103 KAR 16:290. Apportionment; property factor.

RELATES TO: KRS 141.120(12)(a)2., 141.121, 141.901
STATUTORY AUTHORITY: KRS 131.130, 141.120(12)(a)2., 141.121, 141.901
NECESSITY, FUNCTION, AND CONFORMITY: KRS 141.121 and 141.901 require business or apportionable income of multistate corporations to be apportioned to Kentucky by multiplying the income by a fractionKRS 131.130(1) authorizes the department to promulgate administrative regulations to administer and enforce Kentucky's tax laws. This administrative regulation establishes the requirements for determining the property factor of a multistate corporation.

Section 1. Definitions.
(1) "Annual rent" means the actual sum of money or other consideration payable, directly or indirectly, by the corporation for its benefit for the use of the property;
(a) Including:
1. Any amount payable for the use of real or tangible personal property whether designated as a fixed sum of money or as a percentage of sales, profits or otherwise; and
2. Any amount payable as additional rent or in lieu of rents, such as interest, taxes, insurance, repairs or any other items which are required to be paid by the terms of the lease or other arrangement; and
(b) Not including:
1. Amounts paid as service charges, such as utilities or janitorial services; and
2. Incidental day-to-day expenses such as hotel or motel accommodations, or daily rental of automobiles.
(2) "Net annual rental rate" means the total annual rental paid, less total annual rental received from subrentals, which shall:
(a) Be subtracted if they constitute nonbusiness or non-apportionable income; and
(b) Not be subtracted if they constitute business or apportionable income because the property which produces the subrentals is used in the regular course of a trade or business of the taxpayer when it is producing business or apportionable income.
(3) "Original cost" means the basis of the property for federal income tax purposes, prior to any federal adjustments, at the time of acquisition by the corporation and adjusted by subsequent capital additions or improvements thereto and partial disposition thereof, by reason of sale, exchange, or abandonment.

Section 2. General. The property factor shall include all real and tangible personal property owned or rented and used during the taxable year, except coin, and currency.

Section 3. Property Used.
(1) Property shall be included in the property factor if it is actually used or is available for or capable of being used during the taxable year. Property held as reserves or standby facilities or property held as a reserve source of materials shall be included in the factor. For example, a plant temporarily idle or raw material reserves not currently being processed shall be included in the factor.
(2) Inventory in process shall be included in the factor. Property or equipment under construction during the taxable year shall be excluded from the factor until it is actually used or is available for or capable of being used during the taxable year.
(3) Property used shall remain in the property factor until its permanent withdrawal is established by an identifiable event such as its sale.

Section 4. Consistency in Reporting.

(1) Year-to-year consistency. In filing returns with this state, if the taxpayer departs from or modifies the manner of valuing property or of excluding property from or including property in the property 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 valuation of property and in the exclusion of property from or the inclusion of property in the property factor, the taxpayer shall disclose in its return to this state the nature and extent of the variance.

Section 5. Property Factor: Numerator.

(1) Property in transit between a buyer and seller shall be included in the numerator according to the state of destination. Property in transit between locations of the same corporation shall be considered at the destination location for purposes of the property factor.

(2) The value of mobile or movable property such as construction equipment, trucks or leased electronic equipment which is located within and without Kentucky during the taxable year shall be determined, for purposes of the numerator of the factor, on the basis of total time within the state during the taxable year. An automobile assigned to a traveling employee shall be included in the numerator of the factor of the state to which the employee’s compensation is assigned under the payroll factor or in the numerator of the state in which the automobile is licensed.

Section 6. Valuation of Owned Property.

(1) Property owned by the corporation shall be valued at original cost.

(2) Capitalized intangible drilling and development costs shall be included in the property factor whether or not they have been expensed for either federal or state purposes.

(3) If the original cost of property is not ascertainable, is nominal, or is zero, the property shall be included in the factor at its fair market value at the date of acquisition by the corporation.

(4) Inventory shall be included in the factor by the valuation method used for federal income tax purposes.

(5) Property acquired by gift or inheritance shall be included in the factor at its basis for depreciation for federal income tax purposes.

Section 7. Rented Property.

(1) Annual rental rate shall be determined as follows:

(a) If the property is rented for a twelve (12) month period, the annual rental payment;

(b) If the property is rented for less than a twelve (12) month period, the net rent paid for the actual period of rental; or

(c) If the property is rented for a period of twelve (12) or more months, and the current tax period covers a period of less than twelve (12) months due, for example, to a reorganization or change of accounting period, the net rent paid for the short tax period shall be annualized.

(2)(a) Property rented by a corporation shall be valued at eight (8) times the net annual rental rate.

(b) If this calculation results in a negative value or a clearly inaccurate valuation, any other method which will properly reflect the value may be required by the department or may be requested by the corporation, except the net annual rental rate shall not be less than the total annual rental rate multiplied by a fraction, the numerator of which is the fair market value of rent applicable to rental property used by the corporation divided by the fair market value of rent applicable to all of the corporation’s rental property.

(c) If a payment includes rent and other charges unsegregated, the amount of rent shall be determined by consideration of the relative values of the rent and the other items.

(3) If property is used at no charge or rented for a nominal rate, the property shall be included in the property factor on the basis of the fair market value of rent for comparable property in the area.

(4) Leasehold improvements shall, for the purposes of the property factor, be treated as property owned by the corporation regardless of whether the corporation is entitled to remove the improvements or the improvements revert to the lessor upon expiration of the lease. The original cost of a leasehold improvement shall be included in the factor.

Section 8. Monthly Averaging of Property. Averaging by monthly values shall apply if:

(1) Fluctuations in the values of the property exist during the tax period;

(2) Property is acquired after the beginning of the tax period or disposed of before the end of the tax period; or

(3) Fluctuations in the percentage of property used in Kentucky exist during the tax period.

Section 9. This administrative regulation shall be effective for tax periods beginning on or after January 1, 2005. (32 Ky.R. 1831; Am. 33 Ky.R. 72; eff. 8-7-2006; 1108; 1519; eff. 1-5-2007; 45 Ky.R. 1312, 2063; eff. 2-1-2019.)