



Guidelines for Computing the Sales Factor Based on Market-Based Sourcing

I. Sales Other Than Sales of Tangible Personal Property in North Carolina: General Rules.

In general, these guidelines provide for the inclusion in the numerator of the sales factor of gross receipts arising from transactions other than sales of tangible personal property.

(1) Market-Based Sourcing.

Receipts, other than receipts from sales of tangible personal property are in North Carolina if and to the extent that the taxpayer's market for the sales is in North Carolina. In general, the provisions in these guidelines establish uniform rules for (1) determining whether and to what extent the market for a sale other than the sale of tangible personal property is in North Carolina, (2) reasonably approximating the state or states of assignment where the state or states cannot be determined, (3) excluding receipts from the sale of intangible property from the numerator and denominator of the sales factor pursuant to the Market-Based Sourcing Principles set out in subdivision 1.e. of Session Law 2015-268, section 32.14A.(b) and restated in the Introduction and Summary to these guidelines, and (4) excluding receipts from the denominator of the sales factor where the state or states of assignment cannot be determined or reasonably approximated.

(2) Outline of topics.

The provisions in these guidelines are organized as follows:

	Page
I. General Rules	1
(1) Market-Based Sourcing	1
(2) Outline of Topics	1
(3) Definitions	2
(4) General Principles of Application; Contemporaneous Records	4
(5) Rules of Reasonable Approximation	4

(6) Rules with respect to Exclusion of Receipts from the Sales Factor	5
II. Sale, Rental, Lease or License of Real Property	6
III. Rental, Lease or License of Tangible Personal Property	6
IV. Sale of a Service	6
(1) General Rule	6
(2) In-Person Services	7
(3) Services Delivered to the Customer or on Behalf of the Customer, or Delivered Electronically Through the Customer	9
(4) Professional Services	22
V. License or Lease of Intangible Property	30
(1) General Rules	30
(2) License of a Marketing Intangible	30
(3) License of a Production Intangible	31
(4) License of a Mixed Intangible	32
(5) License of Intangible Property where Substance of the Transaction Resembles a Sale of Goods or Services	32
VI. Sale of Intangible Property	39
(1) Assignment of Receipts	39
VII. Special Rules	42
(1) Software Transactions	42
(2) Sales or Licenses of Digital Goods and Services	42
(3) Financial Institutions	43

(3) Definitions.

For the purposes of these guidelines, except as otherwise provided in VII.(3), these terms have the following meanings:

- (A) “Billing address” means the location indicated in the books and records of the taxpayer as the primary mailing address relating to a customer’s account as of the time of the transaction as kept in good faith in the normal course of business and not for tax avoidance purposes.

- (B) "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 must be assigned consistent with the rules for those sales.
- (C) "Code" means the Internal Revenue Code as currently written and subsequently amended.
- (D) "Department" means the North Carolina Department of Revenue.
- (E) "Individual customer" means a customer that is not a business customer.
- (F) "Intangible property" generally means property that is not physical or whose representation by physical means is merely incidental and includes, without limitation, copyrights; patents; trademarks; trade names; brand names; franchises; licenses; trade secrets; trade dress; information; know-how; methods; programs; procedures; systems; formulae; processes; technical data; designs; licenses; literary, musical, or artistic compositions; information; ideas; contract rights including broadcast rights; agreements not to compete; goodwill and going concern value; securities; and, except as otherwise provided in these guidelines, computer software. Receipts from the sale of intangible property may be excluded from the numerator and denominator of the taxpayer's sales factor pursuant to section VI.(1)(D) of these guidelines.
- (G) "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.
- (H) "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.
- (I) "Related entity". – Defined in N.C. Gen. Stat. 105-130.7A.
- (J) "Secretary" means the Secretary of Revenue.
- (K) "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.

(4) General Principles of Application; Contemporaneous Records.

A taxpayer's assignment of receipts from sales of other than tangible personal property must be consistent with the following principles:

(A) A taxpayer shall apply the rules set forth in these guidelines based on objective criteria and shall consider all sources of information reasonably available to the taxpayer at the time of its informational report filing including, without limitation, the taxpayer's books and records kept in the normal course of business. A taxpayer shall determine its method of assigning receipts in good faith, and apply it consistently with respect to similar transactions. 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) These guidelines provide various assignment rules that apply sequentially in a hierarchy. For each sale to which a hierarchical rule applies, a taxpayer must make a reasonable effort to apply the primary rule applicable to the sale before seeking to apply the next rule in the hierarchy (and must continue to do so with each succeeding rule in the hierarchy, where applicable). For example, in some cases, the applicable rule first requires a taxpayer to determine the state or states of assignment, and if the taxpayer cannot do so, the rule requires the taxpayer to reasonably approximate the state or states. In these cases, the taxpayer must 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, where applicable, must reflect an attempt to obtain the most accurate assignment of receipts consistent with the standards set forth in these guidelines, rather than an attempt to lower the taxpayer's tax liability. A method of assignment that is reasonable for one taxpayer may not necessarily be reasonable for another taxpayer, depending upon the applicable facts.

(5) Rules of Reasonable Approximation.

(A) In General. In general, these guidelines establish uniform rules for determining whether and to what extent the market for a sale other than the sale of tangible personal property is in North Carolina. The guidelines also set forth rules of reasonable approximation, which apply if

the state or states of assignment cannot be determined. In some instances, the reasonable approximation must be made in accordance with specific rules of approximation prescribed in these guidelines. In other cases, the applicable rule in these guidelines permits a taxpayer to reasonably approximate the state or states of assignment, using a method that reflects an effort to approximate the results that would be obtained under the applicable rules or standards set forth in these guidelines.

(B) Approximation Based Upon Known Sales. In an instance where, applying the applicable rules set forth in Section IV of these guidelines (Sale of a Service), a taxpayer can ascertain the state or states of assignment of a substantial portion of its receipts from sales of substantially similar services (“assigned receipts”), but not all of those sales, and 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 sales factor in the same proportion as its assigned receipts. This rule also applies in the context of licenses and sales of intangible property where the substance of the transaction resembles a sale of goods or services. See Section V.(5) and VI.(1)(C).

(C) Related-Entity Transactions – Information Imputed from Customer to Taxpayer. Where a taxpayer has receipts subject to these guidelines from transactions with a related-entity customer, information that the customer has that is relevant to the sourcing of receipts from these transactions is imputed to the taxpayer.

(6) Rules with Respect to Exclusion of Receipts from the Sales Factor

(A) The sales factor only includes those gross receipts of the taxpayer that are not allocated under G.S. 105-130.4, and that are received from transactions and activity in the regular course of the taxpayer’s trade or business; except that receipts of a taxpayer from a casual sale of property, receipts exempt from taxation, and the portion of receipts realized from the sale or maturity of securities or other obligations that represent a return of principal, shall be excluded.

(B) Certain receipts arising from the sale of intangibles are excluded from the numerator and denominator of the sales factor pursuant to the Market-Based Sourcing Principles set out in subdivision 1.e. of Session Law 2015-268, section 32.14A.(b) and restated in the Introduction and Summary to these guidelines. See Section VI(1)(D).

(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 these guidelines (including through the use of a method of reasonable approximation, where relevant) using a reasonable amount of effort undertaken in good faith, the receipts must be excluded from the denominator of the taxpayer's sales factor pursuant to these guidelines.

II. 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 North Carolina if and to the extent that the property is in North Carolina.

III. 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 North Carolina if and to the extent that the property is in North Carolina. If property is mobile property that is located both within and without North Carolina during the period of the lease or other contract, the receipts assigned to North Carolina are determined on the basis of total time within the State during the income 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.

IV. Sale of a Service.

(1) General Rule.

The receipts from a sale of a service are in North Carolina if and to the extent that the service is delivered to a location in North Carolina. In general, the term "delivered to a location" refers to the location of the taxpayer's market for the service, which may not be the location of the taxpayer's employees or property. 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 Section IV.(2)-(4).

(2) In-Person Services.

(A) In General.

Except as otherwise provided in this section, in-person services are services that are physically provided in person by the taxpayer, where the customer or the customer's real or tangible property upon which the services are performed is in the same location as the service provider at the time the services are performed. This rule includes situations where the services are provided on behalf of the taxpayer by a third-party contractor. Examples of in-person services include, without limitation, warranty and repair services; cleaning services; plumbing services; carpentry; construction contractor services; pest control; landscape services; medical and dental services, including medical testing, x-rays and mental health care and treatment; child care; hair cutting and salon services; live entertainment and athletic performances; and in-person training or lessons. In-person services include services within the description above that are performed at (1) a location that is owned or operated by the service provider or (2) a location of the customer, including the location of the customer's real or tangible personal property. Various professional services, including legal, accounting, financial and consulting services, and other similar services as described in Section IV.(4), although they may involve some amount of in-person contact, are not treated as in-person services within the meaning of this section.

(B) Assignment of Receipts.

Rule of Determination. Except as otherwise provided in this section, 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 North Carolina if and to the extent the customer receives the in-person service in North Carolina. In assigning its receipts from sales of in-person services, a taxpayer must first attempt to determine the location where a service is received, as follows:

1. If the service is performed with respect to the body of an individual customer in North Carolina (e.g. hair cutting or x-ray services) or in the physical presence of the customer in North Carolina (e.g. live entertainment or athletic performances), the service is received in North Carolina.
2. If the service is performed with respect to the customer's real estate in North Carolina 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 North Carolina, the service is received in North Carolina.

3. 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 North Carolina, the service is received in North Carolina if the property is shipped or delivered to the customer in North Carolina.

(C) Rule of Reasonable Approximation.

In an instance in which 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 can reasonably approximate the state or states where the service is received, the taxpayer shall reasonably approximate such state or states.

(D) Examples.

Note that 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.

Example (i). Salon Corp has retail locations in North Carolina 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 North Carolina locations are North Carolina sales. The receipts from sales of services provided at Salon Corp's locations outside North Carolina, even when provided to residents of North Carolina, are not North Carolina sales.

Example (ii). Landscape Corp provides landscaping and gardening services in North Carolina and in neighboring states. Landscape Corp provides landscaping services at the North Carolina vacation home of an individual who is a resident of another state and who is located outside North Carolina at the time the services are performed. The receipts from the sale of services provided at the North Carolina location are North Carolina sales.

Example (iii). Same facts as in Example (ii), 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 North Carolina and in other states. The receipts from the sale of services provided to Retail Corp are in North Carolina to the extent the services are provided in North Carolina.

Example (iv). Camera Corp provides camera repair services at a North Carolina retail location to walk-in individual and business customers. In some cases, Camera Corp actually repairs a camera that is brought to its North Carolina 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 in-state location. The receipts from sale of these services are in North Carolina.

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

Example (vi). Teaching Corp provides seminars in North Carolina to individual and business customers. The seminars and the materials used in connection with the seminars are prepared outside the state, the teachers who teach the seminars include teachers that are resident outside North Carolina, and the students who attend the seminars include students that are resident outside North Carolina. Because the seminars are taught in North Carolina the receipts from sales of the services are in North Carolina.

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

(A) In General.

If the service provided by the taxpayer is not an in-person service within the meaning of Section IV.(2) or a professional service within the meaning of Section IV.(4), 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 North Carolina if and to the extent that the service is delivered in North Carolina. For purposes 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 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 can 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 section, a service delivered by an electronic transmission is not a delivery by a physical means). If a rule of assignment set forth in this section 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.

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, product delivery services where property is delivered to the customer or to a third party on behalf of the customer; the delivery of brochures, fliers or other direct mail services; the delivery of advertising or advertising-related services to the customer's intended audience in the form of a physical medium; and the sale of custom software (e.g., where software is developed for a specific customer in a case where the transaction is properly treated as a service transaction for purposes of corporate taxation) where the taxpayer installs the custom software at the customer's site. The rules in these guidelines, Section IV.(3)(B)1, apply whether the taxpayer's customer is an individual customer or a business customer.
 - a. 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 must 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.
 - b. 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 can reasonably approximate the state or states where the service is delivered, it shall reasonably approximate the state or states.

c. Examples:

Example (i). Direct Mail Corp, a corporation based outside North Carolina, provides direct mail services to its customer, Business Corp. Business Corp transacts with Direct Mail Corp to deliver printed fliers to a list of customers that is provided to it by Business Corp. Some of Business Corp's customers are in North Carolina 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 North Carolina to the extent that the services are delivered on behalf of Business Corp to North Carolina customers (i.e., to the extent that the fliers are delivered on behalf of Business Corp to Business Corp's intended audience in North Carolina).

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

Example (iii). Same facts as example (ii), except that the contract is with a business customer that is based outside North Carolina. The receipts from the sale of the design services are in North Carolina because the services are physically delivered on behalf of the customer to the customer's intended audience in North Carolina.

Example (iv). Fulfillment Corp, a corporation based outside North Carolina, provides product delivery fulfillment services in North Carolina and in neighboring states to Sales Corp, a corporation located outside North Carolina that sells tangible personal property through a mail order catalog and over the Internet to customers. In some cases when a

customer purchases tangible personal property from Sales Corp to be delivered in North Carolina, Fulfillment Corp will, pursuant to its contract with Sales Corp, deliver that property from its fulfillment warehouse located outside North Carolina. The receipts from the sale of the fulfillment services of Fulfillment Corp to Sales Corp are assigned to North Carolina to the extent that Fulfillment Corp's deliveries on behalf of Sales Corp are to recipients in North Carolina.

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

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

2. Delivery to a Customer by Electronic Transmission. Services delivered by electronic transmission include, without limitation, services that are transmitted through the means of wire, lines, cable, fiber optics, electronic signals, satellite transmission, audio or radio waves, or other similar means, whether or not the service provider owns, leases or otherwise controls the transmission equipment. In the case of the delivery of a service by electronic transmission to a customer, the following rules apply.
 - a. Services Delivered By Electronic Transmission to an Individual Customer.
 - i. Rule of Determination. In the case of the delivery of a service to an individual customer by electronic transmission, the service is delivered in North Carolina if and to the extent that the taxpayer's customer receives the service in North Carolina. If

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

- ii. 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 can reasonably approximate the state or states where the service is received, it shall reasonably approximate the state or states. If a taxpayer does not have sufficient information from which it can 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.

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

- i. Rule of Determination. In the case of the delivery of a service to a business customer by electronic transmission, the service is delivered in North Carolina if and to the extent that the taxpayer's customer receives the service in North Carolina. If the taxpayer can 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 this section, it is intended that the state or states where the service is received reflect the location at which the service is directly used by the employees or designees of the customer.
- ii. Rule of Reasonable Approximation. If the taxpayer cannot determine the state or states where the customer actually receives the service, but has sufficient information regarding the place of receipt from which it can reasonably approximate the state or states where the service is received, it shall reasonably approximate the state or states.
- iii. Secondary Rule of Reasonable Approximation. In the case of the delivery of a service to a business customer by electronic transmission where a taxpayer does not have sufficient information from which it can determine or reasonably approximate the state or states in which the service is received, the taxpayer shall reasonably approximate the state or states as set forth in this regulation. In these cases, unless the taxpayer can apply the safe harbor set forth in Section IV.(3)(B)2.b.iv, the taxpayer shall reasonably approximate the state or states in which the service is received as follows: first, by assigning the receipts from the sale to the state where

the contract of sale is principally managed by the customer; second, if the state where the customer principally manages the contract is not reasonably determinable, by assigning the receipts from the sale to the customer's place of order; and third, if the customer's place of order is not reasonably determinable, by assigning the receipts from the sale using the customer's billing address; provided, however, if the taxpayer derives more than 5% of its receipts from sales of services from any single customer, the taxpayer is required to identify the state in which the contract of sale is principally managed by that customer.

- iv. **Safe Harbor.** In the case of the delivery of a service to a business customer by electronic transmission, a taxpayer may not be able to determine, or reasonably approximate under Section IV.(3)(B)2.b.ii, the state or states in which the service is received. In these cases, the taxpayer may, in lieu of the rule stated at Section IV.(3)(B)2.b.iii, apply the safe harbor stated in this subsection. 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 (1) engages in substantially similar service transactions with more than 250 customers, whether business or individual, and (2) does not derive more than 5% of its receipts from sales of all services from that customer. This safe harbor applies only for purposes of services delivered by electronic transmission to a business customer, and not otherwise.
- v. **Related Entity Transactions.** In the case of a sale of a service by electronic transmission to a business customer that is a related entity, the taxpayer may not use the secondary rule of reasonable approximation in Section IV.(3)(B)2.b.iii but may use the rule of reasonable approximation in Section IV.(3)(B)2.b.ii, and the safe harbor in Section IV.(3)(B)2.b.iv, provided that the Secretary may aggregate sales to related parties in determining whether the sales exceed 5% of receipts from sales of all services under that safe harbor provision if necessary or appropriate to prevent distortion.

c. **Examples:**

In these examples, unless otherwise stated, assume that the taxpayer is not related to the customer to which the service is delivered. Also, assume if relevant, unless otherwise stated, that the safe harbor set forth at Section IV.(3)(B)2.b.iv does not apply.

Example (i). Support Corp, a corporation that is based outside North Carolina, 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 North Carolina and other states. Support Corp supplies its services on a case by case basis when directly contacted by its customer. Support Corp generally provides these services through the Internet but sometimes provides these services by phone. In all cases, Support Corp verifies the customer's account information before providing any service. Using the information that Support Corp verifies before performing a service, Support Corp can determine where its services are received, and therefore must assign its receipts to these locations. The receipts from sales made to Support Corp's individual and business customers are in North Carolina to the extent that Support Corp's services are received in North Carolina. See Section IV.(3)(B)2.a. and b.

Example (ii). Online Corp, a corporation based outside North Carolina, provides web-based services through the means of the Internet to individual customers who are resident in North Carolina and in other states. These customers access Online Corp's web services primarily in their states of residence, and sometimes, while traveling, in other states. For a substantial portion of its receipts from the sale of services, Online Corp can either determine the state or states where the services are received, or, where 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 must assign to North Carolina the receipts from sales for which it does not know the customers' location in the same proportion as those receipts for which it has this information. See Section I.(5)(B).

Example (iii). 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 must assign

the receipts from sales of its services for which it lacks information as provided to its individual customers using the customers' billing addresses. See Section IV.(3)(B)2.a.

Example (iv). Net Corp, a corporation based outside North Carolina, provides web-based services to a business customer, Business Corp, a company with offices in North Carolina and two neighboring states. Particular employees of Business Corp access the services from computers in each Business Corp office. Assume that Net Corp determines that Business Corp employees in North Carolina were responsible for 75% of Business Corp's use of Net Corp's services, and Business Corp employees in other states were responsible for 25% of Business Corp's use of Net Corp's services. In this case, 75% of the receipts from the sale are received in North Carolina. See Section IV.(3)(B)2.a.i. 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 5% or less of its receipts from sales to Business Corp, Net Corp must assign the receipts under Section IV.(3)(B)2.b.iii. to the state where Business Corp principally managed the contract, or if that state is not reasonably determinable, to the state where Business Corp placed the order for the services, or if that state is not reasonably determinable, to the state of Business Corp's billing address. If Net Corp derives more than 5% of its receipts from sales of services to Business Corp, Net Corp is required to identify the state in which its contract of sale is principally managed by Business Corp and must assign the receipts to that state.

Example (v). Net Corp, a corporation based outside North Carolina, provides web-based services through the means of the Internet to more than 250 individual and business customers in North Carolina 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. Also assume that Net Corp does not derive more than 5% of its receipts from sales of services to a single customer. Net Corp may apply the safe harbor stated in Section IV.(3)(B)2.b.iv., and may assign its receipts using each customer's billing address.

3. Services Delivered Electronically Through or on Behalf of an Individual or Business Customer. A service delivered electronically "on behalf of" the customer is one in which a customer contracts for a service to be delivered electronically but one or more third parties, rather than the customer, is the recipient of the service, such as the direct or indirect

delivery of advertising on behalf of a customer to the customer's intended audience. A service delivered electronically "through" a customer to third-party recipients is a service that is delivered electronically to a customer for purposes of resale and subsequent electronic delivery in substantially identical form to end users or other third-party recipients.

- a. Rule of Determination. In the case of the delivery of a service by electronic transmission, where the service is delivered electronically to end users or other third-party recipients through or on behalf of the customer, the service is delivered in North Carolina if and to the extent that the end users or other third-party recipients are in North Carolina. 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 North Carolina to the extent that the audience for the advertising is in North Carolina. 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 North Carolina to the extent that the end users or other third-party recipients receive the services in North Carolina. The provisions in this subsection 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.
- b. 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 can reasonably approximate the state or states where the services are delivered, it shall reasonably approximate the state or states.
- c. Select Secondary Rules of Reasonable Approximation.
 - i. 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 information regarding the location of the audience from which it can determine or reasonably approximate that location, the taxpayer shall reasonably 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 reasonably approximate

the audience for advertising in a state using a percentage that reflects the ratio of the state's subscribers in the specific geographic area in which the advertising is delivered relative to the total subscribers in that area. For a taxpayer with less information about its audience, the taxpayer shall reasonably approximate the audience in a state using the percentage that reflects the ratio of the state's population in the specific geographic area in which the advertising is delivered relative to the total population in that area.

- ii. 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, if the taxpayer lacks sufficient information regarding the location of the end users or other third party recipients from which it can determine or reasonably approximate that location, the taxpayer shall reasonably approximate the extent to which the service is received in a state by using the percentage that reflects the ratio of the state's population in the specific geographic area in which the taxpayer's intermediary resells the services, relative to the total population in that area.
- iii. When using the secondary reasonable approximation methods provided above, the relevant specific geographic area of delivery includes only the areas where the service was substantially and materially delivered or resold. Unless the taxpayer demonstrates the contrary, it will be presumed that the area where the service was substantially and materially delivered or resold does not include areas outside the United States.

d. Examples:

Example (i). Cable TV Corp, a corporation that is based outside of North Carolina, has two revenue streams. First, Cable TV Corp sells advertising time to business customers pursuant to which the business customers' advertisements will run as commercials during Cable TV Corp's televised programming. Some of these business customers, though not all of them, have a physical presence in North Carolina. Second, Cable TV Corp sells monthly subscriptions to individual customers in North Carolina and in other states. The receipts from Cable TV Corp's sale of advertising time to its business customers are assigned to North Carolina to the extent that the audience for Cable TV Corp's televised programming during which the advertisements run is in North Carolina. See Section IV.(3)(B)3.a. If Cable TV Corp is unable to determine the actual location of its audience for the programming, and

lacks sufficient information regarding audience location to reasonably approximate the location, Cable TV Corp must approximate its North Carolina audience using the percentage that reflects the ratio of its North Carolina subscribers in the geographic area in which Cable TV Corp's televised programming featuring the advertisements is delivered relative to its total number of subscribers in that area. See Section IV.(3)(B)3.c.i. To the extent that Cable TV Corp's sales of monthly subscriptions represent the sale of a service, the receipts from these sales are properly assigned to North Carolina in any case in which the programming is received by a customer in North Carolina. See Section IV.(3)(B)2.a. In any case in which Cable TV Corp cannot determine the actual location where the programming is received, and lacks sufficient information regarding the location of receipt to reasonably approximate the location, the receipts from these sales of Cable TV Corp's monthly subscriptions are assigned to North Carolina where its customer's billing address is in North Carolina. See Section IV.(3)(B)2.a.ii. Note that whether and to the extent that the monthly subscription fee represents a fee for a service or for a license of intangible property does not affect the analysis or result as to the state or states to which the receipts are properly assigned. See Section V.(5).

Example (ii). Network Corp, a corporation that is based outside of North Carolina, sells advertising time to business customers pursuant to which the customers' advertisements will run as commercials during Network Corp's televised programming as distributed by unrelated cable television and satellite television transmission companies. The receipts from Network Corp's sale of advertising time to its business customers are assigned to North Carolina to the extent that the audience for Network Corp's televised programming during which the advertisements will run is in North Carolina. See Section IV.(3)(B)3.a. If Network Corp cannot determine the actual location of the audience for its programming during which the advertisements will run, and lacks sufficient information regarding audience location to reasonably approximate the location, Network Corp must approximate the receipts from sales of advertising that constitute North Carolina sales by multiplying the amount of advertising receipts by a percentage that reflects the ratio of the North Carolina population in the specific geographic area in which the televised programming containing the advertising is run relative to the total population in that area. See Section IV.(3)(B)3.c.ii. and iii.

Example (iii). Web Corp, a corporation that is based outside North Carolina, provides Internet content to viewers in North Carolina and other states. Web Corp sells advertising space to business customers pursuant to which the customers' advertisements will appear

in connection with Web Corp's Internet content. Web Corp receives a fee for running the advertisements that is determined by reference to the number of times the advertisement is viewed or clicked upon by the viewers of its website. The receipts from Web Corp's sale of advertising space to its business customers are assigned to North Carolina to the extent that the viewers of the Internet content are in North Carolina, as measured by viewings or clicks. See Section IV.(3)(B)3.a. 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 must approximate the amount of its North Carolina receipts by multiplying the amount of receipts from sales of advertising by a percentage that reflects the North Carolina population in the specific geographic area in which the content containing the advertising is delivered relative to the total population in that area. See Section IV.(3)(B)3.c.

Example (iv). Retail Corp, a corporation that is based outside of North Carolina, sells tangible property through its retail stores located in North Carolina and other states, and through a mail order catalog. Answer Co, a corporation that operates call centers in multiple states, contracts with Retail Corp to answer telephone calls from individuals placing orders for products found in Retail Corp's catalogs. In this case, the phone answering services of Answer Co are being delivered to Retail Corp's customers and prospective customers. Therefore, Answer Co is delivering a service electronically to Retail Corp's customers or prospective customers on behalf of Retail Corp, and must assign the proceeds from this service to the state or states from which the phone calls are placed by 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 must approximate the amount of its North Carolina sales by multiplying the amount of its fee from Retail Corp by a percentage that reflects the North Carolina population in the specific geographic area from which the calls are placed relative to the total population in that area. See Section IV.(3)(B)3.c.i.

Example (v). Web Corp, a corporation that is based outside of North Carolina, sells tangible property to customers via its Internet website. Design Co. designed and maintains Web Corp's website, including making changes to the site based on customer feedback received through the site. Design Co.'s services are delivered to Web Corp, the proceeds from which are assigned pursuant to Section IV.(3)(B)2. The fact that Web Corp's customers and prospective customers incidentally benefit from Design Co.'s services, and may even

interact with Design Co. in the course of providing feedback, does not transform the service into one delivered “on behalf of” Web Corp to Web Corp’s customers and prospective customers.

Example (vi). Wholesale Corp, a corporation that is based outside North Carolina, develops an Internet-based information database outside North Carolina and enters into a contract with Retail Corp whereby Retail Corp will market and sell access to this database to end users. Depending on the facts, the provision of database access may be either the sale of a service or the license of intangible property or may have elements of both. Assume that on the particular facts applicable in this example Wholesale Corp is selling database access in transactions properly characterized as involving the performance of a service. When an end user purchases access to Wholesale Corp’s database from Retail Corp, Retail Corp in turn compensates Wholesale Corp in connection with that transaction. In this case, Wholesale Corp’s services are being delivered through Retail Corp to the end user. Wholesale Corp must assign its receipts from sales to Retail Corp to the state or states in which the end users receive access to Wholesale Corp’s database. If Wholesale Corp cannot determine the state or states where the end users actually receive access to Wholesale Corp’s database, and lacks sufficient information regarding the location from which the end users access the database to reasonably approximate the location, Wholesale Corp must approximate the extent to which its services are received by end users in North Carolina by using a percentage that reflects the ratio of the North Carolina population in the specific geographic area in which Retail Corp regularly markets and sells Wholesale Corp’s database relative to the total population in that area. See Section IV.(3)(B)3.c.ii. Note that it does not matter for purposes of the analysis whether Wholesale Corp’s sale of database access constitutes a service or a license of intangible property, or some combination of both. See Section V.(5).

(4) Professional Services.

(A) In General.

Except as otherwise provided in these guidelines, Section IV.(4), 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, without

limitation, management services, bank and financial services, financial custodial services, investment and brokerage services, fiduciary services, tax preparation, payroll and accounting services, lending services, credit card services (including credit card processing services), data processing services, legal services, consulting services, video production services, graphic and other design services, engineering services, and architectural services.

(B) Overlap with Other Categories of Services.

1. Certain services that fall within the definition of “professional services” set forth in these guidelines, Section IV.(4), are nevertheless treated as “in-person services” within the meaning of Section IV.(2), and are assigned under the rules of that subsection. Specifically, professional services that are physically provided in person by the taxpayer such as carpentry, certain medical and dental services or child care services, where the customer or the customer’s real or tangible property upon which the services are provided is in the same location as the service provider at the time the services are performed, are “in-person services” and are assigned as such, notwithstanding that they may also be considered to be “professional services.” However, professional services where the service is of an intellectual or intangible nature, such as legal, accounting, financial and consulting services, are assigned as professional services under the rules of these guidelines, Section IV.(4), 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 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 these guidelines, Section IV.(4), and not those set forth in Section IV.(3), 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 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 must be reasonably approximated. The assignment of receipts from a sale of a professional service

depends in many cases upon whether the customer is an individual or business customer. In any instance in which the taxpayer, acting in good faith, cannot reasonably determine whether the customer is an individual or business customer, the taxpayer shall treat the customer as a business customer. For purposes of assigning the receipts from a sale of a professional service, a taxpayer's customer is the person that contracts for the service, irrespective of whether another person pays for or also benefits from the taxpayer's services.

1. General Rule. Receipts from sales of professional services other than those services described in Section IV.(4)(C)2., (architectural and engineering services), Section IV.(4)(C)3., (services provided by a financial institution) and Section IV.(4)(C)4., (transactions with related entities), are assigned in accordance with this guideline, Section IV.(4)(C)1.
 - a. Professional Services Delivered to Individual Customers. Except as otherwise provided in Section IV.(4), see in particular Section IV.(4)(C)4, 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 must be reasonably approximated as set forth in this guideline, Section IV.(4)(C)1. In particular, the taxpayer shall assign the receipts from a sale to the customer's state of primary residence, or, if the taxpayer cannot reasonably identify the customer's state of primary residence, to the state of the customer's billing address; provided, however, in any instance in which the taxpayer derives more than 5% 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.
 - b. Professional Services Delivered to Business Customers. Except as otherwise provided in Section IV.(4), 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 must be reasonably approximated as set forth in this section. In particular, unless the taxpayer can use the safe harbor set forth at Section IV.(4)(C)1.c., the taxpayer shall assign the receipts from the sale as follows: first, by assigning the receipts to the state where the contract of sale is principally managed by the customer; second, if the place of customer management is not reasonably determinable, to the customer's place of order; and third, if the customer place of order is not reasonably determinable, to the customer's billing address; provided, however, in any instance in

which the taxpayer derives more than 5% of its receipts from sales of all services from a customer, the taxpayer is required to identify the state in which the contract of sale is principally managed by the customer.

- c. **Safe Harbor; Large Volume of Transactions.** Notwithstanding the rules set forth in Section IV.(4)(C)1.a and b., 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 (1) engages in substantially similar service transactions with more than 250 customers, whether individual or business, and (2) does not derive more than 5% of its receipts from sales of all services from that customer. This safe harbor applies only for purposes of Section IV.(4)(C)1. and not otherwise.
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 these guidelines, Section IV.(4). However, unlike in the case of the general rule that applies to professional services, (1) 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 (2) 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 Section IV.(4)(C)2., the receipts from a sale of these services must be assigned under the general rule for professional services. See Section IV.(4)(C)1.
3. **Services provided by a Financial Institution.** The apportionment rules that apply to financial institutions are set forth in Section VII.(3) of these guidelines. That section includes specific rules to determine a financial institution's sales factor. However, those guidelines also provide that receipts from sales, other than sales of tangible personal property, including service transactions, that are not otherwise apportioned under that Section, are to be assigned pursuant to the guidelines applicable to all other business entities. For example, financial custodial services, those services are considered professional services within the meaning of this Section IV.(4) and are assigned according to the general rule for professional service transactions as set forth at Section IV.(4)(C)1.

4. **Related Entity Transactions.** In any instance in which the professional service is sold to a related party, rather than applying the rule for professional services delivered to business customers in Section IV.(4)(C)1.b, the state or states to which the service is assigned is the place of receipt by the related party as reasonably approximated using the following hierarchy: (1) if the service primarily relates to specific operations or activities of a related party conducted in one or more locations, then to the state or states in which those operations or activities are conducted in proportion to the related party's payroll at the locations to which the service relates in the state or states; or (2) if the service does not relate primarily to operations or activities of a related party conducted in particular locations, but instead relates to the operations of the related entity generally, then to the state or states in which the related party has employees, in proportion to the related party's payroll in those states. The taxpayer may use the safe harbor provided by Section IV.(4)(C)1.c.

5. **Examples:**

Assume in each of these examples, where relevant that the customer is not a related entity and that the safe harbor set forth at Section IV.(4)(C)1.c. does not apply.

Example (i). Broker Corp provides securities brokerage services to individual customers who are resident in North Carolina and in other states. Assume that Broker Corp knows the state of primary residence for many of its customers, and where it does not know this state of primary residence, it knows the customer's billing address. Also assume that Broker Corp does not derive more than 5% of its receipts from sales of all services from any one 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. See Section IV.(4)(C)1.a.

Example (ii). Same facts as in Example (i), except that Broker Corp has several individual customers from whom it derives, in each instance, more than 5% of its receipts from sales of all services. Receipts from sales to customers from whom Broker Corp derives 5% or less of its receipts from sales of all services must be assigned as described in Example (i). For each customer from whom it derives more than 5% of its receipts from sales of all services, Broker Corp is required to determine the customer's state of primary residence and must assign the receipts from the services provided to that customer to that state. In

any case in which a 5% customer's state of primary residence is North Carolina, receipts from a sale made to that customer must be assigned to North Carolina; in any case in which a 5% customer's state of primary residence is not North Carolina receipts from a sale made to that customer are not assigned to North Carolina.

Example (iii). Architecture Corp provides building design services as to buildings located, or expected to be located, in North Carolina to individual customers who are resident in North Carolina and other states, and to business customers that are based in North Carolina and other states. The receipts from Architecture Corp's sales are assigned to North Carolina because the locations of the buildings to which its design services relate are in North Carolina, or are expected to be in North Carolina. 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 North Carolina even if Architecture Corp's designs are either physically delivered to its customer in paper form in a state other than North Carolina or are electronically delivered to its customer in a state other than North Carolina. See Section IV.(4)(B)2. and (C)2.

Example (iv). Law Corp provides legal services to individual clients who are resident in North Carolina and in other states. In some cases, Law Corp may prepare one or more legal documents for its client as a result of these services and/or the legal work may be related to litigation or a legal matter that is ongoing in a state other than where the client is resident. Assume that Law Corp knows the state of primary residence for many of its clients, and where it does not know the state of primary residence, it knows the client's billing address. Also assume that Law Corp does not derive more than 5% of its receipts from sales of all services from any one 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. See Section IV.(4)(B)2 and (C)1.

Example (v). Law Corp provides legal services to several multistate business clients. In each case, Law Corp knows the state in which the agreement for legal services that governs the client relationship is principally managed by the client. In one case, the agreement is principally managed in North Carolina; in the other cases, the agreement is principally managed in a state other than North Carolina. If the agreement for legal services is principally managed by the client in North Carolina the receipts from sale of the services are assigned to North Carolina; in the other cases, the receipts are not assigned to North Carolina. In the case of receipts that are assigned to North Carolina, the receipts are so assigned even if (1) the legal documents relating to the service are mailed or otherwise delivered to a location in another state, or (2) the litigation or other legal matter that is the underlying predicate for the services is in another state. See Section IV.(4)(B)2. and (C)1.

Example (vi). Consulting Corp, a company that provides consulting services to law firms and other customers, is hired by Law Corp in connection with legal representation that Law Corp provides to Client Co. Specifically, Consulting Corp is hired to provide expert testimony at a trial being conducted by Law Corp on behalf of Client Co. Client Co pays for Consulting Corp's services directly. Assuming that Consulting Corp knows that its agreement with Law Co is principally managed by Law Corp in North Carolina, the receipts from the sale of Consulting Corp's services are assigned to North Carolina. 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. See Section IV.(4)(C)1.b.

*Example (vii).*¹ Bank Corp provides financial custodial services to 100 individual customers who are resident in North Carolina and in other states, including the safekeeping of some of its customers' financial assets. Assume for purposes of this example that Bank Corp knows the state of primary residence for many of its customers, and where it does not know this state of primary residence, it knows the customer's billing address. Also assume that Bank Corp does not derive more than 5% of its receipts from sales of all of its services from any single customer. Note that because Bank Corp does not have more than 250 customers, it may not apply the safe harbor for professional services stated in Section IV.(4)(C)1.c. If Bank Corp knows its customer's state of primary

¹ See Guideline re: Financial Institutions, Section IV.(4)(C)3, p. 27.

residence, it must 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 must assign the receipts to that state. Bank Corp's receipts are assigned to North Carolina if the customer's state of primary residence (or billing address, in cases where it does not know the customer's state of primary residence) is in North Carolina, even if Bank Corp's financial custodial work, including the safekeeping of the customer's financial assets, takes place in a state other than North Carolina. See Section IV.(4)(C)1.

*Example (viii).*² Same facts as Example (vii), except that Bank Corp has more than 250 customers, individual or business. Bank Corp may apply the safe harbor for professional services stated in Section IV.(4)(C)1.c., and may assign its receipts from sales to a state or states using each customer's billing address.

*Example (ix).*³ Same facts as Example (viii), except that Bank Corp derives more than 5% of its receipts from sales from a single individual customer. As to the sales made to this customer, Bank Corp is required to determine the individual customer's state of primary residence and must assign the receipts from the service or services provided to that customer to that state. See Section IV.(4)(C)1.a. and (C)3. Receipts from sales to all other customers are assigned as described in Example (viii).

Example (x). 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 resident in numerous states, which may or may not include North Carolina. Assuming that Advisor Corp knows that its agreement with Investment Co is principally managed by Investment Co in North Carolina, receipts from the sale of Advisor Corp's services are assigned to North Carolina. 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. See Section IV.(4)(C)1.b.

² See Guideline re: Financial Institutions, Section IV.(4)(C)3, p. 27.

³ See Guideline re: Financial Institutions, Section IV.(4)(C)3, p. 27.

Example (xi). 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 North Carolina, receipts from the sale of Advisor Corp's services are assigned to North Carolina. See Section IV.(4)(C)1.b. Note that it is not relevant for purposes of the analysis that the partners in Investment Fund LP are residents of numerous states.

Example (xii). Design Corp is a corporation based outside North Carolina that provides graphic design and similar services in North Carolina and in neighboring states. Design Corp enters into a contract at a location outside North Carolina with an individual customer to design fliers for the customer. Assume that Design Corp does not know the individual customer's state of primary residence and does not derive more than 5% of its receipts from sales of services from the individual customer. All of the design work is performed outside North Carolina. Receipts from the sale are in North Carolina if the customer's billing address is in North Carolina. See Section IV.(4)(C)1.a.

V. License or Lease of Intangible Property.

(1) General Rules.

- (A) The receipts from the license of intangible property are in North Carolina if and to the extent the intangible is used in North Carolina. In general, the term "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 at Section V.(2)-(5). For purposes of the rules set forth in this Section V., a lease of intangible property is to be treated the same as a license of intangible property.
- (B) In general, a license of intangible property that conveys all substantial rights in that property is treated as a sale of intangible property for purposes of these guidelines. See Section VI. Note, however, that for purposes of Sections V. and VI., a sale or exchange of intangible property is treated as a license of that property where the receipts from the sale or exchange derive from payments that are contingent on the productivity, use or disposition of the property.

- (C) Intangible property licensed as part of the sale or lease of tangible property is treated under these guidelines as the sale or lease of tangible property.
- (D) Nothing in this Section V. shall be construed to allow or require inclusion of sales in the sales factor that are not included in the definition of “sales” pursuant to N. C. Gen. Stat. § 105-130.4, or that are excluded from the numerator and the denominator of the sales factor pursuant to Market Based Sourcing Principle 1.e. of Session Law 2015-268, section 32.14A.(b) and restated in the Introduction and Summary to these guidelines. To the extent that the transfer of either a security or business “goodwill” or similar intangible value, including, without limitation, “going concern value” or “workforce in place,” may be characterized as a license or lease of intangible property, receipts from such transaction shall be excluded from the numerator and the denominator of the taxpayer’s sales factor.

(2) License of a Marketing Intangible.

Where a license is granted for the right to use intangible property in connection with the sale, lease, license, or other marketing of goods, services, or other items (i.e., a marketing intangible) to a consumer, the royalties or other licensing fees paid by the licensee for that marketing intangible are assigned to North Carolina 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 North Carolina. Examples of a license of a marketing intangible include, without limitation, the license of a service mark, trademark, or trade name; certain copyrights; the license of a film, television or multimedia production or event for commercial distribution; and a franchise agreement. In each of these instances the license of the marketing intangible is intended to promote consumer sales. In the case of the license of a marketing intangible, where a taxpayer has actual evidence of the amount or proportion of its receipts that is attributable to North Carolina, it shall assign that amount or proportion to North Carolina. In the absence of actual evidence of the amount or proportion of the licensee's receipts that are derived from North Carolina consumers, the portion of the licensing fee to be assigned to North Carolina must be reasonably approximated by multiplying the total fee by a percentage that reflects the ratio of the North Carolina population in the specific geographic area in which the licensee makes material use of the intangible property to regularly market its goods, services or other items relative to the total population in 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 North Carolina must be reasonably approximated by multiplying the

total fee by a percentage that reflects the ratio of the North Carolina population in the specific geographic area in which the licensee's goods, services, or other items are ultimately and materially marketed using the intangible property relative to the total population of 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 that marketing intangible will be presumed to be derived from within the United States.

(3) 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 North Carolina to the extent that the use for which the fees are paid takes place in North Carolina. Examples of a license of a production intangible include, without limitation, the license of a patent, a copyright, or trade secrets to be used in a manufacturing process, where the value of the intangible lies predominately in its use in that process. If the actual use of intangible property pursuant to a license of a production intangible takes place in part in North Carolina, it is presumed that the entire use is in this state except to the extent that the taxpayer can demonstrate that the actual location of a portion of the use takes place outside North Carolina. In the case of a license of a production intangible to a related party, the taxpayer must assign the receipts to where the intangible property is actually used. In the case of a license of a production intangible to a party other than a related party where 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).

(4) 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 Secretary will accept that separate statement for purposes of these guidelines. 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 can reasonably establish otherwise.

(5) License of Intangible Property where Substance of Transaction Resembles a Sale of Goods or Services.

(A) In general.

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 Section IV.(3)(B)2. and 3., 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 Section V.(5) include, without limitation, the license of database access, the license of access to information, the license of digital goods (see Section VII.(2)), and the license of certain software (e.g., where the transaction is not the license of pre-written software that is treated as the sale of tangible personal property. See Section VII.(1)).

(B) Sublicenses.

Pursuant to Section V.(5)(A), the guidelines of Section IV.(3)(B)3. may apply where 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. In particular, the guidelines set forth at Section IV.(3)(B)3. that apply to services delivered electronically to a customer for purposes of resale and subsequent electronic delivery in substantially identical form to end users or other recipients may also apply with respect to licenses of intangible property for purposes of sublicense to end users. 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.

(C) Examples:

In these examples, assume that the customer is not a related entity.

Example (i). Crayon Corp and Dealer Co enter into a license contract under which Dealer Co as licensee is permitted to use trademarks that are owned by Crayon Corp in connection with Dealer Co's sale of certain products to retail customers. Under the contract, Dealer Co is required to pay Crayon Corp a licensing fee that is a fixed percentage of the total volume of monthly sales made by Dealer Co of products using the Crayon Corp trademarks. Under the contract, Dealer Co is permitted to sell the products at multiple store locations, including store locations that are both within and without North Carolina. 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 North Carolina are determined by multiplying the fees by a percentage that reflects the ratio of Dealer Co's receipts that are derived from its North Carolina stores relative to Dealer Co's total receipts. See Section V.(2).

Example (ii). Program Corp, a corporation that is based outside North Carolina, licenses programming that it owns to licensees, such as cable networks, that in turn will offer the programming to their customers on television or other media outlets in North Carolina and in all other U.S. states. Each of these licensing contracts constitutes the license of a marketing intangible. For each licensee, assuming that Program Corp lacks evidence of the actual number of viewers of the programming in North Carolina, the component of the licensing fee paid to Program Corp by the licensee that constitutes Program Corp's North Carolina receipts is determined by multiplying the amount of the licensing fee by a percentage that reflects the ratio of the North Carolina audience of the licensee for the programming relative to the licensee's total U.S. audience for the programming. See Section V. Note that the analysis and result as to the state or states to which receipts are properly assigned would be the same to the extent that the substance of Program Corp's licensing transactions may be determined to resemble a sale of goods or services, instead of the license of a marketing intangible. See Section V.(5).

Example (iii). Moniker Corp enters into a license contract with Wholesale Co. Pursuant to the contract Wholesale Co is granted the right to use trademarks owned by Moniker Corp to brand sports equipment that is to be manufactured by Wholesale Co or an unrelated entity,

and to sell the manufactured equipment to unrelated companies that will ultimately market the equipment to consumers in a specific geographic region, including a foreign country. The license agreement confers a license of a marketing intangible, even though the trademarks in question will be affixed to property to be manufactured. In addition, the license of the marketing intangible is for the right to use the intangible property in connection with sales to be made at wholesale rather than directly to retail customers. The component of the licensing fee that constitutes the North Carolina receipts of Moniker Corp is determined by multiplying the amount of the fee by a percentage that reflects the ratio of the North Carolina population in the specific geographic region relative to the total population in that region. See Section V.(2). 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 will 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.

Example (iv). Formula, Inc and Appliance Co enter into a license contract under which Appliance Co is permitted to use a patent owned by Formula, Inc to manufacture appliances. The license contract specifies that Appliance Co is to pay Formula, Inc a royalty that is a fixed percentage of the gross receipts from the products that are later sold. The contract does not specify any other fees. The appliances are both manufactured and sold in North Carolina 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 actual use of the intangible property takes place in part in North Carolina, the royalty is assigned based to the location of that use rather than to location of the licensee's commercial domicile, in accordance with Section V.(1). It is presumed that the entire use is in North Carolina except to the extent that the taxpayer can demonstrate that the actual location of some or all of the use takes place outside North Carolina. Assuming that Formula, Inc can demonstrate the percentage of manufacturing that takes place in North Carolina using the patent relative to the manufacturing in other states, that percentage of the total licensing fee paid to Formula, Inc under the contract will constitute Formula, Inc's North Carolina receipts. See Section V.(5).

Example (v). Axel Corp enters into a license agreement with Biker Co in which Biker Co is granted the right to produce motor scooters using patented technology owned by Axel Corp, and also to sell 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 North Carolina. Assume that Axel Corp lacks actual information regarding the proportion of Biker Co.'s receipts that are derived from North Carolina customers. Also assume that Biker Co is granted the right to sell the scooters in a U.S. geographic region in which the North Carolina population constitutes 25% of the total population during the period in question. The licensing contract requires an upfront licensing fee to be paid by Biker Co to Axel Corp and does not specify what percentage of the fee derives from Biker Co's right to use Axel Corp's patented technology. Because the fees for the license of the marketing and production intangible are not separately and reasonably stated in the contract, it is presumed that the licensing fees are paid entirely for the license of a marketing intangible, unless the taxpayer reasonably establishes otherwise. Assuming the taxpayer does not establish otherwise, 25% of the licensing fee constitutes North Carolina receipts. See Section V.(2), V.(4).

Example (vi). Same facts as Example 5, except that the license contract specifies separate fees to be paid for the right to produce the motor scooters and for the right to sell the scooters by marketing the fact that the scooters were manufactured using the special technology. The licensing contract constitutes both the license of a marketing intangible and the license of a production intangible. Assuming that the separately stated fees are reasonable, (1) no part of the licensing fee paid for the production intangible will be assigned to North Carolina, and (2) 25% of the licensing fee paid for the marketing intangible will be assigned to North Carolina. See Section V.(4).

Example (vii). Better Burger Corp, which is based outside North Carolina, 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 North Carolina. 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 North Carolina

franchises constitute fees paid for the licensing of a marketing intangible. These fees constitute North Carolina receipts because the franchises are for the right to make North Carolina sales. The monthly franchise fees paid by North Carolina franchisees constitute fees paid for (1) the license of marketing intangibles (the Better Burger name and service marks), (2) the license of production intangibles (food processes and know-how) and (3) personal services (management fees). The fees paid for the license of the marketing intangibles and the production intangibles constitute North Carolina receipts because in each case the use of the intangibles is to take place in North Carolina. See Section V.(2)-(3). The fees paid for the personal services are to be assigned pursuant to Section IV.

Example (viii). Online Corp, a corporation based outside North Carolina, licenses an information database through the means of the Internet to individual customers that are resident in North Carolina 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 Section V.(5). If Online Corp can determine or reasonably approximate the state or states where its database is accessed, it must do so. Assuming that Online Corp cannot determine or reasonably approximate the location where its database is accessed, Online Corp must assign the receipts made to the individual customers using the customers' billing addresses to the extent known. Assume for purposes of this example that Online Corp knows the billing address for each of its customers. In this case, Online Corp's receipts from sales made to its individual customers are in North Carolina in any case in which the customer's billing address is in North Carolina. See Section IV.(3)(B)2.a.

Example (ix). Net Corp, a corporation based outside North Carolina, licenses an information database through the means of the Internet to a business customer, Business Corp, a company with offices in North Carolina and two neighboring states. The license is a license of intangible property that resembles a sale of goods or services and are assigned in accordance with Section V.(5). Assume that Net Corp cannot determine where its database is accessed but reasonably approximates that 75% of Business Corp's database access took place in North Carolina, and 25% of Business Corp's database access took place in other states. In that case, 75% of the receipts from database access are in North Carolina. 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 5% or less of its receipts from database access from Business Corp, Net Corp must assign the receipts under Section IV.(3)(B)2.b. to the state where Business Corp principally managed the contract, or if that state is not reasonably determinable to the state where Business Corp placed the order for the services, or if that state is not reasonably determinable to the state of Business Corp's billing address. If Net Corp derives more than 5% of its receipts from database access from Business Corp, Net Corp is required to identify the state in which its contract of sale is principally managed by Business Corp and must assign the receipts to that state. See Section IV.(3)(B)2.b.

Example (x). Net Corp, a corporation based outside North Carolina, licenses an information database through the means of the Internet to more than 250 individual and business customers in North Carolina 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 Section V.(5). Assume that Net Corp cannot determine or reasonably approximate the location where its information database is accessed. Also assume that Net Corp does not derive more than 5% of its receipts from sales of database access from any single customer. Net Corp may apply the safe harbor stated in Section IV.(3)(B)2.b.iv., and may assign its receipts to a state or states using each customer's billing address.

Example (xi). Web Corp, a corporation based outside of North Carolina, licenses an Internet-based information database to business customers who then sublicense the database to individual end users that are resident in North Carolina 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 Section IV.(3)(B)3. See Section V.(5). If Web Corp can determine or reasonably approximate the state or states where its database is accessed by end users, it must do so. Assuming that Web Corp lacks sufficient information from which it can determine or

reasonably approximate the location where its database is accessed by end users, Web Corp must approximate the extent to which its database is accessed in North Carolina using a percentage that represents the ratio of the North Carolina population in the specific geographic area in which Web Corp's customer sublicenses the database access relative to the total population in that area. See Section IV.(3)(B)3.c.

VI. Sale of Intangible Property.

(1) 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 Section VI, a sale or exchange of intangible property includes a license of that property where the transaction is treated for tax purposes as a sale of all substantial rights in the property and the receipts from the transaction are not contingent on the productivity, use or disposition of the property. For the rules that apply where the consideration for the transfer of rights is contingent on the productivity, use or disposition of the property. See Section V.(1).

(A) Contract Right or Government License that Authorizes Business Activity in Specific Geographic Area.

In the case of a sale or exchange of intangible property where the property sold or exchanged is a contract right, government license or similar intangible property that authorizes the holder to conduct a business activity in a specific geographic area, the receipts from the sale are assigned to a state if and to the extent that the intangible property is used or is authorized to be used within the state. If the intangible property is used or may be used only in this State the taxpayer shall assign the receipts from the sale to North Carolina. If the intangible property is used or is authorized to be used in North Carolina and one or more other states, the taxpayer shall assign the receipts from the sale to North Carolina to the extent that the intangible property is used in or authorized for use in North Carolina, through the means of a reasonable approximation.

(B) Sale that Resembles a License (Receipts are Contingent on Productivity, Use or Disposition of the Intangible Property).

In the case of a sale or exchange of intangible property where the receipts from the sale or exchange are contingent on the productivity, use or disposition of the property, the receipts from the sale are assigned by applying the rules set forth in Section V. (pertaining to the license or lease of intangible property).

(C) Sale that Resembles a Sale of Goods and Services.

In the case of a sale or exchange of intangible property where the substance of the transaction resembles a sale of goods or services and where the receipts from the sale or exchange do not derive from payments contingent on the productivity, use or disposition of the property, the receipts from the sale are assigned by applying the rules set forth in Section V.(5) (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 Section V.(5).

(D) Excluded Receipts.

Receipts from the sale of intangible property are not included in the sales factor in any case in which the sale does not give rise to receipts within the meaning of Section I.(6)(A) of these guidelines. In addition, in any case in which the sale of intangible property does result in receipts within the meaning of Section I.(6)(A), those receipts are excluded from the numerator and the denominator of the taxpayer's sales factor if the receipts are not referenced in the Market-Based Sourcing Principles set out in subdivisions 1.d and 1.e of Session Law 2015-268, section 32.14A.(b) and restated in the Introduction and Summary to these guidelines. The sale of intangible property that is excluded from the numerator and denominator of the taxpayer's sales factor under this provision includes, without limitation, the sale of business "goodwill," the sale of an agreement not to compete, or similar intangible value.

(E) Examples.

Example (i). Airline Corp, a corporation based outside North Carolina, sells its rights to use several gates at an airport located in North Carolina to Buyer Corp, a corporation that is based outside North Carolina. The contract of sale is negotiated and signed outside of North Carolina. The receipts from the sale are in North Carolina because the intangible

property sold is a contract right that authorizes the holder to conduct a business activity solely in North Carolina. See Section VI.(1).

Example (ii). Wireless Corp, a corporation based outside North Carolina, sells a license issued by the Federal Communications Commission (FCC) to operate wireless telecommunications services in a designated area in North Carolina to Buyer Corp, a corporation that is based outside North Carolina. The contract of sale is negotiated and signed outside of North Carolina. The receipts from the sale are in North Carolina because the intangible property sold is a government license that authorizes the holder to conduct business activity solely in North Carolina. See Section VI.(1)(A).

Example (iii). Same facts as in Example (ii) except that Wireless Corp sells to Buyer Corp an FCC license to operate wireless telecommunications services in a designated area in North Carolina and an adjacent state. Wireless Corp must attempt to reasonably approximate the extent to which the intangible property is used in or may be used in North Carolina. 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 states covered by the license. See Section VI.(1)(A).

Example (iv). Sports League Corp, a corporation that is based outside North Carolina, sells the rights to broadcast the sporting events played by the teams in its league in all 50 U.S. states to Network Corp. Although the games played by Sports League Corp will be broadcast in all 50 states, the games are of greater interest in the eastern region of the country, including North Carolina. Because the intangible property sold is a contract right that authorizes the holder to conduct a business activity in a specified geographic area, Sports League Corp must attempt to reasonably approximate the extent to which the intangible property is used in or may be used in North Carolina. 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 North Carolina and the other states. See Section VI.(1)(A).

Example (v). Inventor Corp, a corporation that is based outside North Carolina, sells patented technology that it has developed to Buyer Corp, a business customer that is based in North Carolina. 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. See

Section VI.(1)(A). Inventor Corp understands that Buyer Corp is likely to use the patented technology in North Carolina, but the patented technology can 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 sales factor. See Section VI.(1)(D).

VII. Special Rules.

(1) 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 North Carolina as determined under the rules for the sale of tangible personal property set forth under N.C. Gen. Stat. § 105-130.4 and related regulations. In all other cases, the receipts from a license or sale of software are to be assigned to North Carolina as determined otherwise under these guidelines, (e.g., depending on the facts, as the development and sale of custom software, see Section IV.(3), as a license of a marketing intangible, see Section V.(2), as a license of a production intangible, see Section V.(3), as a license of intangible property where the substance of the transaction resembles a sale of goods or services, see Section V.(5), or as a sale of intangible property, see Section VI.)

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

(A) In general.

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 guidelines as are set forth in Section IV.(3)(B)2. or 3., 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. See Section V.(5) and VI.(1)(C).

(B) Telecommunications Companies.

In the case of a taxpayer that provides telecommunications or ancillary services and that is thereby subject to Multistate Tax Commission Reg. IV.18(i), receipts from the sale or license of digital goods or services not otherwise assigned for apportionment purposes pursuant to that regulation are assigned pursuant to these guidelines, Section VII.(2)(B), by applying the rules set forth in Section IV.(3)(B)2. or 3. 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. However, in applying these rules, if the taxpayer cannot determine the state or states where a customer receives the purchased product it may reasonably approximate this location using the customer's place of "primary use" of the purchased product, applying the definition of "primary use" set forth in MTC Model Regulation for Sourcing Sales of Telecommunications and Ancillary Services.

(3) Financial Institutions

(A). Apportionment and Allocation.

(1) Except as otherwise specifically provided in these guidelines, a financial institution whose business activity is taxable both within and without North Carolina shall allocate and apportion its net income as provided in Article 4 of Chapter 105. All items of nonapportionable income (income which is not includable in the apportionable income tax base) shall be allocated pursuant to the provisions of G.S. 105-130.4. A financial institution organized under the laws of a foreign country, the Commonwealth of Puerto Rico, or a territory or possession of the United States whose effectively connected income (as defined under the Federal Internal Revenue Code) is taxable both within this State and within another state, other than the state in which it is organized, shall allocate and apportion its net income as provided in Article 4 of Chapter 105.

(2) All apportionable income shall be apportioned to this state by multiplying such income by the sales factor as provided in N.C. Gen. Stat. § 105-130.4 and these guidelines.

(B) Definitions.

As used in this section unless the context otherwise requires:

(1) "**Billing address**" means the location indicated in the books and records of the taxpayer on the first day of the taxable year (or on such later date in the taxable year when the customer relationship began) as the address where any notice, statement and/or bill relating to a customer's account is mailed.

(2) "**Borrower or credit card holder located in this state**" means:

- (a) a borrower, other than a credit card holder, that is engaged in a trade or business which maintains its commercial domicile in this state; or
- (b) a borrower that is not engaged in a trade or business or a credit card holder whose billing address is in this state.

(3) "**Card issuer's reimbursement fee**" means the fee a taxpayer receives from a merchant's bank because one of the persons to whom the taxpayer has issued a credit, debit, or similar type of card has charged merchandise or services to the card.

(4) "**Commercial domicile**" means:

- (a) the headquarters of the trade or business, that is, the place from which the trade or business is principally managed and directed; or
- (b) if a taxpayer is organized under the laws of a foreign country, or of the Commonwealth of Puerto Rico, or any territory or possession of the United States, such taxpayer's commercial domicile shall be deemed for the purposes of these guidelines to be the state of the United States or the District of Columbia from which such taxpayer's trade or business in the United States is principally managed and directed. It shall be presumed, subject to rebuttal, that the location from which the taxpayer's trade or business is principally managed and directed is the state of the United States or the District of Columbia to which the greatest number of employees are regularly connected or out of which they are working, irrespective of where the services of such employees are performed, as of the last day of the taxable year.

(5) "**Credit card**" means a card, or other means of providing information, that entitles the holder to charge the cost of purchases, or a cash advance, against a line of credit.

(6) "**Debit card**" means a card, or other means of providing information, that enables the holder to charge the cost of purchases, or a cash withdrawal, against the holder's bank account or a remaining balance on the card.

(7) "**Employee**" means, with respect to a particular taxpayer, any individual who, under the usual common-law rules applicable in determining the employer-employee relationship, has the status of an employee of that taxpayer.

(8) "**Financial institution**" means,

- (a) Any corporation or other business entity registered under state law as a bank holding company or registered under the Federal Bank Holding Company Act of 1956, as amended, or registered as a savings and loan holding company under the Federal National Housing Act, as amended;
- (b) A national bank organized and existing as a national bank association pursuant to the provisions of the National Bank Act, 12 U.S.C. §§21 et seq.;
- (c) A savings association or federal savings bank as defined in the Federal Deposit Insurance Act, 12 U.S.C 1813(b)(1);
- (d) Any bank or thrift institution incorporated or organized under the laws of any state;
- (e) Any corporation organized under the provisions of 12 U.S.C. 611 to 631.
- (f) Any agency or branch of a foreign depository as defined in 12 U.S.C. §3101;
- (g) A state credit union the loan assets of which exceed \$50,000,000 as of the first day of its taxable year;
- (h) A production credit association organized under the Federal Farm Credit Act of 1933, all of whose stock held by the Federal Production Credit Corporation has been retired;
- (i) Any corporation whose voting stock is more than fifty percent (50%) owned, directly or indirectly, by any person or business entity described in subsections (a) through (h) above other than an insurance company taxable under Article 8B of Chapter 105;
- (j) A corporation or other business entity that derives more than fifty percent (50%) of its total gross income for financial accounting purposes from finance leases. For purposes of this subsection, a "finance lease" shall mean any lease transaction which is the functional equivalent of an extension of credit and that transfers substantially all of the benefits and risks incident to the ownership of property. The phrase shall include any "direct financing lease" or "leverage lease" that meets the criteria of Financial Accounting Standards Board Statement No. 13, "Accounting for Leases" or any other lease that is accounted for as a financing by a lessor under generally accepted accounting principles.

For this classification to apply,

- (a) the average of the gross income in the current tax year and immediately preceding two tax years must satisfy the more than fifty percent (50%) requirement; and

(b) gross income from incidental or occasional transactions shall be disregarded;

(k) Any other person or business entity, other than an insurance company taxable under Article 8B of Chapter 105, a real estate broker defined in Article 1 of Chapter 93A, or a securities dealer regulated under Chapter 78A, which derives more than fifty percent (50%) of its gross income from activities that a person described in subsections (b) through (h) and (j) above is authorized to transact. For the purpose of this subsection, the computation of gross income shall not include income from non-recurring, extraordinary items.

The Secretary is authorized to exclude any person from the application of subsection (k) upon such person proving, by clear and convincing evidence, that the income-producing activity of such person is not in substantial competition with those persons described in subsections (b) through (h) and (j) above.

(9) "**Loan**" means any extension of credit resulting from direct negotiations between the taxpayer and its customer, and/or the purchase, in whole or in part, of such extension of credit from another. Loans include participations, syndications, and leases treated as loans for federal income tax purposes. Loans shall not include: futures or forward contracts; options; notional principal contracts such as swaps; credit card receivables, including purchased credit card relationships; non-interest bearing balances due from depository institutions; cash items in the process of collection; federal funds sold; securities purchased under agreements to resell; assets held in a trading account; securities; interests in a REMIC, or other mortgage-backed or asset-backed security; and other similar items.

(10) "**Loan secured by real property**" means that fifty percent or more of the aggregate value of the collateral used to secure a loan or other obligation, when valued at fair market value as of the time the original loan or obligation was incurred, was real property.

(11) "**Merchant discount**" means the fee (or negotiated discount) charged to a merchant by the taxpayer for the privilege of participating in a program whereby a credit, debit, or similar type of card is accepted in payment for merchandise or services sold to the card holder, net of any cardholder charge-back and unreduced by any interchange transaction or issuer reimbursement fee paid to another for charges or purchases made its cardholder.

(12) "**Participation**" means an extension of credit in which an undivided ownership interest is held on a *pro rata* basis in a single loan or pool of loans and related collateral. In a loan participation, the

credit originator initially makes the loan and then subsequently resells all or a portion of it to other lenders. The participation may or may not be known to the borrower.

(13) "**Person**" means an individual, estate, trust, partnership, corporation and any other business entity.

(14) "**Principal base of operations**" with respect to transportation property means the place of more or less permanent nature from which said property is regularly directed or controlled. With respect to an employee, the "principal base of operations" means the place of more or less permanent nature from which the employee regularly (1) starts his or her work and to which he or she customarily returns in order to receive instructions from his or her employer or (2) communicates with his or her customers or other persons, or (3) performs any other functions necessary to the exercise of his or her trade or profession at some other point or points.

(15) "**Real property owned**" and "**tangible personal property owned**" mean real and tangible personal property, respectively, (1) on which the taxpayer may claim depreciation for federal income tax purposes, or (2) property to which the taxpayer holds legal title and on which no other person may claim depreciation for federal income tax purposes (or could claim depreciation if subject to federal income tax). Real and tangible personal property do not include coin, currency, or property acquired in lieu of or pursuant to a foreclosure.

(16) "**Regular place of business**" means an office at which the taxpayer carries on its business in a regular and systematic manner and which is continuously maintained, occupied and used by employees of the taxpayer.

(17) "**State**" means a state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, any territory or possession of the United States or any foreign country.

(18) "**Syndication**" means an extension of credit in which two or more persons fund and each person is at risk only up to a specified percentage of the total extension of credit or up to a specified dollar amount.

(19) "**Taxable**" means either:

- (a) that a taxpayer is subject in another state to a net income tax, a franchise tax measured by net income, a franchise tax for the privilege of doing business, a corporate stock tax (including a bank shares tax), a single business tax, or an earned surplus tax, or any tax which is imposed upon or measured by gross or net income; or

(b) that another state has jurisdiction to subject the taxpayer to any of such taxes regardless of whether, in fact, the state does or does not.

(20) "**Transportation property**" means vehicles and vessels capable of moving under their own power, such as aircraft, trains, water vessels and motor vehicles, as well as any equipment or containers attached to such property, such as rolling stock, barges, trailers or the like.

(C) Sales Factor.

(1) **General.** The sales factor is a fraction, the numerator of which is the sales of the taxpayer in this State during the taxable year and the denominator of which is the sales of the taxpayer within and without this State during the taxable year. The method of calculating sales for purposes of the denominator is the same as the method used in determining sales for purposes of the numerator. The sales factor shall include only those receipts described herein which constitute apportionable income and are included in the computation of the apportionable income base for the taxable year.

(2) **Receipts from the lease of real property.** The numerator of the sales factor includes receipts from the lease or rental of real property owned by the taxpayer if the property is located within this State or receipts from the sublease of real property if the property is located within this State.

(3) **Receipts from the lease of tangible personal property.**

(a) Except as described in paragraph (b) of this subsection, the numerator of the sales factor includes receipts from the lease or rental of tangible personal property owned by the taxpayer if the property is located within this state when it is first placed in service by the lessee.

(b) Receipts from the lease or rental of transportation property owned by the taxpayer are included in the numerator of the sales factor to the extent that the property is used in this State. The extent an aircraft will be deemed to be used in this State and the amount of receipts that is to be included in the numerator of the North Carolina sales factor is determined by multiplying all the receipts from the lease or rental of the aircraft by a fraction, the numerator of which is the number of landings of the aircraft in this State and the denominator of which is the total number of landings of the aircraft. If the extent of the use of any transportation property within this State cannot be determined, then the property will be deemed to be used wholly in the state in which the property has its principal base of

operations. A motor vehicle will be deemed to be used wholly in the state in which it is registered.

(4) Interest, fees and penalties imposed in connection with loans secured by real property.

- (a) The numerator of the sales factor includes interest, fees, and penalties imposed in connection with loans secured by real property if the property is located within this State. If the property is located both within this State and one or more other states, the receipts described in this subsection are included in the numerator of the sales factor if more than fifty percent of the fair market value of the real property is located within this State. If more than fifty percent of the fair market value of the real property is not located within any one state, then the receipts described in this subsection shall be included in the numerator of the sales factor if the borrower is located in this State.
- (b) The determination of whether the real property securing a loan is located within this state shall be made as of the time the original agreement was made and any and all subsequent substitutions of collateral shall be disregarded.

(5) Interest, fees, and penalties imposed in connection with loans not secured by real property. The numerator of the sales factor includes interest, fees, and penalties imposed in connection with loans not secured by real property if the borrower is located in this State.

(6) Net gains from the sale of loans. The numerator of the sales factor includes net gains from the sale of loans. Net gains from the sale of loans includes income recorded under the coupon stripping rules of Section 1286 of the Internal Revenue Code.

- (a) The amount of net gains (but not less than zero) from the sale of loans secured by real property included in the numerator is determined by multiplying such net gains by a fraction the numerator of which is the amount included in the numerator of the sales factor pursuant to subsection (4) of this section and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans secured by real property.
- (b) The amount of net gains (but not less than zero) from the sale of loans not secured by real property included in the numerator is determined by multiplying such net gains by a fraction the numerator of which is the amount included in the numerator of the sales factor pursuant to subsection (5) of this section and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans not secured by real property.

(7) **Receipts from fees, interest, and penalties charged to card holders.** The numerator of the sales factor includes fees, interest and penalties charged to credit, debit or similar card holders, including but not limited to annual fees and overdraft fees, if the billing address of the card holder is in this State.

(8) **Net gains from the sale of credit card receivables.** The numerator of the sales factor includes net gains (but not less than zero) from the sale of credit card receivables multiplied by a fraction, the numerator of which is the amount included in the numerator of the sales factor pursuant to subsection (7) of this section and the denominator of which is the taxpayer's total amount of interest and fees or penalties in the nature of interest from credit card receivables and fees charged to card holders.

(9) **Card issuer's reimbursement fees.** The numerator of the sales factor includes:

- (a) all credit card issuer's reimbursement fees multiplied by a fraction, the numerator of which is the amount of fees, interest, and penalties charged to credit card holders included in the numerator of the sales factor pursuant to subsection (7) of this section and the denominator of which is the taxpayer's total amount of fees, interest, and penalties charged to credit card holders.
- (b) all debit card issuer's reimbursement fees multiplied by a fraction, the numerator of which is the amount of fees, interest, and penalties charged to debit card holders included in the numerator of the sales factor pursuant to subsection (7) of this section and the denominator of which is the taxpayer's total amount of fees, interest, and penalties charged to debit card holders.
- (c) all other card issuer's reimbursement fees multiplied by a fraction, the numerator of which is the amount of fees, interest, and penalties charged to all other card holders included in the numerator of the sales factor pursuant to subsection (7) of this section and the denominator of which is the taxpayer's total amount of fees, interest, and penalties charged to all other card holders.

(10) **Receipts from merchant discount.**

- (a) If the taxpayer can readily determine the location of the merchant and if the merchant is in this State, the numerator of the sales factor includes receipts from merchant discount.
- (b) If the taxpayer cannot readily determine the location of the merchant, the numerator of the sales factor includes such receipts from the merchant discount multiplied by a fraction:

- i. in the case of a merchant discount related to the use of a credit card, the numerator of which is the amount of fees, interest and penalties charged to credit card holders that is included in the numerator of the sales factor pursuant to subsection (7) of this section and the denominator of which is the taxpayer's total amount of fees, interest and penalties charged to credit card holders, and
 - ii. in the case of a merchant discount related to the use of a debit card, the numerator of which is the amount of fees, interest and penalties charged to debit card holders that is included in the numerator of the sales factor pursuant to subsection (7) of this section, and the denominator of which is the taxpayer's total amount of fees, interest and penalties charged to debit card holders.
 - iii. in the case of a merchant discount related to the use of all other types of cards, the numerator of which is the amount of fees, interest and penalties charged to all other card holders that is included in the numerator of the sales factor pursuant to subsection (7) of this section, and the denominator of which is the taxpayer's total amount of fees, interest and penalties charged to all other card holders.
- (c) The taxpayer's method for sourcing each receipt from a merchant discount must be consistently applied to such receipt in all states that have adopted sourcing methods substantially similar to subsections (a) and (b) of this section.

(11) **Receipts from ATM fees.** The sales factor includes all ATM fees that are not forwarded directly to another bank.

- (a) The numerator of the sales factor includes fees charged to a cardholder for the use at an ATM of a card issued by the taxpayer if the cardholder's billing address is in this State.
- (b) The numerator of the sales factor includes fees charged to a cardholder, other than the taxpayer's cardholder, for the use of such card at an ATM owned or rented by the taxpayer, if the ATM is in this State.

(12) **Loan servicing fees.**

- (a) i. The numerator of the sales factor includes loan servicing fees derived from loans secured by real property multiplied by a fraction the numerator of which is the amount included in the numerator of the sales factor pursuant to subsection (4) of this section and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans secured by real property.
- ii. The numerator of the sales factor includes loan servicing fees derived from loans not secured by real property multiplied by a fraction the numerator of which is the amount

included in the numerator of the sales factor pursuant to subsection (5) of this section and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans not secured by real property.

- (b) In circumstances in which the taxpayer receives loan servicing fees for servicing either the secured or the unsecured loans of another, the numerator of the sales factor shall include such fees if the borrower is located in this State.

(13) Receipts from services.

The numerator of the sales factor includes receipts from services not otherwise apportioned under this section, which receipts shall be sourced in accordance with Section IV of these guidelines.

(14) Receipts from the financial institution's investment assets and activity and trading assets and activity.

- (a) Interest, dividends, net gains (but not less than zero) and other income from investment assets and activities and from trading assets and activities that are reported on the taxpayer's financial statements, call reports, or similar reports shall be included in the sales factor. Investment assets and activities and trading assets and activities include but are not limited to: investment securities; trading account assets; federal funds; securities purchased and sold under agreements to resell or repurchase; options; futures contracts; forward contracts; notional principal contracts such as swaps; equities; and foreign currency transactions. With respect to the investment and trading assets and activities described in subparagraphs i and ii of this paragraph, the sales factor shall include the amounts described in such subparagraphs.
 - i. The sales factor shall include the amount by which interest from federal funds sold and securities purchased under resale agreements exceeds interest expense on federal funds purchased and securities sold under repurchase agreements.
 - ii. The sales factor shall include the amount by which interest, dividends, gains and other income from trading assets and activities, including but not limited to assets and activities in the matched book, in the arbitrage book, and foreign currency transactions, exceed amounts paid in lieu of interest, amounts paid in lieu of dividends, and losses from such assets and activities.
- (b) The numerator of the sales factor includes interest, dividends, net gains (but not less than zero) and other income from investment assets and activities and from trading assets and activities described in paragraph (a) of this subsection that are attributable to this State.

- i. The amount of interest, dividends, net gains (but not less than zero) and other income from investment assets and activities in the investment account to be attributed to this State and included in the numerator is determined by multiplying all such income from such assets and activities by a fraction, the numerator of which is the average value of such assets which are properly assigned to a regular place of business of the taxpayer within this State and the denominator of which is the average value of all such assets.
 - ii. The amount of interest from federal funds sold and purchased and from securities purchased under resale agreements and securities sold under repurchase agreements attributable to this State and included in the numerator is determined by multiplying the amount described in subparagraph i of paragraph (a) of this subsection from such funds and such securities by a fraction, the numerator of which is the average value of federal funds sold and securities purchased under agreements to resell which are properly assigned to a regular place of business of the taxpayer within this State and the denominator of which is the average value of all such funds and such securities.
 - iii. The amount of interest, dividends, gains and other income from trading assets and activities, including but not limited to assets and activities in the matched book, in the arbitrage book and foreign currency transactions (but excluding amounts described in subparagraphs i or ii of this paragraph), attributable to this State and included in the numerator is determined by multiplying the amount described in subparagraph ii of paragraph (a) of this subsection by a fraction, the numerator of which is the average value of such trading assets which are properly assigned to a regular place of business of the taxpayer within this State and the denominator of which is the average value of all such assets.
 - iv. For purposes of this paragraph, average value shall be determined pursuant to N.C. Gen. Stat. § 105-130.4(j)(2) and (3).
- (c) In lieu of using the method set forth in paragraph (b) of this subsection, the taxpayer may elect, in order to fairly represent the business activity of the taxpayer in this State, the use of the method set forth in this paragraph.
- i. The amount of interest, dividends, net gains (but not less than zero) and other income from investment assets and activities in the investment account to be attributed to this State and included in the numerator is determined by multiplying all such income from such assets and activities by a fraction, the numerator of which is the gross income from such assets and activities which are properly assigned to a regular place of business of

the taxpayer within this State and the denominator of which is the gross income from all such assets and activities.

- ii. The amount of interest from federal funds sold and purchased and from securities purchased under resale agreements and securities sold under repurchase agreements attributable to this State and included in the numerator is determined by multiplying the amount described in subparagraph i. of paragraph (a) of this subsection from such funds and such securities by a fraction, the numerator of which is the gross income from such funds and such securities which are properly assigned to a regular place of business of the taxpayer within this State and the denominator of which is the gross income from all such funds and such securities.
- iii. The amount of interest, dividends, gains and other income from trading assets and activities, including but not limited to assets and activities in the matched book, in the arbitrage book and foreign currency transactions (but excluding amounts described in subparagraphs i. or ii. of this paragraph), attributable to this State and included in the numerator is determined by multiplying the amount described in subparagraph ii of paragraph (a) of this subsection by a fraction, the numerator of which is the gross income from such trading assets and activities which are properly assigned to a regular place of business of the taxpayer within this State and the denominator of which is the gross income from all such assets and activities.

(d) The taxpayer shall have the burden of proving that an investment asset or activity or trading asset or activity was properly assigned to a regular place of business outside of this State by demonstrating that the day-to-day decisions regarding the asset or activity occurred at a regular place of business outside this State. Where the day-to-day decisions regarding an investment asset or activity or trading asset or activity occur at more than one regular place of business and one such regular place of business is in this State and one such regular place of business is outside this State, such asset or activity shall be considered to be located at the regular place of business of the taxpayer where the investment or trading policies or guidelines with respect to the asset or activity are established. Unless the taxpayer demonstrates to the contrary, such policies and guidelines shall be presumed to be established at the commercial domicile of the taxpayer.

(15) **All other receipts.** The numerator of the sales factor includes all other receipts pursuant to the rules set forth in N.C. Gen.Stat. § 105-130.4.