

103 KAR 16:270. Apportionment; receipts factor.

RELATES TO: KRS 141.040, 141.120, 141.121, 141.206

STATUTORY AUTHORITY: KRS 131.130, 141.018, 141.120

NECESSITY, FUNCTION, AND CONFORMITY: KRS 131.130(1) authorizes the Department of Revenue to promulgate administrative regulations to administer and enforce Kentucky's tax laws. KRS 141.120(9) requires that all apportionable income of multi-state corporations be apportioned to Kentucky by multiplying the income by a fraction. KRS 141.120(11)(d) authorizes the department to promulgate administrative regulations providing how to determine the receipts factor used in the multi-state apportionable income apportionment formula. This administrative regulation provides guidelines for determining the receipts factor of a multistate corporation.

Section 1. Definitions.

(1) "Advertising services" means an agreement to include the broadcast customer's advertising content in the broadcaster's film programming.

(2) "Affiliated airline" is defined by KRS 141.121(1)(a).

(3) "Barrel mile" means the transportation of one (1) barrel of liquid or gas one (1) mile.

(4) "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 that at the time of the transaction is kept in good faith in the normal course of business, and not for tax avoidance purposes.

(5) "Broadcast customer" means a person, corporation, partnership, limited liability company, or other entity, such as an advertiser or a platform distribution company, that has a direct connection or contractual relationship with the broadcaster under which revenue is derived by a broadcaster.

(6) "Broadcaster" means a taxpayer that is a television broadcast network, a cable program network, or a television distribution company. The term "broadcaster" does not include a platform distribution company.

(7) "Business customer" means a customer that is a business operating in any form, including a sole proprietorship. Sales to a non-profit organization, to a trust, to the U.S. Government, to a foreign, state, or local government, or to an agency or instrumentality of that government are treated as sales to a business customer and are assigned consistent with the rules for those sales.

(8) "Code" means the Internal Revenue Code as defined by KRS 141.010(14).

(9) "Delivered to a location" means to the location of the taxpayer's market for the service, which may not be the location of the taxpayer's employees or property.

(10) "Film programming" means one (1) or more performances, events, or productions (or segments of performances, events, or productions) intended to be distributed for visual and auditory perception, including items such as news, entertainment, sporting events, plays, stories, or other literary, commercial, educational, or artistic works.

(11) "Financial institution" is defined by KRS 136.500.

(12) "Financial organization" is defined by KRS 141.120(1)(c).

(13) "Individual customer" means a customer that is not a business customer.

(14) "Intangible property" means property that is not physical or whose representation by physical means is merely incidental and includes items such as 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 val-

ue; securities; and computer software.

(15) "Kentucky revenue passenger mile" is defined by KRS 141.121(1)(c).

(16) "Mile operated" means the movement of a barge, tug, or other watercraft one (1) mile.

(17) "Passenger airline is defined by KRS 141.121(1)(d).

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

(19) "Platform distribution company" means a cable service provider, a direct broadcast satellite system, an Internet content distributor, or any distributor that directly charges viewers for access to any film programming.

(20) "Population" means the most recent population data maintained by the U.S. Census Bureau for the year in question as of the close of the taxable period.

(21) "Provider" is defined by KRS 141.121(1)(e).

(22) "Public service company" is defined by KRS 141.0401(6)(i).

(23) "Qualified air freight forwarder" is defined by KRS 141.121(1)(f).

(24) "Receipts" is defined by KRS 141.120(1)(e).

(25) "Related member" is defined by KRS 141.205(1)(g).

(26) "Revenue car mile" means the movement of a loaded railroad car one (1) mile.

(27) "Revenue passenger mile" is defined by KRS 141.121(1)(g).

(28) "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 taxpayer with respect to the day-to-day execution and performance of a contract entered into by the taxpayer with the customer.

Section 2. Additional Principles.

(1) Year to year consistency. If the taxpayer departs from or modifies the basis for excluding or including gross receipts in the receipts factor used in returns for prior years, the taxpayer shall disclose in the return for the current year the nature and extent of the modification.

(2) State to state consistency. If the returns or reports filed by the taxpayer with all states to which the taxpayer reports are not uniform in the inclusion or exclusion of gross receipts, the taxpayer shall disclose in its Kentucky return the nature and extent of the variance.

(3) Denominator. The denominator of the receipts factor shall include the gross receipts derived by the taxpayer from transactions and activity in the regular course of its trade or business, except gross receipts excluded under this administrative regulation.

(4) Numerator. The numerator of the receipts factor shall include gross receipts attributable to this state and derived by the taxpayer from transactions and activity in the regular course of its trade or business, except gross receipts excluded under this administrative regulation.

Section 3. Sales of Tangible Personal Property in This State.

(1) Gross receipts from sales of tangible personal property (except sales to the United States Government) are in this state if the property is delivered or shipped to a purchaser within this state regardless of the f.o.b. point or other conditions of sale.

(2) Property shall be determined as delivered or shipped to a purchaser within this state if the recipient is located in this state, even though the property is ordered from outside this state.

Example. The taxpayer, with inventory in State A, sold \$100,000 of its products to a purchaser having branch stores in several states, including Kentucky. The order for the purchase was placed by the purchaser's central purchasing department located in State B. \$25,000 of the purchase order was shipped directly to purchaser's branch store in Kentucky. The branch

store in Kentucky is the purchaser with respect to \$25,000 of the taxpayer's sales.

(3) Property is delivered or shipped to a purchaser within this state if the shipment terminates in this state, even though the property is subsequently transferred by the purchaser to another state.

Example. The taxpayer makes a sale to a purchaser who maintains a central warehouse in Kentucky at which all merchandise purchases are received. The purchaser reships the goods to its branch stores in other states for sale. All of the taxpayer's products shipped to the purchaser's warehouse in Kentucky constitute property delivered or shipped to a purchaser within Kentucky.

(4) A purchaser within this state shall include the ultimate recipient of the property if the taxpayer in this state, at the designation of the purchaser, delivers to or has the property shipped to the ultimate recipient within this state.

Example. A taxpayer in Kentucky sold merchandise to a purchaser in State A. Taxpayer directed the manufacturer or supplier of the merchandise in State B to ship the merchandise to the purchaser's customer in Kentucky pursuant to purchaser's instructions. The sale by the taxpayer is in Kentucky.

(5) If property being shipped by a seller from the state of origin to a consignee in another state is diverted while en route to a purchaser in this state, the sales are in this state.

Example. The taxpayer, a produce grower in State A, begins shipment of perishable produce to the purchaser's place of business in State B. While en route, the produce is diverted to the purchaser's place of business in Kentucky in which state the taxpayer is subject to tax. The sale by the taxpayer is attributed to Kentucky.

Section 4. Sales of Tangible Personal Property to the United States Government. Gross receipts from sales of tangible personal property to the United States Government are in this state if the property is shipped from an office, store, warehouse, factory, or other place of storage in this state. For the purposes of this administrative regulation, only sales for which the United States Government makes direct payment to the seller pursuant to the terms of a contract constitute sales to the United States Government. Sales by a subcontractor to the prime contractor, the party to the contract with the United States Government, do not constitute sales to the United States Government.

(1) Example. A taxpayer contracts with General Services Administration to deliver X number of trucks which were paid for by the United States Government. The sale is a sale to the United States Government.

(2) Example. The taxpayer, as a subcontractor to a prime contractor with the National Aeronautics and Space Administration, contracts to build a component of a rocket for \$1,000,000. The sale by the subcontractor to the prime contractor is not a sale to the United States Government.

Section 5. Sales Other Than Sales of Tangible Personal Property: General Rules. KRS 141.120(11) provides for the inclusion in the numerator of the receipts factor of gross receipts arising from transactions other than sales of tangible personal property.

(1) Market-Based Sourcing. Receipts, other than receipts described in KRS 141.120(10) (from sales of tangible personal property), are in this state within the meaning of KRS 141.120(11) if and to the extent that the taxpayer's market for the sales is in this state. The provisions in this section establish uniform rules for:

(a) Determining whether and to what extent the market for a sale other than the sale of tangible personal property is in this state;

(b) Reasonably approximating the state or states of assignment if the state or states cannot

be determined;

(c)1. Excluding receipts from the sale of intangible property from the numerator and denominator of the receipts factor pursuant to KRS141.120(11)(a)(4)(b)iii;

2. Excluding receipts from the denominator of the receipts factor, pursuant to KRS 141.120(11)(c) if the state or states of assignment cannot be determined or reasonably approximated; or

3. Excluding receipts from the denominator of the receipts factor, pursuant to KRS 141.120(11)(c) if the taxpayer is not taxable in the state to which the receipts are assigned as determined under KRS 141.120(3).

(2) General Principles of Application; Contemporaneous Records. In order to satisfy the requirements of this administrative regulation, a taxpayer's assignment of receipts from sales of other than tangible personal property shall be consistent with the following principles:

(a)1. A taxpayer shall apply the rules set forth in this administrative regulation based on objective criteria and shall consider all sources of information reasonably available to the taxpayer upon its tax filing including, items such as the taxpayer's books and records kept in the normal course of business;

2. A taxpayer shall determine its method of assigning receipts in good faith, and apply it consistently with respect to similar transactions year to year; and

3. 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 those records to the department upon request.

(b) This administrative regulation provides various assignment rules that apply sequentially in a hierarchy. For each sale to which a hierarchical rule applies, a taxpayer shall make an effort to apply the primary rule applicable to the sale before seeking to apply the next rule in the hierarchy (and shall continue to do so with each succeeding rule in the hierarchy, if applicable). For example, in some cases, the applicable rule first requires a taxpayer to determine the state or states of assignment, and if the taxpayer cannot do so, the rule requires the taxpayer to reasonably approximate the state or states. In these cases, the taxpayer shall attempt to determine the state or states of assignment (i.e., apply the primary rule in the hierarchy) in good faith and with reasonable effort before it may reasonably approximate the state or states.

(c) A taxpayer's method of assigning its receipts, including the use of a method of approximation, if applicable, shall reflect an attempt to obtain the most accurate assignment of receipts consistent with this administrative regulation, rather than an attempt to lower the taxpayer's tax liability. A method of assignment that is reasonable for one (1) taxpayer may not necessarily be reasonable for another taxpayer, depending upon the applicable facts.

(3) Rules of Reasonable Approximation.

(a) This administrative regulation establishes uniform rules for determining whether and to what extent the market for a sale other than the sale of tangible personal property is in this state. The administrative regulation sets forth rules of reasonable approximation, which apply if the state or states of assignment cannot be determined. In some instances, the reasonable approximation shall be made in accordance with specific rules of approximation prescribed in this administrative regulation. In other cases, the applicable rule in this administrative 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 may be obtained under the applicable rules or standards set forth in this administrative regulation.

(b) Approximation Based Upon Known Sales.

1. If applying the applicable rules set forth in subsections (7), (8), (9), and (10) of this section, a taxpayer may 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 those

sales; and

2. The taxpayer reasonably believes, based on all available information, that the geographic distribution of some or all of the remainder of those 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 receipts factor in the same proportion as its assigned receipts. This rule applies in the context of licenses and sales of intangible property if the substance of the transaction resembles a sale of goods or services.

(c) Related-Member Transactions – Information Imputed from Customer to Taxpayer. If a taxpayer has receipts subject to this administrative regulation from transactions with a related-member customer, information that the customer has that is relevant to the sourcing of receipts from these transactions is imputed to the taxpayer.

(4) Rules with Respect to Exclusion of Receipts from the Receipts Factor.

(a) The receipts factor only includes those amounts defined as receipts.

(b) Certain receipts arising from the sale of intangibles are excluded from the numerator and denominator of the sales factor pursuant to KRS 141.120(11)(a)(4)(b)iii.

(c) In a case in which a taxpayer cannot ascertain the state or states to which receipts of a sale are to be assigned pursuant to the applicable rules set forth in this administrative regulation (including through the use of a method of reasonable approximation, if relevant) using a reasonable amount of effort undertaken in good faith, the receipts shall be excluded from the denominator of the taxpayer's receipts factor pursuant to KRS 141.120(11)(c).

(d) In a case in which a taxpayer may ascertain the state or states to which receipts from a sale are to be assigned pursuant to the applicable rules set forth in this administrative regulation, but the taxpayer is not taxable in one (1) or more of those states, the receipts that may be assigned to those states where the taxpayer is not taxable shall be excluded from the denominator of the taxpayer's receipts factor pursuant to KRS 141.120(11)(c).

(e) Receipts of a taxpayer from hedging transactions, or from the maturity, redemption, sale, exchange, loan, or other disposition of cash or securities, shall be excluded pursuant to KRS 141.120(1)(e).

(f) Nothing in the provisions adopted here pursuant to KRS 141.120 is intended to limit the application of KRS 141.120(12) or the authority granted to the department under KRS 141.120(12).

(5) Sale, Rental, Lease, or License of Real Property. In the case of a sale, rental, lease, or license of real property, the receipts from the sale are in this state if and to the extent that the property is in this state.

(6) Rental, Lease, or License of Tangible Personal Property. In the case of a rental, lease, or license of tangible personal property, the receipts from the sale are in this state if and to the extent that the property is in this state. If property is mobile property that is located both within and without this state during the period of the lease or other contract, the receipts assigned to this state are the receipts from the contract period multiplied by the fraction computed under 103 KAR 16:290. (as adjusted if necessary to reflect differences between usage during the contract period and usage during the taxable year).

(7) Sale of a Service.

(a) General Rule. The receipts from a sale of a service are in this state if and to the extent that the service is delivered to a location in this state. The rules to determine the location of the delivery of a service in the context of several specific types of service transactions are set forth in this subsection and in subsections (8), (9), and (10) of this section.

(b) In-Person Services.

1. Except as provided in this paragraph, in-person services are services that are physically provided in person by the taxpayer, if 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 when the services are performed. This rule includes situations when the services are provided on behalf of the taxpayer by a third-party contractor. Examples of in-person services may include:

- a. Warranty and repair services;
- b. Cleaning services;
- c. Plumbing services;
- d. Carpentry;
- e. Construction contractor services;
- f. Pest control;
- g. Landscape services;
- h. Medical and dental services, including medical testing, x-rays and mental health care and treatment;
- i. Child care;
- j. Hair cutting and salon services;
- k. Live entertainment and athletic performances; and
- l. In-person training or lessons.

2. In-person services include services as described in subparagraph 1., clauses a. through l. of this paragraph that are performed:

- a. At a location that is owned or operated by the service provider; or
- b. A location of the customer, including the location of the customer's real or tangible personal property.

3. Various professional services, including services such as accounting, financial and consulting services, and other similar services are not treated as in-person services within the meaning of this paragraph, although they may involve some amount of in-person contact.

4. Assignment of Receipts.

Rule of Determination. Except as provided in this subparagraph, if the service provided by the taxpayer is an in-person service, the service is delivered to the location where the service is received. Therefore, the receipts from a sale are in this state if and to the extent the customer receives the in-person service in this state. 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:

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

b. If the service is performed with respect to the customer's real estate in this state or if the service is performed with respect to the customer's tangible personal property at the customer's residence or in the customer's possession in this state, the service is received in this state.

c. If 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 within or outside this state, the service is received in this state if the property is shipped or delivered to the customer in this state.

5. Rule of Reasonable Approximation. If the state or states where a service is actually received cannot be determined, but the taxpayer has sufficient information regarding the place of receipt from which it may reasonably approximate the state or states where the service is received, the taxpayer shall reasonably approximate the state or states. If the state to which the receipts are to be assigned may be determined or reasonably approximated, but the taxpayer is not taxable in that state, the receipts that may be assigned to the state are excluded from the denominator of the taxpayer's receipts factor pursuant to KRS 141.120(11)(c).

6. Examples. In these examples assume, unless otherwise stated, that the taxpayer is taxable in each state to which its receipts may be assigned, so that there is no requirement that the receipts from the sale or sales be eliminated from the denominator of the taxpayer's receipts factor. For purposes of the examples, it is irrelevant whether the services are performed by an employee of the taxpayer, or by an independent contractor acting on the taxpayer's behalf.

a. Example. Salon Corp has retail locations in Kentucky 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 Kentucky. The receipts from sales of services provided at Salon Corp's locations outside Kentucky, even if provided to residents of Kentucky, are not receipts from in-state sales.

b. Example. Landscape Corp provides landscaping and gardening services in Kentucky 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 Kentucky when the services are performed. The receipts from sale of services provided at the in-state location are in Kentucky.

c. Example. Same facts as in Example b., 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 those locations of Retail Corp that are in Kentucky and in other states. The receipts from the sale of services provided to Retail Corp are in Kentucky to the extent the services are provided in Kentucky.

d. Example. Camera Corp provides camera repair services at a Kentucky 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 these cases, the repaired camera is then returned to the customer at Camera Corp's Kentucky location. The receipts from sale of these services are in Kentucky.

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

f. Example. Teaching Corp provides seminars in Kentucky 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 residents outside the state, and the students who attend the seminars include students that are residents outside the state. Because the seminars are taught in Kentucky, the receipts from sales of the services are in Kentucky.

(8) Services Delivered to the Customer, or on Behalf of the Customer, or Delivered Electronically Through the Customer.

(a) If the service provided by the taxpayer is not an in-person service within the meaning of subsection (7)(b) of this section, or a professional service within the meaning of subsection (10) of this section, and the service is delivered to or on behalf of the customer, or delivered electronically through the customer, the receipts from a sale are in this state if and to the extent that the service is delivered in this state. For the purposes of this subsection and subsection (9) of this section, 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 (1) 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 may be delivered to or on behalf of a customer by physical means or through electronic transmission.

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.

(b) Assignment of Receipts. The assignment of receipts to a state or states in the instance of a sale 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 subsection, a service delivered by an electronic transmission is not a delivery by a physical means). If a rule of assignment set forth in this administrative regulation, 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. If the state to which the receipts from a sale are to be assigned may be determined or reasonably approximated, but the taxpayer is not taxable in that state, the receipts that may be assigned to that state are excluded from the denominator of the taxpayer's receipts factor.

1. 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:

- a. Product delivery services if property is delivered to the customer or to a third party on behalf of the customer;
- b. The delivery of brochures, fliers, or other direct mail services;
- c. The delivery of advertising or advertising-related services to the customer's intended audience in the form of a physical medium; and
- d. The sale of custom software if the taxpayer installs the custom software at the customer's site (e.g., if software is developed for a specific customer in a case when the transaction is properly treated as a service transaction for purposes of corporate taxation.) The rules in this administrative regulation apply whether the taxpayer's customer is an individual customer or a business customer.

2. Rule of Determination. In assigning the receipts from a sale of a service delivered to a customer or on behalf of a customer through a physical means, a taxpayer shall first attempt to determine the state or states where the service is delivered. If the taxpayer is able to determine the state or states where the service is delivered, it shall assign the receipts to that state or states.

3. Rule of Reasonable Approximation. If 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 may reasonably approximate the state or states where the service is delivered, it shall reasonably approximate the state or states.

4. Examples. In these examples assume, unless otherwise stated, that the taxpayer is taxable in each state to which its receipts may be assigned, so that there is no requirement in these examples that the receipts shall be eliminated from the denominator of the taxpayer's receipts factor.

a. Example. Direct Mail Corp, a corporation based outside Kentucky, provides direct mail services to its customer, Business Corp. Business Corp contracts 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 Kentucky 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 Kentucky to the extent that the services are delivered on behalf of Business Corp to

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

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

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

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

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

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

(9) Delivery to a Customer by Electronic Transmission. Services delivered by electronic transmission include services such as those 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 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.

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

b. Rules of Reasonable Approximation. If the taxpayer cannot determine the state or states where the customer actually receives the service, but has sufficient information regarding the place of receipt from which it may reasonably approximate the state or states where the ser-

vice is received, it shall reasonably approximate the state or states. If a taxpayer does not have sufficient information from which it may determine or reasonably approximate the state or states in which the service is received, it shall reasonably approximate the state or states using the customer's billing address.

2. Services Delivered By Electronic Transmission to a Business Customer.

a. Rule of Determination. In the case of the delivery of a service to a business customer by electronic transmission, the service is delivered in this state if and to the extent that the taxpayer's customer receives the service in this state. If the taxpayer may determine the state or states where the service is received, it shall assign the receipts from that sale to the state or states. For purposes of paragraph (b)2. of this subsection it is intended that the state or states where the service is received reflect the location at which the service is directly used by the employees or designees of the customer.

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

c. Secondary Rule of Reasonable Approximation. In the case of the delivery of a service to a business customer by electronic transmission if a taxpayer does not have sufficient information from which it may determine or reasonably approximate the state or states in which the service is received, the taxpayer shall reasonably approximate the state or states as set forth in this administrative regulation. In these cases, unless the taxpayer may apply the safe harbor set forth in this subsection the taxpayer shall reasonably approximate the state or states in which the service is received as follows:

i. By assigning the receipts from the sale to the state where the contract of sale is principally managed by the customer;

ii. 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

iii. If the customer's place of order is not reasonably determinable, by assigning the receipts from the sale using the customer's billing address; except if the taxpayer derives more than five (5) percent of its receipts from sales of services from any single customer, then the taxpayer shall identify the state in which the contract of sale is principally managed by that customer.

d. Safe Harbor. In the case of the delivery of a service to a business customer by electronic transmission a taxpayer may not be able to determine, or reasonably approximate the state or states in which the service is received. In these cases, the taxpayer may, in lieu of the rule stated in paragraph (a)2.c. of this subsection, apply the safe harbor stated in this clause. Under this safe harbor, a taxpayer may assign its receipts from sales to a particular customer based upon the customer's billing address in a taxable year in which the taxpayer:

(i) Engages in substantially similar service transactions with more than 250 customers, whether business or individual; and

(ii) Does not derive more than five (5) percent of its receipts from sales of all services from that customer. This safe harbor applies only for purposes of services delivered by electronic transmission to a business customer.

e. Related Member Transactions. In the case of a sale of a service by electronic transmission to a business customer that is a related member, the taxpayer may not use the secondary rule of reasonable approximation in subclause iii of clause c. within this subparagraph, but may use the rule of reasonable approximation and the safe harbor if the department may aggregate sales to related members in determining whether the sales exceed five (5) percent of receipts from sales of all services under that safe harbor provision if necessary or appropriate to pre-

vent distortion.

f. Examples. In these examples, unless otherwise stated, assume that the taxpayer is not related to the customer to which the service is delivered. Assume that the taxpayer is taxable in each state to which its receipts may be assigned, so that there is no requirement in these examples that the receipts shall be eliminated from the denominator of the taxpayer's receipts factor. Further, assume if relevant, unless otherwise stated, that the safe harbor set forth in clause d. of this subparagraph does not apply.

(i) Example. Support Corp, a corporation that is based outside Kentucky, 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 Kentucky and other states. Support Corp supplies its services on a case-by-case basis if 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 may determine where its services are received, and therefore shall assign its receipts to these locations. The receipts from sales made to Support Corp's individual and business customers are in Kentucky to the extent that Support Corp's services are received in Kentucky.

(ii) Example. Online Corp, a corporation based outside Kentucky, provides Web-based services through the means of the Internet to individual customers who are residents in Kentucky 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 may either determine the state or states where the services are received, or, if it cannot determine the state or states, it has sufficient information regarding the place of receipt to reasonably approximate the state or states. However, Online Corp cannot determine or reasonably approximate the state or states of receipt for all of the sales of its services. 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 shall assign to Kentucky the receipts from sales for which it does not know the customers' locations in the same proportion as those receipts for which it has this information.

(iii) Example. Same facts as in Example (ii), 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 shall assign the receipts from sales of its services for which it lacks information as provided to its individual customers using the customers' billing addresses.

(iv) Example. Same facts as in Example (iii), except that Online Corp is not taxable in one (1) state to which some of its receipts from sales may be assigned. The receipts that may be assigned to that state are excluded from the denominator of Online Corp's receipts factor.

(v) Example. Net Corp, a corporation based outside Kentucky, provides Web-based services to a business customer, Business Corp, a company with offices in Kentucky and two (2) 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 Kentucky were responsible for seventy-five (75) percent of Business Corp's use of Net Corp's services, and Business Corp employees in other states were responsible for twenty-five (25) percent of Business Corp's use of Net Corp's services. Seventy-five (75) percent of the receipts from the sale are received in Kentucky. 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 the location or locations. Under these circumstances, if Net Corp derives five (5) percent or less of its receipts from sales to Business Corp, Net Corp shall assign the receipts under the secondary rule of approximation to the state where Business Corp principally managed the contract, or if that state is not 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 five (5) percent of its receipts from sales of services to Business Corp, Net Corp shall identify the state in which its contract of sale is principally managed by Business Corp and shall assign the receipts to that state.

(vi) Example. Net Corp, a corporation based outside Kentucky, provides Web-based services through the means of the Internet to more than 250 individual and business customers in Kentucky 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 the state or states. Assume that Net Corp does not derive more than five (5) percent of its receipts from sales of services to a single customer. Net Corp may apply the safe harbor, and may assign its receipts using each customer's billing address. If Net Corp is not taxable in one (1) or more states to which some of its receipts may be assigned, it shall exclude those receipts from the denominator of its receipts factor.

(b) 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 (1) 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.

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

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

3. Select Secondary Rules of Reasonable Approximation.

a. If a taxpayer's service is the direct or indirect electronic delivery of advertising on behalf of its customer to the customer's intended audience, and if the taxpayer lacks sufficient infor-

mation regarding the location of the audience from which it may determine or approximate that location, the taxpayer shall approximate the audience in a state for the advertising using the following secondary rules of reasonable approximation. If a taxpayer is delivering advertising directly or indirectly to a known list of subscribers, the taxpayer shall 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 that area. For a taxpayer with less information about its audience, the taxpayer shall 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 that area.

b. The taxpayer shall approximate the extent to which the service is received in a state by using the percentage that reflects the ratio of the state's population in the specific geographic area in which the taxpayer's intermediary resells the services, relative to the total population in that area:

(i) If a taxpayer's service is the delivery of a service to a customer that then acts as the taxpayer's intermediary in reselling that service to end users or other third party recipients; or

(ii) If the taxpayer lacks sufficient information regarding the location of the end users or other third party recipients from which it may determine or reasonably approximate that location.

c. Examples. Assume in each of these examples that the taxpayer that provides the service is taxable in this state and shall apportion its income pursuant to KRS 141.120.

(i) Example: Web Corp, a corporation that is based outside Kentucky, provides Internet content to viewers in Kentucky and other states. Web Corp sells advertising space to business customers pursuant to which the customers' advertisements shall 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 Web site. Web Corp's sale of advertising space to its business customers is assigned to Kentucky to the extent that the viewers of the Internet content are in Kentucky, 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 the location, Web Corp shall approximate the amount of its Kentucky sales by multiplying the amount of the sales by a percentage that reflects the Kentucky population in the specific geographic area in which the content containing the advertising is delivered relative to the total population in the area.

(ii) Example. Retail Corp, a corporation that is based outside of Kentucky, sells tangible property through its retail stores located in Kentucky 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. 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 shall assign the proceeds from this service to the state or states from which the phone calls are placed by the 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 the locations, Answer Co shall approximate the amount of its Kentucky sales by multiplying the amount of its fee from Retail Corp by a percentage that reflects the Kentucky population in the specific geographic area from which the calls are placed relative to the total population in the area.

(iii) Example. Web Corp, a corporation that is based outside of Kentucky, sells tangible property to customers via its Internet Web site. Design Co designed and maintains Web Corp's

Web site, including making changes to the site based on customer feedback received through the site. Design Co's services are delivered to Web Corp, the proceeds from which are assigned pursuant to this subsection. 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.

(iv) Example. Wholesale Corp, a corporation that is based outside Kentucky, develops an Internet-based information database outside Kentucky and enters into a contract with Retail Corp under which 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. If 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. Wholesale Corp's services are being delivered through Retail Corp to the end user. Wholesale Corp shall assign its sales to Retail Corp to the state or states in which the end users receive access to Wholesale Corp's database. If Wholesale Corp cannot determine the state or states where the end users actually receive access to Wholesale Corp's database, and lacks sufficient information regarding the location from which the end users access the database to reasonably approximate the location, Wholesale Corp shall approximate the extent to which its services are received by end users in Kentucky. Wholesale Corp shall approximate by using a percentage that reflects the ratio of the Kentucky population in the specific geographic area in which Retail Corp regularly markets and sells Wholesale Corp's database relative to the total population in the area. 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.

(10) Professional Services.

(a) Except as provided in this subsection, professional services are services that require specialized knowledge, and in some cases, require a professional certification, license, or degree. These services include the performance of technical services that require the application of specialized knowledge. Professional services include, services such as:

1. Management services;
2. Bank and financial services;
3. Financial custodial services;
4. Investment and brokerage services;
5. Fiduciary services;
6. Tax preparation;
7. Payroll and accounting services;
8. Lending services;
9. Credit card services (including credit card processing services);
10. Data processing services;
11. Legal services;
12. Consulting services;
13. Video production services;
14. Graphic and other design services;
15. Engineering services; and
16. Architectural services.

(b) Overlap with Other Categories of Services.

1. Certain services that are under "professional services" as set forth in paragraph (a)1.

through 16. of this subsection are nevertheless treated as "in-person services", and are assigned under the rules of subsection (7)(b) of this section. Professional services that are physically provided in person by the taxpayer such as carpentry, certain medical and dental services or child care services, if 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 when the services are performed, are "in-person services". In-person services are assigned as these, but may be considered to be "professional services." However, professional services if the service is of an intellectual or intangible nature, such as legal, accounting, financial, and consulting services are assigned as professional services under the rules of this subsection, notwithstanding the fact that these services may involve some amount of in-person contact.

2. Professional services may in some cases include the transmission of one (1) or more documents or other communications by mail or by electronic means. In some cases, all or most communications between the service provider and the service recipient may be by mail or by electronic means. However, in these cases, despite this transmission, the assignment rules that apply are those set forth in this subsection and not those set forth in subsection (8) of this section pertaining to services delivered to a customer or through or on behalf of a customer.

(c) Assignment of Receipts. In the case of a professional service, it is generally possible to characterize the location of delivery in multiple ways by emphasizing different elements of the service provided, no one (1) of which will consistently represent the market for the services. Therefore, the location of delivery in the case of professional services is not susceptible to a general rule of determination, and shall 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 taxpayer's customer is the person that contracts for the service, irrespective of whether another person pays for or benefits from the taxpayer's services. In any instance in which the taxpayer is not taxable in the state to which receipts from a sale is assigned, the receipts are excluded from the denominator of the taxpayer's receipts factor.

1. General Rule. Receipts from sales of professional services are assigned in accordance with this section, other than those services described in:

- a. Subparagraph 2. of this paragraph on architectural and engineering services;
- b. Subparagraph 3. of this paragraph on services provided by a financial institution; and
- c. Subparagraph 4. of this paragraph on transactions with related members.

d. Professional Services Delivered to Individual Customers. Except as provided in this subsection, in any instance in which the service provided is a professional service and the taxpayer's customer is an individual customer, the state or states in which the service is delivered shall be reasonably approximated as set forth in this subsection. 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. Except in any instance in which the taxpayer derives more than five (5) percent of its receipts from sales of all services from an individual customer, the taxpayer shall identify the customer's state of primary residence and assign the receipts from the service or services provided to that customer to that state.

e. Professional Services Delivered to Business Customers. Except as provided in this subsection, in any instance in which the service provided is a professional service and the taxpayer's customer is a business customer, the state or states in which the service is delivered shall

be reasonably approximated as set forth in this section. Unless the taxpayer may use the safe harbor set forth in clause f. of this subparagraph, the taxpayer shall assign the receipts from the sale as follows:

(i) By assigning the receipts to the state where the contract of sale is principally managed by the customer;

(ii) If the place of customer management is not reasonably determinable, to the customer's place of order; and

(iii) If the customer's place of order is not reasonably determinable, to the customer's billing address. Except in any instance in which the taxpayer derives more than five (5) percent of its receipts from sales of all services from a customer, the taxpayer shall identify the state in which the contract of sale is principally managed by the customer.

f. Safe Harbor; Large Volume of Transactions. Except as provided in, the rules set forth in clauses d. and e. of this subparagraph, a taxpayer may assign its receipts from sales to a particular customer based on the customer's billing address in any taxable year in which the taxpayer engages in substantially similar service transactions with more than 250 customers, whether individual or business, and does not derive more than five (5) percent of its receipts from sales of all services from that customer. This safe harbor applies only for purposes of clause d. of this subparagraph.

2. 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 subsection. However, unlike in the case of the general rule that applies to professional services:

a. The receipts from a sale of 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 the state or states; and

b. The receipts from a sale of 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 the state or states, including real estate improvements located in, or expected to be located in, the 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 subparagraph, the receipts from a sale of these services shall be assigned under the general rule for professional services.

3. Services Provided by Financial Organizations and Institutions. The apportionment rules that apply to financial organizations are set forth in KRS 141.121(5) and in this administrative regulation. In any instance in which a financial organization performs services that are to be assigned pursuant to KRS 141.121(5) and this administrative regulation, including, for example, financial custodial services, those services are considered professional services within the meaning of this subsection, and are assigned according to the general rule for professional service transactions as set forth in paragraph(c)1. of this subsection. Financial institutions are subject to the franchise tax imposed by KRS 136.505 and related statutes and administrative regulations under KRS Chapter 136 and are exempt from the corporation income tax per KRS 141.040(1)(a) and the limited liability entity tax per KRS 141.040(6)(a).

4. Related Member Transactions. In any instance in which the professional service is sold to a related member, rather than applying the rule for professional services delivered to business customers in paragraph (c)1.e. of this subsection, the state or states to which the service is assigned is the place of receipt by the related member as reasonably approximated using the following hierarchy:

a. If the service primarily relates to specific operations or activities of a related member conducted in one (1) or more locations, then to the state or states in which those operations or ac-

tivities are conducted in proportion to the related member's payroll at the locations to which the service relates in the state or states; or

b. If the service does not relate primarily to operations or activities of a related member conducted in particular locations, but instead relates to the operations of the related member generally, then to the state or states in which the related member has employees, in proportion to the related member's payroll in those states. The taxpayer may use the safe harbor provided by this administrative regulation if the department may aggregate the receipts from sales to related members in applying the five (5) percent rule if necessary or appropriate to avoid distortion.

5. Broadcast Advertising Services. Notwithstanding anything contained in this administrative regulation to the contrary, receipts from a broadcaster's sale of advertising services to a broadcast customer are assigned to this state if the commercial domicile of the broadcast customer is in this state.

6. Examples. Unless otherwise stated, assume in each of these examples, if relevant, that the taxpayer is taxable in each state to which its receipts may be assigned, so that there is no requirement in the examples that the receipts shall be excluded from the denominator of the taxpayer's receipts factor. Assume that the customer is not a related member and that the safe harbor does not apply.

a. Example. Broker Corp provides securities brokerage services to individual customers who are resident in Kentucky and in other states. Assume that Broker Corp knows the state of primary residence for many of its customers, and if it does not know this state of primary residence, it knows the customer's billing address. Assume that Broker Corp does not derive more than five (5) percent of its receipts from sales of all services from any one (1) individual customer. If Broker Corp knows its customer's state of primary residence, it shall assign the receipts to that state. If Broker Corp does not know its customer's state of primary residence, but rather knows the customer's billing address, it shall assign the receipts to that state.

b. Example. Same facts as in Example a., except that Broker Corp has several individual customers from whom it derives, in each instance, more than five (5) percent of its receipts from sales of all services. Receipts from sales to customers from whom Broker Corp derives five (5) percent or less of its receipts from sales of all services shall be assigned as described in Example a.. For each customer from whom it derives more than five (5) percent of its receipts from sales of all services, Broker Corp shall determine the customer's state of primary residence and shall assign the receipts from the services provided to that customer to that state. In any case in which a five (5) percent customer's state of primary residence is Kentucky, receipts from a sale made to that customer shall be assigned to Kentucky. In any case in which a five (5) percent customer's state of primary residence is not Kentucky receipts from a sale made to that customer are not assigned to Kentucky. If receipts from a sale are assigned to a state other than Kentucky, if the state of assignment (i.e., the state of primary residence of the individual customer) is a state in which Broker Corp is not taxable, receipts from the sales shall be excluded from the denominator of Broker Corp's receipts factor.

c. Example. Architecture Corp provides building design services as to buildings located, or expected to be located, in Kentucky to individual customers who are resident in Kentucky and other states, and to business customers that are based in Kentucky and other states. The receipts from Architecture Corp's sales are assigned to Kentucky because the locations of the buildings to which its design services relate are in Kentucky, or are expected to be in Kentucky. 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 the 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 the services. Further, these receipts are

assigned to Kentucky even if Architecture Corp's designs are either physically delivered to its customer in paper form in a state other than Kentucky or are electronically delivered to its customer in a state other than Kentucky.

d. Example. Law Corp provides legal services to individual clients who are residents in Kentucky and in other states. In some cases, Law Corp may prepare one (1) or more legal documents for its client as a result of these services 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 if it does not know this state of primary residence, it knows the client's billing address. Assume that Law Corp does not derive more than five (5) percent of its receipts from sales of all services from any one (1) individual client. If Law Corp knows its client's state of primary residence, it shall assign the receipts to that state. If 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.

e. Example. Same facts as in Example d., except that Law Corp provides legal services to several individual clients who it knows have a primary residence in a state where Law Corp is not taxable. Receipts from these services are excluded from the denominator of Law Corp's receipts factor even if the billing address of one (1) or more of these clients is in a state in which Law Corp is taxable, including Kentucky.

f. Example. 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 (1) case, the agreement is principally managed in Kentucky; in the other cases, the agreement is principally managed in a state other than Kentucky. If the agreement for legal services is principally managed by the client in Kentucky the receipts from sale of the services are assigned to Kentucky; in the other cases, the receipts are not assigned to Kentucky. In the case of receipts that are assigned to Kentucky, the receipts are so assigned even if:

(i) The legal documents relating to the service are mailed or otherwise delivered to a location in another state; or

(ii) the litigation or other legal matter that is the underlying predicate for the services is in another state.

g. Example. Same facts as in Example f., except that Law Corp is not taxable in one (1) of the states other than Kentucky in which Law Corp's agreement for legal services that governs the client relationship is principally managed by the business client. Receipts from these latter services are excluded from the denominator of Law Corp's receipts factor.

h. Example. 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 Corp is principally managed by Law Corp in Kentucky, the receipts from the sale of Consulting Corp's services are assigned to Kentucky. 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.

i. Example. Bank Corp provides financial custodial services, including the safekeeping of some of its customers' financial assets, to 100 individual customers who are resident in Kentucky and in other states. Assume for purposes of this example that Bank Corp knows the

state of primary residence for many of its customers, and if it does not know the state of primary residence, it knows the customer's billing address. Assume that Bank Corp does not derive more than five (5) percent of its receipts from sales of all of its services from any single customer. Because Bank Corp does not have more than 250 customers, it may not apply the safe harbor for professional services stated in this subsection. If Bank Corp knows its customer's state of primary residence, it shall assign the receipts to that state. If Bank Corp does not know its customer's state of primary residence, but rather knows the customer's billing address, it shall assign the receipts to that state. Bank Corp's receipts are assigned to Kentucky if the customer's state of primary residence (or billing address, in cases when it does not know the customer's state of primary residence) is in Kentucky, even if Bank Corp's financial custodial work, including the safekeeping of the customer's financial assets, takes place in a state other than Kentucky.

j. Example. Same facts as Example i., except that Bank Corp has more than 250 customers, individual or business. Bank Corp may apply the safe harbor for professional services stated in paragraph (c)1.f. of this subsection, and may assign its receipts from sales to a state or states using each customer's billing address.

k. Example. Same facts as Example j., except that Bank Corp derives more than five (5) percent of its receipts from sales from a single individual customer. As to the sales made to this customer, Bank Corp shall determine the individual customer's state of primary residence and shall assign the receipts from the service or services provided to that customer to that state. Receipts from sales to all other customers are assigned as described in Example j..

l. Example. Advisor Corp, a corporation that provides investment advisory services, provides these advisory services to Investment Co. Investment Co is a multistate business client of Advisor Corp that uses Advisor Corp's services in connection with investment accounts that it manages for individual clients, who are the ultimate beneficiaries of Advisor Corp's services. Assume that Investment Co's individual clients are persons that are residents in numerous states, which may or may not include Kentucky. Assuming that Advisor Corp knows that its agreement with Investment Co is principally managed by Investment Co in Kentucky, receipts from the sale of Advisor Corp's services are assigned to Kentucky. It is not relevant for purposes of the analysis that the ultimate beneficiaries of Advisor Corp's services may be Investment Co's clients, who are residents of numerous states.

m. Example. Advisor Corp provides investment advisory services to Investment Fund LP, a partnership that invests in securities and other assets. Assuming that Advisor Corp knows that its agreement with Investment Fund LP is principally managed by Investment Fund LP in Kentucky, receipts from the sale of Advisor Corp's services are assigned to Kentucky. It is not relevant for purposes of the analysis that the partners in Investment Fund LP are residents of numerous states.

n. Example. Design Corp is a corporation based outside Kentucky that provides graphic design and similar services in Kentucky and in neighboring states. Design Corp enters into a contract at a location outside Kentucky 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 five (5) percent of its receipts from sales of services from the individual customer. All of the design work is performed outside Kentucky. Receipts from the sales are in Kentucky if the customer's billing address is in Kentucky.

(11) License or Lease of Intangible Property.

(a)1. The receipts from the license of intangible property are in this state if and to the extent the intangible is used in this state. "Use" is construed to refer to the location of the taxpayer's market for the use of the intangible property that is being licensed and is not to be construed to refer to the location of the property or payroll of the taxpayer. 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 in paragraphs(b)-(f) of this subsection. For purposes of the rules set forth in this subsection, a lease of intangible property is to be treated the same as a license of intangible property.

2. A license of intangible property that conveys all substantial rights in that property is treated as a sale of intangible property for purposes of this administrative regulation. For purposes of this subsection and subsection (12) of this section, a sale or exchange of intangible property is treated as a license of that property if the receipts from the sale or exchange derived from payments that are contingent on the productivity, use or disposition of the property.

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

4. In any instance in which the taxpayer is not taxable in the state to which the receipts from the license of intangible property are assigned, the receipts are excluded from the denominator of the taxpayer's receipts factor.

5. Nothing in this administrative regulation shall be construed to allow or require inclusion of receipts in the receipts factor that are not included in the definition of "receipts" pursuant to KRS 141.120(1)(e), or that are excluded from the numerator and the denominator of the receipts factor pursuant to KRS 141.120(11)(a)(4)(b)iii. To the extent that the transfer of either a security or business "goodwill" or similar intangible value, including, "going concern value" or "workforce in place," may be characterized as a license or lease of intangible property, receipts from the transaction shall be excluded from the numerator and the denominator of the taxpayer's receipts factor.

(b) License of a Marketing Intangible. If 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) to a consumer, the royalties or other licensing fees paid by the licensee for that marketing intangible are assigned to this state to the extent that those 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 this state. Examples of a license of a marketing intangible include 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, if a taxpayer has actual evidence of the amount or proportion of its receipts that is attributable to this state, it shall assign that amount or proportion to this state. In the absence of actual evidence of the amount or proportion of the licensee's receipts that are derived from consumers in this state, the portion of the licensing fee to be assigned to this state shall be reasonably approximated by multiplying the total fee by a percentage that reflects the ratio of the population of this state 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 that area. If 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 this state shall be reasonably approximated by multiplying the total fee by a percentage that reflects the ratio of the population of this state 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 that area. Unless the taxpayer demonstrates that the marketing intangible is materially used in the marketing of items outside the United States, the fees from licensing those marketing intangible shall be presumed to be derived from within the United States.

(c) License of a Production Intangible. If a license is granted for the right to use intangible property other than in connection with the sale, lease, license, or other marketing of goods, services, or other items, and the license is to be used in a production capacity (a "production intangible"), the licensing fees paid by the licensee for that right are assigned to this state to the extent that the use for which the fees are paid takes place in this state. Examples of a license of a production intangible include items such as the license of a patent, a copyright, or trade secrets to be used in a manufacturing process, if the value of the intangible lies predominately in its use in that process. In the case of a license of a production intangible to a member other than a related member if the location of actual use is unknown, it is 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). If the department may reasonably establish that the actual use of intangible property pursuant to a license of a production intangible takes place in part in this state, it is presumed that the entire use is in this state, except to the extent that the taxpayer may demonstrate that the actual location of a portion of the use takes place outside this state. In the case of a license of a production intangible to a related member, the taxpayer shall assign the receipts to where the intangible property is actually used.

(d) License of a Broadcasting Intangible. If a broadcaster grants a license to a broadcast customer for the right to use film programming, the licensing fees paid by the licensee for the right are assigned to this state to the extent that the broadcast customer is located in this state. In the case of business customers, the broadcast customer's location shall be determined using the broadcast customer's commercial domicile. In the case of individual customers, the broadcast customer's location shall be determined using the address of the broadcast customer listed in the broadcaster's records.

(e) License of a Mixed Intangible. If 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 department shall accept that separate statement for purposes of this administrative regulation. If 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 is presumed that the licensing fees are paid entirely for the license of the marketing intangible, except to the extent that the taxpayer or the department may reasonably establish otherwise.

(f) License of Intangible Property if Substance of Transaction Resembles a Sale of Goods or Services.

1. 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 these cases, the receipts from the licensing transaction are assigned by applying the rules set forth in subsection (9)(a) and (b) of this section, 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 subsection include transactions such as the license of database access, the license of access to information, the license of digital goods and the license of certain software (e.g., if the transaction is not the license of pre-written software that is treated as the sale of tangible personal property).

2. Sublicenses. Pursuant to this paragraph, the rules of subsection (9)(b) of this subsection may apply if a taxpayer licenses intangible property to a customer that in turn sublicenses the intangible property to end users as if the transaction were a service delivered electronically through a customer to end users. The rules set forth in subsection (9)(b) of this subsection 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 apply with respect to licenses of intangible property for purposes of sublicense to end users. For this purpose, 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 that 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 that property is bundled with additional services or items of property.

3. Examples. In these examples, unless otherwise stated, assume that the taxpayer is taxable in each state to which its receipts may be assigned so that there is no requirement in these examples that the receipts shall be eliminated from the denominator of the taxpayer's receipts factor. Assume that the customer is not a related member.

a. Example. Crayon Corp and Dealer Co enter into a license contract under which Dealer Co as licensee may 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 shall 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 may sell the products at multiple store locations, including store locations that are both within and without Kentucky. 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 Kentucky are determined by multiplying the fees by a percentage that reflects the ratio of Dealer Co's receipts that are derived from its Kentucky stores relative to Dealer Co's total receipts.

b. Example. Network Corp is a broadcaster that licenses rights to its film programming to both platform distribution companies and individual customers. Platform distribution companies pay licensing fees to Network Corp for the rights to distribute Network Corp's film programming to the platform distribution companies' customers. Network Corp's individual customers pay access fees to Network Corp for the right to directly access and view Network Corp's film programming. Network Corp's receipts from each platform distribution company shall be assigned to Kentucky if the broadcast customer's commercial domicile is in Kentucky. Network Corp's receipts from each individual broadcast customer shall be assigned to Kentucky if the address of the broadcast customer listed in the broadcaster's records is in Kentucky.

c. Example. Moniker Corp enters into a license contract with Wholesale Co. Pursuant to the contract, Wholesale Co may 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 shall 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 Kentucky receipts of Moniker Corp is determined by multiplying the amount of the fee by a percentage that reflects the ratio of the Kentucky population in the specific geographic region relative to the total population in that region. If Moniker Corp is able to reasonably establish that the marketing intangible was materially used throughout a foreign country, then the population of that country shall be included in the population ratio calculation. However, if Moniker Corp is unable to reasonably establish that the marketing intangible was materially used in the foreign country in areas outside a particular major city; then none of the foreign country's population

beyond the population of the major city is included in the population ratio calculation. If Moniker Corp is not taxable in any state (including a foreign country) in which Wholesale Co's ultimate consumers are located, the receipts that may be assigned to that state are excluded from the denominator of Moniker Corp's receipts factor.

d. Example. Formula, Inc and Appliance Co enter into a license contract under which Appliance Co may 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 other fees. The appliances are both manufactured and sold in Kentucky 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 department may reasonably establish that the actual use of the intangible property takes place in part in Kentucky, the royalty is assigned based to the location of that use rather than to location of the licensee's commercial domicile. It is presumed that the entire use is in Kentucky, except to the extent that the taxpayer may demonstrate that the actual location of some or all of the use takes place outside Kentucky. Assuming that Formula, Inc may demonstrate the percentage of manufacturing that takes place in Kentucky using the patent relative to the manufacturing in other states, that percentage of the total licensing fee paid to Formula, Inc under the contract shall constitute Formula, Inc's Kentucky receipts.

e. Example. Axel Corp enters into a license agreement with Biker Co in which Biker Co may produce motor scooters using patented technology owned by Axel Corp, and to sell the 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 Kentucky. Assume that Axel Corp lacks actual information regarding the proportion of Biker Co.'s receipts that are derived from Kentucky customers. Assume that Biker Co is granted the right to sell the scooters in a U.S. geographic region in which the Kentucky population constitutes twenty-five (25) percent 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 the department reasonably establishes otherwise. Assuming that neither member establishes otherwise, twenty-five (25) percent of the licensing fee constitutes Kentucky receipts.

f. Example. Same facts as Example e., 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 department shall:

- (i) Assign no part of the licensing fee paid for the production intangible to Kentucky; and
- (ii) Assign twenty-five (25) percent of the licensing fee paid for the marketing intangible to Kentucky.

g. Example. Better Burger Corp, which is based outside Kentucky, enters into franchise contracts with franchisees that agree to operate Better Burger restaurants as franchisees in various states. Several of the Better Burger Corp franchises are in Kentucky. In each case, the franchise contract between the individual and Better Burger provides that the franchisee is to

pay Better Burger Corp an upfront fee for the receipt of the franchise and monthly franchise fees, which cover, among other things, the right to use the Better Burger name and service marks, food processes and cooking know-how, as well as fees for management services. The upfront fees for the receipt of the Kentucky franchises constitute fees paid for the licensing of a marketing intangible. These fees constitute Kentucky receipts because the franchises are for the right to make Kentucky sales. The monthly franchise fees paid by Kentucky franchisees constitute fees paid for:

- (i) The license of marketing intangibles (the Better Burger name and service marks);
- (ii) The license of production intangibles (food processes and know-how); and
- (iii) Personal services (management fees). The fees paid for the license of the marketing intangibles and the production intangibles constitute Kentucky receipts because in each case the use of the intangibles is to take place in Kentucky. The fees paid for the personal services are to be assigned pursuant to this section.

h. Example. Online Corp, a corporation based outside Kentucky, licenses an information database through the means of the Internet to individual customers that are resident in Kentucky and in other states. These customers access Online Corp's information database primarily in their states of residence, and sometimes, while traveling, in other states. The license is a license of intangible property that resembles a sale of goods or services and are assigned in accordance with this paragraph. If Online Corp may determine or reasonably approximate the state or states where its database is accessed, it shall do so. Assuming that Online Corp cannot determine or reasonably approximate the location where its database is accessed, Online Corp shall 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. Online Corp's receipts from sales made to its individual customers are in Kentucky in any case in which the customer's billing address is in Kentucky.

i. Example. Net Corp, a corporation based outside Kentucky, licenses an information database through the means of the Internet to a business customer, Business Corp, a company with offices in Kentucky and two (2) neighboring states. The license is a license of intangible property that resembles a sale of goods or services and are assigned in accordance with this paragraph. Assume that Net Corp cannot determine where its database is accessed, but reasonably approximates that seventy-five (75) percent of Business Corp's database access took place in Kentucky, and twenty-five (25) percent of Business Corp's database access took place in other states. In that case, seventy-five (75) percent of the receipts from database access is in Kentucky. Assume alternatively that Net Corp lacks sufficient information regarding the location where its database is accessed to reasonably approximate the location. Under these circumstances, if Net Corp derives five (5) percent or less of its receipts from database access from Business Corp, Net Corp shall assign the receipts under subsection(9)(b) of this section 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 five (5) percent of its receipts from database access from Business Corp, Net Corp shall identify the state in which its contract of sale is principally managed by Business Corp and shall assign the receipts to that state.

j. Example. Net Corp, a corporation based outside Kentucky, licenses an information database through the means of the Internet to more than 250 individual and business customers in Kentucky and in other states. The license is a license of intangible property that resembles a sale of goods or services and receipts from that license are assigned in accordance with this paragraph. Assume that Net Corp cannot determine or reasonably approximate the location

where its information database is accessed. Assume that Net Corp does not derive more than five (5) percent of its receipts from sales of database access from any single customer. Net Corp may apply the safe harbor stated in subsection(9)(a)2.d. of this section, and may assign its receipts to a state or states using each customer's billing address. If Net Corp is not taxable in one (1) or more states to which some of its receipts may be otherwise assigned, it shall exclude those receipts from the denominator of its receipts factor.

k. Example. Web Corp, a corporation based outside of Kentucky, licenses an Internet-based information database to business customers who then sublicense the database to individual end users that are resident in Kentucky and in other states. These end users access Web Corp's information database primarily in their states of residence, and sometimes, while traveling, in other states. Web Corp's license of the database to its customers includes the right to sublicense the database to end users, while the sublicenses provide that the rights to access and use the database are limited to the end users' own use and prohibit the individual end users from further sublicensing the database. Web Corp receives a fee from each customer based upon the number of sublicenses issued to end users. The license is a license of intangible property that resembles a sale of goods or services and are assigned by applying the rules set forth in subsection(9)(b) of this section. If Web Corp may determine or reasonably approximate the state or states where its database is accessed by end users, it shall do so. Assuming that Web Corp lacks sufficient information from which it may determine or reasonably approximate the location where its database is accessed by end users, Web Corp shall approximate the extent to which its database is accessed in Kentucky using a percentage that represents the ratio of the Kentucky population in the specific geographic area in which Web Corp's customer sublicenses the database access relative to the total population in that area.

(12) Sale of Intangible Property.

(a) Assignment of Receipts. The assignment of receipts 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 subsection, a sale or exchange of intangible property includes a license of that property if the transaction is treated for tax purposes as a sale of all substantial rights in the property and the receipts from transaction are not contingent on the productivity, use or disposition of the property. For the rules that apply if the consideration for the transfer of rights is contingent on the productivity, use or disposition of the property, see KRS 141.120(11)(a)(4)(b)ii.

1. Contract Right or Government License that Authorizes Business Activity in Specific Geographic Area. In the case of a sale or exchange of intangible property if 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 may be used within the state. If the intangible property is used or may be used only in Kentucky, the taxpayer shall assign the receipts from the sale to this state. If the intangible property is used or may be used in this state and one (1) or more other states, the taxpayer shall assign the receipts from the sale to this state to the extent that the intangible property is used in or authorized for use in this state, through the means of a reasonable approximation.

2. 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 if the receipts from the sale or exchange are contingent on the productivity, use or disposition of the property, the receipts from the sale are assigned by applying the rules set forth in subsection (11) of this section (pertaining to the license or lease of intangible property).

3. Sale that Resembles a Sale of Goods and Services. In the case of a sale or exchange of intangible property if the substance of the transaction resembles a sale of goods or services

and if 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 are assigned by applying the rules set forth in subsection (11)(f) of this section (relating to licenses of intangible property that resemble sales of goods and services). Examples of these transactions include those that are analogous to the license transactions cited as examples in subsection (11)(f)3. of this section.

4. Excluded Receipts. Receipts from the sale of intangible property are not included in the receipts factor in any case in which the sale does not give rise to receipts within the meaning of KRS 141.120(1)(e). In addition, pursuant to KRS 141.120(11)(a)(4)(b)(iii), receipts from the sale of intangible property are excluded from the numerator and the denominator of the taxpayer's receipts factor if the receipts are not referenced in KRS 141.120(11)(a)(4)(b)(i) or KRS 141.120(11)(a)(4)(b)(ii). The sale of intangible property that is excluded from the numerator and denominator of the taxpayer's receipts factor under KRS 141.120(11)(a)(4)(b)(iii) includes the sale of a partnership interest, the sale of business "goodwill," the sale of an agreement not to compete, or similar intangible value. In any instance in which, the state to which the receipts from a sale is to be assigned may be determined or reasonably approximated, but if the taxpayer is not taxable in the state, the receipts that may be assigned to the state shall be excluded from the denominator of the taxpayer's receipts factor.

5. Examples. In these examples, unless otherwise stated, assume that the taxpayer is taxable in each state to which some of its receipts may be assigned, so that there is no requirement in these examples that the receipts to other states shall be excluded from the taxpayer's denominator pursuant to subsection (11)(a) of this section and KRS 141.120(11)(c).

a. Example. Airline Corp, a corporation based outside Kentucky, sells its rights to use several gates at an airport located in Kentucky to Buyer Corp, a corporation that is based outside Kentucky. The contract of sale is negotiated and signed outside of Kentucky. The receipts from the sale are in Kentucky because the intangible property sold is a contract right that authorizes the holder to conduct a business activity solely in Kentucky.

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

c. Example. Same facts as in Example b., except that Wireless Corp sells to Buyer Corp an FCC license to operate wireless telecommunications services in a designated area in Kentucky and an adjacent state. Wireless Corp shall attempt to reasonably approximate the extent to which the intangible property is used in or may be used in Kentucky. For purposes of making this reasonable approximation, Wireless Corp may rely upon credible data that identifies the percentage of persons that use wireless telecommunications in the two (2) states covered by the license.

d. Example. Same facts as in Example c., except that Wireless Corp is not taxable in the adjacent state in which the FCC license authorizes it to operate wireless telecommunications services. The receipts paid to Wireless Corp that may be assigned to the adjacent state shall be excluded from the denominator of Wireless Corp's receipts factor.

e. Example. Sports League Corp, a corporation that is based outside Kentucky, sells the rights to broadcast the sporting events played by the teams in its league in all fifty (50) U.S. states to Network Corp. Although the games played by Sports League Corp will be broadcast in all fifty (50) states, the games are of greater interest in the southeast region of the country, including Kentucky. 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 shall attempt to reasonably approximate the extent to which the intangible property is used in or may be used in Kentucky. 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 Kentucky and the other states.

f. Example. Same facts as in Example e., except that Sports League Corp is not taxable in one (1) state. The receipts paid to Sports League Corp that may be assigned to that state shall be excluded from the denominator of Sports League Corp's receipts factor.

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

(13) Special Rules.

(a) Software Transactions. A license or sale of pre-written software for purposes other than commercial reproduction (or other exploitation of the intellectual property rights) 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 these cases, the receipts are in this state as determined under the rules for the sale of tangible personal property set forth under KRS 141.120(10) and related administrative regulations. In all other cases, the receipts from a license or sale of software are to be assigned to this state as determined otherwise under this administrative regulation. (e.g., depending on the facts, as the development and sale of custom software, see subsection (8) of this section, as a license of a marketing intangible, see subsection (11)(b) of this section, as a license of a production intangible, see subsection (11)(c) of this section, as a license of intangible property if the substance of the transaction resembles a sale of goods or services, see subsection (11)(f) of this section, or as a sale of intangible property, see subsection (12) of this section.

(b) Sales or Licenses of Digital Goods or Services.

1. In the case of a sale or license of digital goods or services, including, among other things, the sale of various video, audio, and software products, or similar transactions, the receipts from the sale or license are assigned by applying the same rules as are set forth in subsection (9)(a) and (b) or subsection 10(c)5. of this section, 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.

2. Providers of communication services, cable service, and Internet access. Providers shall apportion income to this state using a three (3) factor formula as provided in KRS 141.901 pursuant to KRS 141.121(3).

Section 6. Special Rules: Receipts Factor. The following special rules are established in respect to the receipts factor of the apportionment formula:

(1) Bank holding company. For any corporation or other business entity registered under state law as a bank holding company or registered under 12 U.S.C. 1841, et. seq., the Federal

Bank Holding Company Act of 1956, as amended, or registered as a savings and loan holding company under 12 U.S.C. 1701 to 1750, the Federal National Housing Act, as amended, and any entity more than fifty (50) percent owned, directly or indirectly, by these holding companies, receipts are included in the receipts factor denominator and assigned to the receipts factor numerator in this state to the extent those receipts may be included in the denominator and assigned to this state under KRS 136.530.

(2) Bargeline. Bargelines shall determine receipts in this state by multiplying total transportation revenues by a fraction, the numerator of which is miles operated in this state and the denominator of which is total miles operated for the taxable year. Miles operated in this state shall be fifty (50) percent of the miles operated on the Ohio River, the Big Sandy River, and the Mississippi River adjacent to this state's shoreline plus all miles operated on other inland waterways within this state.

(3) Busline. Buslines shall determine receipts in this state by multiplying total transportation revenues by a fraction, the numerator of which is miles operated in this state and the denominator of which is total miles operated for the taxable year.

(4) Passenger airline. Pursuant to KRS 141.121(2)(b)(1), passenger airlines shall determine receipts in this state by multiplying total transportation revenues by a fraction, the numerator of which is Kentucky revenue passenger miles in this state and the denominator of which is total revenue passenger miles for the taxable year.

(5) Pipeline. Pipeline companies shall determine receipts in this state by multiplying total operating revenues by a fraction, the numerator of which is barrel miles transported in this state and the denominator of which is total barrel miles transported for the taxable year.

(6) Public service company. Public service companies shall allocate and apportion net income in accordance with KRS 141.121(5).

(7) Qualified air freight forwarder. Pursuant to KRS 141.121(2)(b)(2), qualified air freight forwarders shall determine receipts in this state by multiplying total freight forwarding revenues by a fraction, the numerator of which is miles operated in this state and the denominator of which is total miles operated by the affiliated airline for the taxable year.

(8) Railroad. Railroads shall determine receipts in this state by multiplying total transportation revenues by a fraction, the numerator of which is revenue car miles in this state and the denominator of which is total revenue car miles for the taxable year.

(9) Regulated investment company. Regulated investment companies shall apportion income pursuant to KRS 141.120 and this administrative regulation; except that a regulated investment company may elect an alternative method for determining receipts pursuant to KRS 141.121(4)(b).

(10) Securities brokerage services. Securities brokers operating within certain Kentucky Enterprises Zones defined by KRS 141.121(4)(c), shall apportion income pursuant to KRS 141.120 and this administrative regulation, except that a securities broker so defined may elect an alternative method for determining receipts pursuant to KRS 141.121(4)(c).

(11) Truckline. Trucklines shall determine receipts in this state by multiplying total transportation revenues by a fraction, the numerator of which is miles operated in this state and the denominator of which is total miles operated for the taxable year.

Section 7. This administrative regulation shall apply to tax periods beginning on or after January 1, 2018. (32 Ky.R. 1830; 2290; 33 Ky.R. 71; eff. 8-7-2006; 45 Ky.R. 1708, 2688, 2845; eff. 5-3-2019.)