions and arguments and the decisions thereon shall be made by a majority vote of the augmented Board.

(2) If the corporation employs in its books of account a detailed allocation of receipts and expenditures which reflects more clearly than the applicable allocation formula prescribed by this section the income attributable to the business within this State, application for permission to base the return upon the taxpayer's books of account shall be considered by the Tax Review Board. The Board may permit such separate accounting method in lieu of applying the applicable allocation formula if the Board finds that method best reflects the income and earnings attributable to this State.

(3) If the corporation shows that any other method of allocation than the applicable allocation formula prescribed by this section reflects more clearly the income attributable to the business within this State, application for permission to base the return upon such other method shall be considered by the Tax Review Board. The application shall be accompanied by a statement setting forth in detail, with full explanations, the method the corporation believes will more nearly reflect its income from business within this State. If the Board concludes that the allocation formula prescribed by this section allocates to this State a greater portion of the net income of the corporation than is reasonably attributable to business or earnings within this State, it shall determine the allocable net income by such other method as it finds best calculated to assign to this State for taxation the portion of the corporation's net income reasonably attributable to its business or earnings within this State.

(4) There shall be a presumption that the appropriate allocation formula reasonably attributes to this State the portion of the corporation's income earned in this State, and the burden shall rest upon the corporation to show the contrary. The relief herein authorized shall be granted by the Board only in cases of clear, cogent and convincing proof that the petitioning corporation is entitled thereto. No corporation shall use any alternative formula or method other than the applicable allocation formula provided by statute in making a report or return of its income to this State except upon order in writing of the Board, and any return in which any alternative formula or other method, other than the applicable allocation formula prescribed by statute, is used without permission of the Board shall not be a lawful return.

When the Board determines, pursuant to the provisions of this subsection, that an alternative formula or other method more accurately reflects the income allocable to North Carolina and renders its decision with regard thereto, the corporation shall allocate its net income for future years in accordance with such determination and decision of the Board so long as the conditions constituting the basis upon which the decision was made remain unchanged or until such time as the business method of operation of the corporation changes. Provided, however, that the Secretary may, with respect to any subsequent year, require the corporation to furnish information relating to its property, operations, and activities.

(5) A corporation which proposes to do business in this State may file a petition with the Board setting forth the facts upon which it contends that the applicable allocation formula will allocate a greater portion of the corporation's future income to North Carolina than will be reasonably attributable to its proposed business or contemplated earnings within the State. Upon a proper showing in accordance with the procedure described above for determinations by the Board, the Board may authorize such corporation to allocate income from its future business to North Carolina on the basis prescribed by the Board under the provisions of this section for such future years if the conditions constituting the basis upon which the Board's decision is made remain unchanged and the business operations of the corporation continue to conform to the statement of proposed methods of business operation presented by the corporation to the Board.

(6) When the Secretary asserts liability under the formula adjustment decision of the Tax Review Board, an aggrieved corporation may pay the tax and bring a civil action for recovery under the provisions of Article 9."

S**ECTION 2.** This act is effective for taxable years beginning on or after January 1, 2003.