

## CHAPTER 5 - CORPORATE FRANCHISE, INCOME, AND INSURANCE TAXES

### SUBCHAPTER 5A - DIVISIONAL RULES

<b>17 NCAC 05A .0101</b>	<b>LOCATION</b>
<b>17 NCAC 05A .0102</b>	<b>GENERAL PURPOSE</b>
<b>17 NCAC 05A .0103</b>	<b>DIVISIONAL ORGANIZATION</b>

*History Note:* Authority G.S. 105-114 to 105-132; 105-163.25 to 105-163.37; 143B-10; 143B-221;  
Eff. February 1, 1976;  
Repealed Eff. October 1, 1993.

### SUBCHAPTER 5B - FRANCHISE TAX

#### SECTION .0100 - GENERAL INFORMATION

<b>17 NCAC 05B .0101</b>	<b>SCOPE AND NATURE</b>
<b>17 NCAC 05B .0102</b>	<b>CORPORATION DEFINED</b>
<b>17 NCAC 05B .0103</b>	<b>PERIOD COVERED</b>

*History Note:* Authority G.S. 105-114; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.

#### **17 NCAC 05B .0104 INACTIVE CORPORATIONS**

A corporation that is inactive and without assets is subject annually to a minimum franchise tax. A return is required containing a statement of the status of the corporation. Failure to file this return and pay the minimum tax will result in suspension of the articles of incorporation or certificate of authority.

*History Note:* Authority G.S. 105-114; 105-262;  
Eff. February 1, 1976;  
Amended Eff. November 1, 1991; November 1, 1987;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

#### **17 NCAC 05B .0105 DISSOLUTION OR WITHDRAWAL OF CORPORATE RIGHTS**

Corporations are not subject to franchise tax after the end of the income year in which articles of dissolution or withdrawal are filed with the Secretary of State unless they engage in business activities not incidental to winding up their affairs. Therefore, no franchise tax is required with the income return filed for the year in which the application is filed or with any subsequent income returns that may be required in connection with winding up the affairs of the corporation.

*History Note:* Authority G.S. 105-114; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994; October 31, 1981;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

#### **17 NCAC 05B .0106 PAYMENT OF FRANCHISE TAXES**

*History Note:* Authority G.S. 105-127; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 1, 1993.

#### **17 NCAC 05B .0107 EXTENSION OF FILING DATE**

Rule 17 NCAC 5C .2004 sets out the procedure for a corporation to obtain an extension of time to file its corporate franchise and income tax return.

*History Note:* Authority G.S. 105-129; 105-262; 105-263;  
Eff. February 1, 1976;  
Amended Eff. July 1, 1999; January 1, 1994; April 1, 1991; January 1, 1978.  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05B .0108 ELECTRONIC FILING OF GENERAL BUSINESS FRANCHISE TAX RETURNS**

*History Note:* Authority G.S. 105-262;  
Eff. March 1, 2006;  
Expired Eff. September 1, 2017 pursuant to G.S. 150B-21.3A.

**SECTION .0200 - RAILROADS**

**17 NCAC 05B .0201 BASIS FOR TAXATION**  
**17 NCAC 05B .0202 DUE DATE OF THE TAX**

*History Note:* Authority G.S. 105-115; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.

**17 NCAC 05B .0203 BILLED FOR THE TAX**

*History Note:* Authority G.S. 105-115; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 1, 1993.

**SECTION .0300 - ELECTRIC: POWER: GAS: WATER AND SEWERAGE COMPANIES**

**17 NCAC 05B .0301 BASIS FOR TAXATION**  
**17 NCAC 05B .0302 DUE DATE OF THE REPORT AND TAX**  
**17 NCAC 05B .0303 FORM TO BE USED FOR FILING**  
**17 NCAC 05B .0304 SPECIAL EXEMPTION**  
**17 NCAC 05B .0305 DISTRIBUTION TO MUNICIPALITIES**

*History Note:* Authority G.S. 105-116; 105-262;  
Eff. February 1, 1976;  
Amended Eff. October 23, 1977;  
Repealed Eff. October 31, 1981.

**SECTION .0400 - PULLMAN: SLEEPING: CHAIR AND DINING CARS**

**17 NCAC 05B .0401 BASIS FOR TAXATION**  
**17 NCAC 05B .0402 DUE DATE OF THE REPORT AND TAX**

*History Note:* Authority G.S. 105-117; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.

**17 NCAC 05B .0403 FORM TO BE USED FOR FILING**

*History Note:* Authority G.S. 105-117; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994;  
Repealed Eff. December 1, 1997.

**SECTION .0500 - EXPRESS COMPANIES**

**17 NCAC 05B .0501      BASIS FOR TAXATION**  
**17 NCAC 05B .0502      DUE DATE OF THE REPORT AND TAX**

*History Note:      Authority G.S. 105-118; 105-262;*  
*Eff. February 1, 1976;*  
*Repealed Eff. October 31, 1981.*

**17 NCAC 05B .0503      FORM TO BE USED FOR FILING**

*History Note:      Authority G.S. 105-118; 105-262;*  
*Eff. February 1, 1976;*  
*Amended Eff. January 1, 1994;*  
*Repealed Eff. December 1, 1997.*

**SECTION .0600 - TELEGRAPH COMPANIES**

**17 NCAC 05B .0601      BASIS FOR TAXATION**  
**17 NCAC 05B .0602      DUE DATE OF THE REPORT AND TAX**

*History Note:      Authority G.S. 105-119; 105-262;*  
*Eff. February 1, 1976;*  
*Repealed Eff. October 31, 1981.*

**17 NCAC 05B .0603      FORM TO BE USED FOR FILING**

*History Note:      Authority G.S. 105-119; 105-262;*  
*Eff. February 1, 1976;*  
*Amended Eff. January 1, 1994;*  
*Repealed Eff. July 1, 2000.*

**SECTION .0700 - TELEPHONE COMPANIES**

**17 NCAC 05B .0701      BASIS FOR TAXATION**  
**17 NCAC 05B .0702      DUE DATE OF THE REPORT AND TAX**  
**17 NCAC 05B .0703      FORM TO BE USED FOR FILING**  
**17 NCAC 05B .0704      DISTRIBUTION TO MUNICIPALITIES**

*History Note:      Authority G.S. 105-120; 105-262;*  
*Eff. February 1, 1976;*  
*Repealed Eff. October 31, 1981.*

**SECTION .0800 - STREET TRANSPORTATION COMPANIES**

**17 NCAC 05B .0801      BASIS FOR TAXATION**  
**17 NCAC 05B .0802      DUE DATE OF THE TAX**

*History Note:      Authority G.S. 105-120.1; 105-262;*  
*Eff. February 1, 1976;*  
*Repealed Eff. October 31, 1981.*

**17 NCAC 05B .0803      CORPORATION BILLED FOR THE TAX**

*History Note:* Authority G.S. 105-120.1; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994;  
Repealed Eff. July 1, 2000.

#### **SECTION .0900 - MUTUAL BURIAL ASSOCIATION**

**17 NCAC 05B .0901 BASIS FOR TAXATION**  
**17 NCAC 05B .0902 DUE DATE OF THE TAX**

*History Note:* Authority G.S. 105-121.1; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.

**17 NCAC 05B .0903 CORPORATION BILLED FOR THE TAX**

*History Note:* Authority G.S. 105-121.1; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994;  
Repealed Eff. July 1, 2000.

#### **SECTION .1000 - GENERAL BUSINESS CORPORATIONS**

**17 NCAC 05B .1001 BASIS FOR THE TAX**  
**17 NCAC 05B .1002 FRANCHISE TAX BASES**  
**17 NCAC 05B .1003 CORPORATIONS REQUIRED TO FILE**  
**17 NCAC 05B .1004 FORMS TO BE USED FOR FILING**  
**17 NCAC 05B .1005 REPORT AND PAYMENT DUE**  
**17 NCAC 05B .1006 TAX RATE**

*History Note:* Authority G.S. 105-122; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.

#### **SECTION .1100 - CAPITAL STOCK: SURPLUS AND UNDIVIDED PROFITS BASE**

**17 NCAC 05B .1101 BASED ON THE YEAR ENDING BALANCE SHEET**  
**17 NCAC 05B .1102 SURPLUS DEFINED**  
**17 NCAC 05B .1103 ITEMS INCLUDABLE AND EXCLUDABLE**

*History Note:* Authority G.S. 105-120.2; 105-122; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.

**17 NCAC 05B .1104 EXCLUSION OF RETAINED EARNINGS BY PARENT CORPORATION**

A parent corporation may exclude any retained earnings of existing subsidiary corporations which it has capitalized or otherwise recorded on its books from the calculation of the capital stock, surplus and undivided profits base under G.S. 105-122.

*History Note:* Authority G.S. 105-122; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05B .1105 INVESTMENT IN SUBSIDIARY**

For purposes of G.S. 105-122, the net worth base shall not be reduced by the amount invested in a subsidiary.

*History Note:* Authority G.S. 105-122; 105-262;  
Eff. February 1, 1976;  
Amended Eff. July 1, 1999; January 1, 1994;  
Readopted Eff. May 1, 2018.

**17 NCAC 05B .1106      BORROWED CAPITAL TREATMENT: DEBTOR CORPORATION**  
**17 NCAC 05B .1107      BORROWED CAPITAL TREATMENT: CREDITOR CORPORATION**

*History Note:* Authority G.S. 105-122; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.

**17 NCAC 05B .1108      EXCLUSION PROVISION LIMITED TO INDEBTEDNESS OWED**

The exclusion from the net worth base of indebtedness owed that is permitted the debtor corporation and the deduction permitted the creditor corporation in G.S. 105-122 are applicable only to indebtedness owed to or due from a parent, subsidiary, or affiliated corporation. These provisions do not apply where the indebtedness is only endorsed or guaranteed.

*History Note:* Authority G.S. 105-122; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994;  
Readopted Eff. May 1, 2018.

**17 NCAC 05B .1109      EQUITY CAPITAL NOT DEDUCTIBLE**

The equity capital of a wholly owned subsidiary does not represent "indebtedness" owed to a parent corporation which the parent is entitled to deduct from its franchise tax base.

*History Note:* Authority G.S. 105-122; 105-262;  
Eff. February 1, 1976;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05B .1110      RECIPROCAL INDEBTEDNESS BETWEEN AFFILIATES**

A corporation that owes indebtedness to a parent, subsidiary, or affiliated corporation and at the same time is owed indebtedness by the same parent, subsidiary, or affiliated corporation shall net the payable and receivable for purposes of the indebtedness computation in arriving at the net worth base under G.S. 105-122. If the indebtedness is owed to one corporation and the receivable is due from another corporation, each amount shall be treated separately.

*History Note:* Authority G.S. 105-122; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994;  
Readopted Eff. May 1, 2018.

**17 NCAC 05B .1111      INDEBTEDNESS DEFINED**

*History Note:* Authority G.S. 105-122; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 1, 1993.

**17 NCAC 05B .1112      BORROWED CAPITAL DEFINED**

*History Note:* Authority G.S. 105-122; 105-262;  
Eff. February 1, 1976;  
Amended Eff. November 2, 1992;  
Repealed Eff. July 1, 2000.

**17 NCAC 05B .1113 DEDUCTION FOR QUALIFIED RECYCLING FACILITIES**  
**17 NCAC 05B .1114 HOLDING COMPANIES**

*History Note:* Authority G.S. 105-120.2; 105-122; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.

**17 NCAC 05B .1115 CASH BASIS CORPORATIONS**

*History Note:* Authority G.S. 105-122; 105-258;  
Eff. April 1, 1991;  
Expired Eff. September 1, 2017 pursuant to G.S. 150B-21.3A.

**SECTION .1200 - MULTISTATE CORPORATIONS**

**17 NCAC 05B .1201 APPORTIONMENT FORMULA**  
**17 NCAC 05B .1202 ALTERNATIVE APPORTIONMENT FORMULA**

*History Note:* Authority G.S. 105-122; 105-262;  
Eff. February 1, 1976;  
Amended Eff. October 23, 1977;  
Repealed Eff. October 31, 1981.

**SECTION .1300 - INVESTMENT IN TANGIBLE PROPERTIES IN NORTH CAROLINA BASE**

**17 NCAC 05B .1301 BASIS FOR THE INVESTMENT BASE**

*History Note:* Authority G.S. 105-122; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.

**17 NCAC 05B .1302 WHAT IS INCLUDABLE IN THE INVESTMENT BASE**

For purposes of G.S. 105-122, all tangible assets located in North Carolina shall be included in the Tangible Property Base at book value (original purchase price less reserve for depreciation permitted for income tax purposes). Typical items of tangible property would include: inventory, consigned inventories to be included by consignor, machinery and equipment, furniture and fixtures, containers, tools and supplies, land, buildings, leasehold improvements, and all other tangible assets.

*History Note:* Authority G.S. 105-122; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05B .1303 TREATMENT OF CONSTRUCTION IN PROGRESS**

Construction in progress is excluded from the tangible properties base in G.S. 105-122 only if such property is not owned by the corporation filing the return.

*History Note:* Authority G.S. 105-122; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05B .1304 CARRIER OPERATIONS PROPERTY EXEMPT FROM INVESTMENT BASE**

*History Note:* Authority G.S. 105-122; 105-262;

*Eff. February 1, 1976;*  
*Amended Eff. January 1, 1994;*  
*Repealed Eff. October 1, 1998.*

**17 NCAC 05B .1305 INDEBTEDNESS DEDUCTION**

*History Note: Authority G.S. 105-122; 105-262;*  
*Eff. February 1, 1976;*  
*Repealed Eff. October 31, 1981.*

**17 NCAC 05B .1306 REFINANCING OF A LOAN**

*History Note: Authority G.S. 105-122; 105-262;*  
*Eff. February 1, 1976;*  
*Amended Eff. January 1, 1994; October 31, 1981;*  
*Expired Eff. September 1, 2017 pursuant to G.S. 150B-21.3A.*

**17 NCAC 05B .1307 POLLUTION ABATEMENT FACILITIES**  
**17 NCAC 05B .1308 DEDUCTION FOR QUALIFIED RECYCLING FACILITIES**

*History Note: Authority G.S. 105-122; 105-262;*  
*Eff. February 1, 1976;*  
*Repealed Eff. October 31, 1981.*

**17 NCAC 05B .1309 DETERMINATION OF INCLUSION BY DEPRECIATION**

When two or more corporations are in doubt as to which should include property in the investment in tangible property base pursuant to G.S. 105-122, such property shall be included by the corporation allowed depreciation under the Internal Revenue Code.

*History Note: Authority G.S. 105-122; 105-262;*  
*Eff. February 1, 1976;*  
*Amended Eff. January 1, 1994;*  
*Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

**17 NCAC 05B .1310 NO LIMITATION ON HOLDING COMPANIES**

*History Note: Authority G.S. 105-120.2; 105-262;*  
*Eff. February 1, 1976;*  
*Repealed Eff. October 1, 1993.*

**SECTION .1400 - APPRAISED VALUATION OF TANGIBLE AND INTANGIBLE PROPERTY BASE**

**17 NCAC 05B .1401 BASIS FOR TANGIBLE PROPERTY**

*History Note: Authority G.S. 105-122; 105-262;*  
*Eff. February 1, 1976;*  
*Repealed Eff. October 31, 1981.*

**17 NCAC 05B .1402 CARRIER OPERATIONS APPRAISED PROPERTY EXEMPT**

*History Note: Authority G.S. 105-122; 105-262;*  
*Eff. February 1, 1976;*  
*Amended Eff. January 1, 1994;*  
*Repealed Eff. May 1, 1998.*



**SECTION .1700 - CORPORATIONS CONDITIONALLY OR PARTIALLY EXEMPT**

**17 NCAC 05B .1701      NON-PROFIT ORGANIZATIONS**  
**17 NCAC 05B .1702      CORPORATIONS FULLY EXEMPT**

*History Note:*     *Authority G.S. 105-125; 105-262;*  
                          *Eff. February 1, 1976;*  
                          *Repealed Eff. October 31, 1981.*

**17 NCAC 05B .1703      FRANCHISE MOTOR CARRIERS**

*History Note:*     *Authority G.S. 105-122; 105-262;*  
                          *Eff. February 1, 1976;*  
                          *Amended Eff. January 1, 1994;*  
                          *Repealed Eff. May 1, 1998.*

**17 NCAC 05B .1704      REGULATED INVESTMENT COMPANIES**

*History Note:*     *Authority G.S. 105-125; 105-262;*  
                          *Eff. February 1, 1976;*  
                          *Repealed Eff. October 31, 1981.*

**SUBCHAPTER 05C - CORPORATE INCOME TAX**

**SECTION .0100 - CORPORATIONS SUBJECT TO THE TAX: TAX RATE AND ALLOCATION**

**17 NCAC 05C .0101      DOMESTIC AND FOREIGN CORPORATIONS REQUIRED TO FILE**

- (a) A foreign corporation operating in North Carolina may be liable for income tax even if it is not required to obtain a certificate of authority to do business in North Carolina.
- (b) Even for a year in which a domestic corporation or a foreign corporation with a certificate of authority to do business in North Carolina conducted no business activity or did not earn any net income in the State, it must file an income tax return. Entities treated as corporations for federal income tax purposes are also subject to this requirement.

*History Note:*     *Authority G.S. 105-130.3; 105-130.4; 105-130.16; 105-262;*  
                          *Eff. February 1, 1976;*  
                          *Amended Eff. January 1, 1994;*  
                          *Readopted Eff. May 1, 2018.*

**17 NCAC 05C .0102      DOING BUSINESS DEFINED**

- (a) For income tax purposes, the term "doing business" means the operation of any business enterprise or activity in North Carolina for economic gain, including, but not limited to, the following:
- (1) the maintenance of an office or other place of business in North Carolina;
  - (2) the maintenance in North Carolina of an inventory of merchandise or material for sale, distribution or manufacture, regardless of whether kept on the premises of the taxpayer or in a public or rented warehouse;
  - (3) the selling or distributing of merchandise to customers in North Carolina directly from a company-owned or operated vehicle when title to the merchandise is transferred from the seller or distributor to the customer at the time of the sale or distribution;
  - (4) the rendering of a service to clients or customers in North Carolina by agents or employees of a foreign corporation;
  - (5) the owning, renting, or operating of business or income-producing property in North Carolina including, but not limited to, the following:
    - (A) Realty;
    - (B) Tangible personal property;

(C) Trademarks, tradenames, franchise rights, computer programs, copyrights, patented processes, licenses.

(b) Corporations who are partners in a partnership or joint venture operating in North Carolina are considered to be "doing business".

(c) "Doing business" by an interstate motor carrier is defined as the performance of any of the following business activities in North Carolina:

- (1) The maintenance of an office in the State;
- (2) The operation of a terminal or other place of business in the State;
- (3) Having an employee working out of the office or terminal of another company;
- (4) Dropping off or gathering up shipments in the State.

*History Note:* Authority G.S. 105-130.3; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994; November 2, 1992;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

### **17 NCAC 05C .0103 CORPORATIONS OPERATING IN INTERSTATE COMMERCE**

The fact that a foreign corporation's activities or operations in North Carolina are a part of its over-all interstate business does not exempt the corporation from income tax liability. A corporation doing business in North Carolina in any of the capacities outlined in Rule .0102 ("Doing Business" Defined) is subject to income tax even if its only operations in this state are a part of its interstate business. A foreign corporation not domesticated in North Carolina whose only activity in this state is the solicitation of sales of tangible personal property by either resident or nonresident salesmen is not required to file income tax returns. However, if such a corporation maintains an office or other place of business in North Carolina, or if it owns business property in this state, it is subject to the tax.

*History Note:* Authority G.S. 105-130.3; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1995; January 1, 1994;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

- 17 NCAC 05C .0104 TAX RATE AND BASIS FOR THE TAX**
- 17 NCAC 05C .0105 CORPORATIONS REQUIRED TO ALLOCATE INCOME**
- 17 NCAC 05C .0106 WHEN IN DOUBT AS TO LIABILITY**
- 17 NCAC 05C .0107 TAX FORMS MAILED TO TAXPAYER**
- 17 NCAC 05C .0108 DUE DATE OF RETURN**

*History Note:* Authority G.S. 105-130.3; 105-130.4; 105-130.17; 105-130.22 through 105-130.24; 105-262;  
Eff. February 1, 1976;  
Amended Eff. December 23, 1979; October 23, 1977;  
Repealed Eff. October 31, 1981.

### **SECTION .0200 - TAX CREDIT FOR DWELLING UNITS FOR HANDICAPPED PERSONS**

- 17 NCAC 05C .0201 PRELIMINARY STATEMENT**
- 17 NCAC 05C .0202 AMOUNT OF CREDIT ALLOWABLE**
- 17 NCAC 05C .0203 BUILDING CODE AND OTHER REQUIREMENTS**

*History Note:* Authority G.S. 105-130.22; 105-262;  
Eff. February 1, 1976;  
Amended Eff. October 4, 1979;  
Repealed Eff. October 31, 1981.

### **SECTION .0300 - COMPUTATION OF NET INCOME**

- 17 NCAC 05C .0301 PRELIMINARY STATEMENT**

**17 NCAC 05C .0302      ADJUSTMENTS TO FEDERAL TAXABLE INCOME**  
**17 NCAC 05C .0303      MISCELLANEOUS**

*History Note:      Authority G.S. 105-130.3; 105-130.5; 105-262;*  
*Eff. February 1, 1976;*  
*Amended Eff. January 1, 1980; October 4, 1979; October 23, 1977;*  
*Repealed Eff. October 31, 1981.*

**17 NCAC 05C .0304      ATTRIBUTION OF EXPENSES TO NONTAXABLE INCOME**

(a) Direct Expenses - All expenses directly connected with the production of income which is not subject to tax in this State shall be used to compute the net amount of such untaxed income.

(b) Interest Expenses - When a corporation earns income which is not taxed by this State (see examples), or holds property that does or will produce untaxed income, and incurs interest expense which is not specifically related to any particular income or property, it shall attribute a portion of the interest expense to such untaxed income and property in determining taxable income reported to this State. The formula used for computing the amount of interest expense to be attributed to untaxed income and property is as follows:

- (1) Value of assets:
  - (A) Value of the tax return balance sheet of assets which produce or which would produce untaxed income; \*
  - (B) Value of all assets on the tax return balance sheet; \*\*
  - (C) Determine the ratio or percentage of Subparagraphs (b)(1)(A) to (B) of this Rule.
- (2) Income/Profits:
  - (A) Gross untaxed income;
  - (B) Total gross profits;
  - (C) Determine the ratio or percentage of Subparagraphs (b)(2)(A) to (B) of this Rule.
- (3) Total of the ratios or percentages determined in Subparagraphs (b)(1) and (2) of this Rule;
- (4) Divide the total of Subparagraph (b)(3) of this Rule by two;
- (5) Apply average percentage determined in Subparagraph (b)(4) of this Rule to the total interest expense on the return filed in this state.

(c) Examples of Untaxed Income are:

- (1) Dividend income classified as nonapportionable (G.S. 105-130.4);
- (2) Dividend income excludable by statute (G.S. 105-130.5);
- (3) Interest income classified as nonapportionable (G.S. 105-130.4);
- (4) Interest income earned on United States obligations and state of North Carolina obligations;
- (5) Other nonapportionable income or exempt income.

(d) Expenses Connected with Interest Income from United States Obligations - Under G.S. 105-130.5(b)(1), interest income from obligations of the United States or its possessions is excludable from North Carolina taxable income to the extent such income is included in federal taxable income. Expenses incurred in producing the exempt income must be determined and subtracted from the gross amount earned during a taxable period before the deduction is made in computing the state taxable income. In the computation of expenses related to income from United States obligations, the formula described in Paragraph (b) of this Rule may be used with respect to interest expense.

(e) Other Expenses Attributed to Nontaxable Income and to Nonapportionable Income and Property - In the determination of expenses other than interest expense attributed to untaxed income, the procedure set forth in the Federal Code for determining expenses related to foreign source income generally referred to as stewardship and supportive expenses may be used to determine the expenses allocated to untaxed income and property producing or which would produce untaxed income. Alternatively, an income formula as outlined in Paragraph (b)(2) of this Rule relating to interest expenses may be used to determine the amount of supportive function expenses attributable to untaxed income. In the determination of "supportive function expenses", direct expenses incurred exclusively in a specific identifiable taxable or nontaxable activity shall be determined and excluded before application of the attribution percentage to expenses. If direct expenses are determinable for a particular activity resulting in an accurate computation of the net income or loss from such activity, the values of this activity shall be removed as elements of the ratio when computing the attribution percentage.

Note: \* When the equity method of accounting is used, the increase or decrease in value as a result of such accounting method may be excluded from this value.

Note: \*\* Equity included in this value may be excluded and the reserve for depreciation reflected on the balance sheet may be restored to the asset value.

*History Note:* Authority G.S. 105-130.4; 105-130.5; 105-262;  
Eff. April 1, 1991;  
Amended Eff. August 1, 2005; January 1, 2005; January 1, 1994;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

## **SECTION .0400 - INTEREST INCOME ON GOVERNMENT OBLIGATIONS**

### **17 NCAC 05C .0401 NORTH CAROLINA OBLIGATIONS**

Net interest income received by a corporation on obligations of the State of North Carolina and any of its cities, towns or counties is exempt from income taxes imposed by this state.

*History Note:* Authority G.S. 105-130.5; 105-262;  
Eff. February 1, 1976;  
Amended Eff. April 1, 1991;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

### **17 NCAC 05C .0402 OBLIGATIONS OF OTHER STATES**

Net interest income earned by a corporation on its investments in obligations issued by states and their political subdivisions other than the State of North Carolina, represents taxable income and is subject to this state's income tax.

*History Note:* Authority G.S. 105-130.5; 105-262;  
Eff. February 1, 1976;  
Amended Eff. April 1, 1991;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

### **17 NCAC 05C .0403 U.S. OBLIGATIONS**

(a) Net interest income earned on bonds, notes, or other obligations of the United States or its possessions is exempt from income taxation in this State so long as interest on obligations of the State of North Carolina and its political subdivisions is exempt from income taxes imposed by the United States. For the interest income to be deductible, the obligation shall be in writing, bear interest, be a binding promise by the United States to pay specific amounts at specific dates, and be specifically authorized by Congress.

(b) Net interest from obligations that are backed, insured, or guaranteed by the United States, but are not direct obligations of the United States Government, shall not be deductible.

*History Note:* Authority G.S. 105-130.5; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1995; April 1, 1991; October 23, 1977;  
Readopted Eff. May 1, 2018.

### **17 NCAC 05C .0404 SALES OR EXCHANGES**

(a) Gain or loss realized on the sale or other disposition of any type of obligation of the United States or its possessions, the State of North Carolina (not exempted by the specific obligation), or its political subdivisions, any other state or its political subdivisions, or of any other government is a taxable transaction and must be included in the computation of a corporation's state taxable income.

(b) Gain or loss realized on the sale or other disposition of obligations is not included in taxable income if North Carolina law under which obligations were issued specifically exempts the gain from taxation.

*History Note:* Authority G.S. 105-130.5; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1995;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05C .0405 OBLIGATIONS OF FEDERAL NATIONAL MORTGAGE ASSOCIATION**

Interest income or other income realized on obligations of Federal National Mortgage Association is taxable income since the obligations are not those of the United States.

*History Note: Authority G.S. 105-130.5; 105-262;  
Eff. October 23, 1977;  
Amended Eff. January 1, 1994;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

**17 NCAC 05C .0406 MORTGAGE BACKED CERTIFICATE GUARANTEED BY GNMA**

Interest paid by the issuer to the holder of a mortgage backed certificate guaranteed by Government National Mortgage Association (GNMA) is not income from an obligation of the United States and is taxable.

*History Note: Authority G.S. 105-130.5; 105-262;  
Eff. October 23, 1977;  
Amended Eff. January 1, 1994;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

**17 NCAC 05C .0407 REPURCHASE AGREEMENTS**

Income attributable to or received from repurchase agreements of U.S. government securities, an agreement to repurchase securities at an agreed price and date, is not considered income derived directly from federal obligations and is taxable income.

*History Note: Authority G.S. 105-130.5; 105-262;  
Eff. November 2, 1992;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

**SECTION .0500 - ALLOCATION AND APPORTIONMENT PROCEDURES**

**17 NCAC 05C .0501 PRELIMINARY STATEMENT**

**17 NCAC 05C .0502 REPORTING NET INCOME OR LOSS TO NORTH CAROLINA**

*History Note: Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.*

**SECTION .0600 - TAXABLE IN ANOTHER STATE**

**17 NCAC 05C .0601 PRELIMINARY STATEMENT**

A taxpayer must have income from business activity taxable by this state and at least one other state, to allocate and apportion income. Income from business activity includes apportionable or nonapportionable income. Thus, if a taxpayer has nonapportionable income taxable by one state and apportionable income taxable by another state, the taxpayer's income shall be allocated and apportioned in accordance with G.S. 105-130.4. Where a corporation is not taxable in another state on its apportionable income but is taxable in another state only because of nonapportionable income, all apportionable income shall be attributed to this state.

*History Note: Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 2005;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

**17 NCAC 05C .0602 DEFINITION OF TAXPAYER**

The word "taxpayer" includes any corporation subject to the tax imposed by Article 4 of Chapter 105 of the General Statutes.

*History Note: Authority G.S. 105-130.4; 105-262;*

*Eff. February 1, 1976;*  
*Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

### **17 NCAC 05C .0603      IN GENERAL**

*History Note:      Authority G.S. 105-130.4; 105-262;*  
*Eff. February 1, 1976;*  
*Repealed Eff. October 1, 1993.*

### **17 NCAC 05C .0604      WHEN A TAXPAYER IS SUBJECT TO TAX**

(a) If the taxpayer voluntarily files and pays an income tax to a state other than North Carolina when not required to do so by the laws of that state or pays a minimal fee for qualification, organization or for the privilege of doing business in that state, but does not actually engage in business activities in that state, or does actually engage in some activity, not sufficient for nexus, and the minimum tax bears no relation to the corporation's activities within such state, the taxpayer is not subject to tax within that state and is therefore not taxable in another state. The filing of a unitary-combined return in another state with other related corporations does not standing alone constitute business activity for purposes of determining if a corporation is subject to income tax in this State is allowed to allocate and apportion income.

(b) In some states other types of taxes may be imposed as a substitute for an income tax. Therefore, only income tax or any tax measured by net income, shall be considered in determining whether the taxpayer is taxable in another state.

*History Note:      Authority G.S. 105-130.4; 105-262;*  
*Eff. February 1, 1976;*  
*Amended Eff. January 1, 1994; November 2, 1992; October 31, 1981;*  
*Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

### **17 NCAC 05C .0605      WHEN A STATE HAS JURISDICTION**

In the case of any "state," as defined in G.S. 105-130.4, other than a state of the United States or political subdivision of such state, the determination of whether such "state" has jurisdiction to subject the taxpayer to a net income tax shall be made as though the jurisdictional standards applicable to a state of the United States applied in that "state." If jurisdiction is otherwise present, such "state" is not considered as without jurisdiction by reason of the provisions of a treaty between that state and the United States.

*History Note:      Authority G.S. 105-130.4; 105-262;*  
*Eff. February 1, 1976;*  
*Amended Eff. January 1, 1994; October 31, 1981;*  
*Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

## **SECTION .0700 - APPORTIONABLE AND NONAPPORTIONABLE INCOME**

### **17 NCAC 05C .0701      DIVISION OF INCOME: IN GENERAL**

(a) When a taxpayer has income from sources within this state as well as income from sources outside this state, the division of income and the resulting determination of the portion of the taxpayer's entire net income which has its source in this state shall be determined pursuant to the allocation and apportionment provisions set forth in G.S. 105-130.4 and these Rules. The taxpayer shall determine which portion of its entire net income constitutes "apportionable income" and which portion constitutes "nonapportionable income". The various items of nonapportionable income shall be directly allocated to specific jurisdictions pursuant to the provisions of Subsections (d) to (h) of G.S. 105-130.4. The apportionable income of the taxpayer other than public utilities and excluded corporations shall be divided between the jurisdictions in which the business is conducted pursuant to the property, payroll and sales apportionment factors set forth in Subsections (i) to (l) of G.S. 105-130.4. The sum of the items of nonapportionable income directly allocated to this state, plus the amount of apportionable income attributable to this state by the apportionment formula shall constitute the amount of the taxpayer's entire net income which is subject to tax under the income tax laws of this state.

(b) The taxpayer shall classify income as apportionable or nonapportionable income on a consistent basis. In the event the taxpayer is not consistent in reporting, it shall disclose in its return to this state the nature and extent of the inconsistency.

(c) The word "apportionment" refers to the division of net income between jurisdictions by the use of a formula containing apportionment factors, and the word "allocation" refers to the assignment of net income to a particular jurisdiction.

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 2005; January 1, 1994;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

#### **17 NCAC 05C .0702 BUSINESS AND NONBUSINESS INCOME DEFINED**

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994;  
Repealed Eff. July 1, 2000.

#### **17 NCAC 05C .0703 BUSINESS AND NONBUSINESS INCOME**

*History Note:* Authority G.S. 105-130.4; 105-262.  
Eff. February 1, 1976;  
Amended Eff. August 1, 2002; July 1, 2000; July 1, 1999; January 1, 1994; April 1, 1991; October 31, 1981;  
Repealed Eff. August 1, 2003.

#### **17 NCAC 05C .0704 PRORATION OF DEDUCTIONS**

Any allowable deduction that is applicable both to apportionable and nonapportionable income or to more than one "trade or business" of the taxpayer shall be prorated to those classes of income or trades or businesses in determining income subject to tax. The taxpayer shall be consistent in the proration of such deduction or deductions in filing returns under these Rules.

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 2005; January 1, 1994;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

### **SECTION .0800 - PROPERTY FACTOR**

#### **17 NCAC 05C .0801 IN GENERAL**

(a) The property factor as provided in G.S. 105-130.4 shall include all real and tangible personal property owned or rented and used during the income year to produce apportionable income. The term "real and tangible personal property" includes land, buildings, machinery, stocks of goods, equipment, and other real and tangible personal property used in connection with the production of apportionable income but does not include coin or currency.

(b) Property used in connection with the production of nonapportionable income that is allocated in accordance with Subsection (c) to (h) of G.S. 105-130.4 shall be excluded from the factor.

(c) Property used in connection with the production of both apportionable and nonapportionable income shall be included in the factor only to the extent the property was used in connection with the production of apportionable income.

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 2005; January 1, 1994;  
Readopted Eff. May 1, 2018.

#### **17 NCAC 05C .0802 PROPERTY USED FOR THE PRODUCTION OF APPORTIONABLE INCOME**

Property shall be included in the property factor if it is actually used during the income year for the production of apportionable income. Property held as reserves or standby facilities or property held as a reserve source of materials shall be included in the factor. For example, a plant temporarily idle or raw material reserves not currently being processed are includible in the factor. Property or equipment under construction during the income year (except inventoriable goods in process) shall be excluded from the factor until such property is actually used for the production of apportionable income. If

the property is partially used for the production of apportionable income while under construction, the value of the property to the extent used shall be included in the property factor.

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 2005;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

#### **17 NCAC 05C .0803 CONSISTENCY IN REPORTING**

The taxpayer shall be consistent in the valuation of property and in excluding or including property in the property factor in filing returns with this state. In the event the taxpayer is not consistent in its reporting, it shall disclose in its return to this state the nature and extent of the inconsistency.

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

#### **17 NCAC 05C .0804 NUMERATOR**

(a) Property in transit between locations of the taxpayer to which it belongs shall be considered to be at the destination for purposes of the property factor. Property in transit between a buyer and seller which is included by a taxpayer in the denominator of its property factor in accordance with its regular accounting practices shall be included in the numerator according to the state of destination.

(b) The value of mobile or movable property such as construction equipment, trucks or leased electronic equipment which are located within and without this state during the income year shall be determined for purposes of the numerator of the factor 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.

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

#### **17 NCAC 05C .0805 VALUATION OF OWNED PROPERTY**

(a) In determining the property factor in G.S. 105-130.4, property owned by the taxpayer shall be valued at its original cost:

- (1) "Original cost" of property which has a basis other than zero for federal income tax purposes equals the basis of the property for federal income tax purposes at the time of acquisition by the taxpayer and adjusted by subsequent capital additions or improvements thereto and partial disposition thereof, by reason of sale, exchange, abandonment, or any other type of disposition.
- (2) "Original cost" of property which has a zero basis for federal income tax purposes shall equal the taxpayer's actual cost of the property at the time of acquisition; provided, however, if the actual cost is unknown, the "original cost" shall equal the fair market value of the property, or, at the option of the taxpayer, eight times the net annual rental rate as described in G.S. 105-130.4(j)(2). The valuation method chosen by the taxpayer must be used consistently thereafter.

(b) Inventory of stock of goods shall be included in the factor in accordance with the valuation method used for federal income tax purposes.

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

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. December 1, 1994; January 1, 1994; October 31, 1981;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

#### **17 NCAC 05C .0806 RENTED PROPERTY**

**17 NCAC 05C .0807 AVERAGING PROPERTY VALUES**

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.

**SECTION .0900 - PAYROLL FACTOR**

**17 NCAC 05C .0901 IN GENERAL**

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. November 1, 1993.

**17 NCAC 05C .0902 PAYROLL ACCOUNTING METHOD**

(a) The total amount "paid" to employees is determined upon the basis of the taxpayer's accounting method. If the taxpayer has adopted the accrual method of accounting, all compensation properly accrued shall be deemed to have been paid. Notwithstanding the taxpayer's method of accounting, at the election of the taxpayer, compensation paid to employees may be included in the payroll factor by use of the cash method if the taxpayer is required to report such compensation under such method for unemployment compensation purposes.

(b) The taxpayer shall be consistent in the treatment of compensation paid in filing returns with this state. In the event the taxpayer is not consistent in its reporting it shall disclose in its return to this state the nature and extent of the inconsistency.

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05C .0903 COMPENSATION**

Payments made to an independent contractor or any other person not classifiable as an employee are excluded from the term "compensation" for purposes of G.S. 105-130.4. Only amounts paid directly to employees are included in the payroll factor. Amounts considered paid directly include the value of board, rent, housing, lodging and other benefits or services furnished to employees by the taxpayer in return for personal services provided that such amounts constitute income to the recipient under the Federal Internal Revenue Code. In the case of employees not subject to the Federal Internal Revenue Code, e.g., those employed in foreign countries, the determination of whether such benefits or services constitute income to the employees shall be made as though such employees were subject to the Federal Internal Revenue Code.

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05C .0904 THE TERM EMPLOYEE**

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. November 1, 1993.

**17 NCAC 05C .0905 INCLUDE IN PAYROLL FACTOR**

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.

**17 NCAC 05C .0906 DENOMINATOR OF PAYROLL FACTOR**

Except for compensation paid to general executive officers and compensation paid in connection with nonapportionable income the denominator of the payroll factor is the total compensation paid everywhere during the income year. Accordingly, compensation paid to employees whose services are performed entirely in a state where the taxpayer is exempt from taxation, for example, by Public Law 86-272, is included in the denominator of the payroll factor.

Note: A taxpayer has employees in its state of legal domicile (State A) and is taxable in State B. In addition the taxpayer has other employees whose services are performed entirely in State C where the taxpayer is exempt from taxation by Public Law 86-272. As to these latter employees, the compensation will be assigned to State C where their services are performed (i.e. included in the denominator only of the payroll factor) even though the taxpayer is not taxable in State C.

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 2005; October 31, 1981;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

#### **17 NCAC 05C .0907 NUMERATOR OF PAYROLL FACTOR**

Except for compensation paid to general executive officers and compensation paid in connection with nonapportionable income, for purposes of G.S. 105-130.4, the numerator of the payroll factor is the total amount paid in this State during the tax period by the taxpayer for compensation. In determining the payroll factor, information used to file federal forms 941 and the North Carolina Tax and Wage Reports may be used if the amounts can be reconciled to the amounts used for the payroll factor. If compensation paid to employees is included in the payroll factor by use of the cash method of accounting or if the taxpayer is required to report such compensation under such method for unemployment compensation purposes, it shall be presumed that the total wages reported by the taxpayer to this State for unemployment compensation purposes constitutes compensation paid in this State except for compensation excluded under G.S. 105-130.4(k). The presumption may be overcome by satisfactory evidence that an employee's compensation is not reportable to this State for unemployment compensation purposes.

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 2005; January 1, 1994; October 31, 1981;  
Readopted Eff. May 1, 2018.

#### **17 NCAC 05C .0908 CORPORATIONS UTILIZING COMMON PAYMASTER**

(a) A parent corporation or any corporation serving as common paymaster for payroll purposes shall eliminate all payroll amounts paid on behalf of controlled members for which it has charged such member the exact cost and which does not meet the definition of compensation insofar as the common paymaster is concerned from the numerator and denominator of its payroll factor computation. The numerator and denominator of the payroll factor shall be determined in accordance with G.S. 105-130.4 after elimination of the described amounts.

(b) A subsidiary or otherwise controlled corporation, which is a member of or participant in a common paymaster plan for payroll purposes, shall include in its numerator and denominator of the payroll factor computation amounts paid to its parent corporation or to another corporation of the controlled group as reimbursement in whatever form and by whatever label for employee's compensation as defined. The amounts paid by the subsidiary or controlled corporation includable in the numerator and the denominator of the payroll factor shall be determined in accordance with G.S. 105-130.4.

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. November 1, 1991;  
Amended Eff. January 1, 1994;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

### **SECTION .1000 - SALES FACTOR**

#### **17 NCAC 05C .1001 SALES MADE IN GENERAL BUSINESS OPERATIONS**

For purposes of G.S. 105-130.4, 'sales' by a taxpayer whose business activity consists of manufacturing and selling or purchasing and reselling goods or products includes all gross receipts from the sales of such goods or products (or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year) held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business. Gross receipts for this

purpose means gross sales, less returns and allowances, and includes all interest income, service charges, carrying charges or time-price differential charges incidental to such sales. Federal and state excise taxes (including sales taxes) shall be included as part of such receipts if such taxes are passed on to the buyer or included as part of the selling price of the product.

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

#### **17 NCAC 05C .1002 SALES INCIDENTAL TO GENERAL BUSINESS OPERATIONS**

(a) The term "sales" also includes gross receipts derived by a taxpayer from business transactions or activities which are incidental to its principal business activity and which are includible in apportionable income. However, substantial amounts of gross receipts arising from an incidental or occasional sale of a fixed asset used in connection with the taxpayer's regular trade or business will be excluded from the sales factor since such sales constitute a "casual sale" of property and the inclusion of such gross receipts will not fairly apportion to this state the income derived by the taxpayer from its business activity in this state. Gross receipts from casual sales are considered substantial if they cause the sales factor to be distorted. For example, gross receipts from the sale of a factory or plant will be excluded from the sales factor.

(b) In including or excluding gross receipts, the taxpayer shall be consistent in the treatment of such gross receipts in filing returns with this state. In the event the taxpayer is not consistent in its reporting, it shall disclose in its return to this state the nature and extent of the inconsistency.

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 2005;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

#### **17 NCAC 05C .1003 SALES MADE IN OTHER TYPE OF BUSINESS ACTIVITY**

As applied to a taxpayer engaged in business activity other than the manufacturing and selling or purchasing and reselling of property, "sales" includes the gross receipts as defined in Rule .1001 of this Section (Sales Made In General Business Operations):

- (1) If the business activity consists of providing services; such as the operation of an advertising agency, or the performance of equipment service contracts or research and development contracts, "sales" includes the gross receipts from the performance of such services including fees, commissions, and similar items.
- (2) In the case of cost plus fixed fee contracts, such as the operation of a government-owned plant for a fee, gross receipts includes the entire reimbursed cost, plus the fee.
- (3) If the business activity is the renting of real or tangible personal property, "sales" includes the gross receipts from the rental, lease, or licensing the use of the property.
- (4) If the business activity is the sale, assignment, or licensing of intangible personal property such as patents and copyrights, "sales" includes the gross receipts therefrom.

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

#### **17 NCAC 05C .1004 NUMERATOR**

The numerator of the sales factor will include the gross receipts from sales which are attributable to this state, and includes all interest income, service charges, carrying charges, or time-price differential charges incidental to such sales regardless of the place where the accounting records are maintained or the location of the contract or other evidence of indebtedness.

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. October 31, 1981;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05C .1005 WHAT SALES OF TANGIBLE PERSONAL PROPERTY ARE IN THIS STATE**

- (a) Gross receipts from the sales of tangible personal property are in this state if the property is delivered or shipped to a purchaser within this state regardless of the f.o.b. point or other conditions of sale.
- (b) Property shall be deemed to be delivered or shipped to a purchaser within this state if the recipient is located in this state, even though the property is ordered from outside this state.
- (c) Property is delivered or shipped to a purchaser within this state if the shipment terminates in this state, even though the property is subsequently transferred by the purchaser to another state.
- (d) The term "purchaser within this state" shall include the ultimate recipient of the property if the taxpayer in this state, at the designation of the purchaser, delivers to or has the property shipped to the ultimate recipient within this state.
- (e) When property being shipped by a seller from the state of origin to consignee in another state is diverted while enroute to a purchaser in this state the sales are in this state.

*History Note: Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. October 31, 1981;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

**17 NCAC 05C .1006 SALES FACTOR: SALES TO UNITED STATES GOVERNMENT**

- (a) For the purposes of G.S. 105-130.4, gross receipts from the sales of tangible personal property to the United States Government are in this state if the property is shipped to or received or accepted by the United States Government in this state. For the purpose of this Rule, only sales for which the United States Government makes direct payment to the seller pursuant to the terms of its contract constitute sales to the United States Government. Thus, sales by a subcontractor to the prime contractor, the party to the contract with the United States Government, do not constitute sales to the United States Government.
- (b) When the United States Government is the purchaser of property which remains in the possession of the taxpayer in this state for further processing under another contract, or for other reasons, "shipment" is deemed to be made at the time of acceptance by the United States Government.

*History Note: Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994; October 31, 1981;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

**17 NCAC 05C .1007 NUMERATOR: OTHER RECEIPTS CONSTITUTING BUSINESS INCOME**

*History Note: Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.*

**SECTION .1100 - PUBLIC UTILITIES AND EXCLUDED CORPORATIONS APPORTIONMENT FACTORS**

- 17 NCAC 05C .1101 RAILROAD COMPANIES**
- 17 NCAC 05C .1102 TELEPHONE COMPANIES**
- 17 NCAC 05C .1103 MOTOR CARRIERS OF PROPERTY AND/OR PASSENGERS**
- 17 NCAC 05C .1104 TELEGRAPH COMPANIES**
- 17 NCAC 05C .1105 EXCLUDED CORPORATIONS**

*History Note: Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.*

**SECTION .1200 - DEDUCTION OF CONTRIBUTIONS**

- 17 NCAC 05C .1201 PRELIMINARY STATEMENT**
- 17 NCAC 05C .1202 CHARITABLE CONTRIBUTIONS DEFINED AND QUALIFIED DONEES**

<b>17 NCAC 05C .1203</b>	<b>CONTRIBUTIONS LIMITED TO FIVE PERCENT OF NET INCOME</b>
<b>17 NCAC 05C .1204</b>	<b>CONTRIBUTIONS FULLY DEDUCTIBLE</b>
<b>17 NCAC 05C .1205</b>	<b>CONTRIBUTIONS BY CORPORATIONS ALLOCATING NET INCOME</b>
<b>17 NCAC 05C .1206</b>	<b>CONTRIBUTIONS CARRY-OVER UNALLOWABLE</b>

*History Note:* Authority G.S. 105-130.9; 105-202; 105-262;  
 Eff. February 1, 1976;  
 Repealed Eff. October 31, 1981.

**SECTION .1300 - RAPID AMORTIZATION OF AIR OR WATER POLLUTION ABATEMENT FACILITIES**

<b>17 NCAC 05C .1301</b>	<b>AMORTIZATION OVER 60 MONTH PERIOD</b>
<b>17 NCAC 05C .1302</b>	<b>CERTIFICATION OF FACILITIES REQUIRED</b>

*History Note:* Authority G.S. 105-130.10; 105-262;  
 Eff. February 1, 1976;  
 Repealed Eff. October 31, 1981.

**SECTION .1400 - AMORTIZATION OF BOND PREMIUMS**

**17 NCAC 05C .1401 PRELIMINARY STATEMENT**

If a corporation purchases a bond at more than its face value, the amount of premium paid may be amortized over the life of the bond. However, the allowance of a deduction against net income for amortization of the premium paid depends upon the type of bond purchased by the corporation. For example:

- (1) Amortization of premiums on tax-exempt bonds by a corporation is mandatory with no deduction allowed in computing state net income.
- (2) A corporation may at its option amortize the amount of premiums paid on taxable bonds over the life of the bonds. If the premium is not amortized by the corporation, it will constitute part of the basis of the bond in determining gain or loss at maturity of sale.
- (3) For state income tax purposes, obligations of the United States or its possessions and obligations of the State of North Carolina or any of its subdivisions are tax-exempt. Interest income received by a corporation on such obligations is not taxable; however, a corporation must include in its computation of state net income any gain or loss realized on the disposal of such obligations.
- (4) Premiums paid on all bonds acquired prior to January 1, 1963 cannot be amortized but constitute a part of the cost basis of the bonds in determining gain or loss when the bonds are sold.

*History Note:* Authority G.S. 105-130.5; 105-262;  
 Eff. February 1, 1976;  
 Amended Eff. January 1, 1994;  
 Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05C .1402 TAX-EXEMPT BONDS**

The amount of premium paid upon the purchase of a tax-exempt bond is amortized over the life of the bond. Amortization for the taxable year is accomplished by reducing the original cost of the bond by a portion of the premium paid, with no deduction against net income for the year. Therefore, when the bond is sold or otherwise disposed of, the basis for determining gain or loss will always be original cost less the amount of premium amortized for book purposes through the year of disposal.

*History Note:* Authority G.S. 105-130.5; 105-262;  
 Eff. February 1, 1976;  
 Amended Eff. October 31, 1981;  
 Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05C .1403 TAXABLE BONDS**

A portion of the premium paid upon the purchase of a taxable bond may be deducted in the taxable year only if an adjustment is made to the basis of the bond. If a taxpayer elects to amortize the premium, the basis for determining gain or loss will

always be original cost less the amount of premium amortized and deducted in its tax returns through the year of disposal. Otherwise, the basis of a taxable bond for determining gain or loss will always be the entire amount paid for the bond.

*History Note:* Authority G.S. 105-130.5; 105-262;  
Eff. February 1, 1976;  
Amended Eff. October 31, 1981;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05C .1404 DEFINITION OF BOND**

The term "bond" means any bond, debenture, note or certificate or other evidence of indebtedness issued by any corporation and bearing interest and includes any like obligation issued by any government or political subdivision thereof.

*History Note:* Authority G.S. 105-130.5; 105-262;  
Eff. February 1, 1976;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**SECTION .1500 - NET ECONOMIC LOSS CARRY-OVER**

- 17 NCAC 05C .1501 PRELIMINARY STATEMENT**
- 17 NCAC 05C .1502 DIFFERENCES BETWEEN NORTH CAROLINA AND FEDERAL PROVISIONS**
- 17 NCAC 05C .1503 DEFINITION OF NET ECONOMIC LOSS**
- 17 NCAC 05C .1504 INCOME NOT TAXABLE**
- 17 NCAC 05C .1505 PROCEDURE FOR DEDUCTING A NET ECONOMIC LOSS**

*History Note:* Authority G.S. 105-130.8; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.

**17 NCAC 05C .1506 CORPORATIONS APPORTIONING THEIR NET INCOME**

A corporation required to apportion its net income or net loss under G.S. 105-130.4 may carry forward only a portion of its State net loss. For example, a corporation apportioning 50 percent of its net income or loss to North Carolina in a particular year in which it sustains a total State net loss of one thousand dollars (\$1,000.00) may carry forward only five hundred dollars (\$500.00) to a subsequent year.

*History Note:* Authority G.S. 105-130.8; 105-130.8A; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 2005;  
Readopted Eff. May 1, 2018.

**17 NCAC 05C .1507 CORPORATION SUSTAINING LOSS ENTITLED TO DEDUCTION**

*History Note:* Authority G.S. 105-130.8; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994; October 31, 1981; April 1, 1979;  
Expired Eff. September 1, 2017 pursuant to G.S. 150B-21.3A.

**SECTION .1600 - TRANSACTIONS BETWEEN AFFILIATED CORPORATIONS**

- 17 NCAC 05C .1601 PRELIMINARY STATEMENT**
- 17 NCAC 05C .1602 DEDUCTIONS FOR PAYMENTS TO AND CHARGES BY**
- 17 NCAC 05C .1603 CONSOLIDATED RETURNS**
- 17 NCAC 05C .1604 REQUIRED TO FURNISH INFORMATION REQUESTED BY SECRETARY**
- 17 NCAC 05C .1605 DEFINITIONS**
- 17 NCAC 05C .1606 TRANSACTIONS CLOSELY EXAMINED BY THE DEPARTMENT**

*History Note:* Authority G.S. 105-130.6; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.

## **SECTION .1700 - PARTNERSHIPS AND THE CORPORATE PARTNER**

### **17 NCAC 05C .1701 REPORTING PARTNERSHIP NET INCOME**

A corporation which is a member of a partnership or joint venture doing business in North Carolina is subject to North Carolina income tax and is required to include in the total net income subject to apportionment and allocation its share of the partnership's net income or net loss to the same extent required for federal income tax purposes.

*History Note:* Authority G.S. 105-130.3; 105-262;  
Eff. February 1, 1976;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

### **17 NCAC 05C .1702 APPORTIONABLE INCOME OR NONAPPORTIONABLE INCOME**

Income shall be classified as nonapportionable income where the corporate partner limits its connection to the partnership to the investment of funds or property and does not regularly or materially participate in the day-to-day operation of the partnership. Where the business of the partnership is directly or integrally related to the business of the corporate partner, the corporate partner's share of the partnership net income is classified as apportionable income. When classified as apportionable income, the corporate partner's apportionment factors shall include its proportionate share of the partnership's property, payroll, and sales. If the income is classified as nonapportionable income, it shall be included in the corporate partner's net taxable income and allocated in accordance with the allocation provisions of G.S. 105-130.4.

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 2005; January 1, 1994; October 31, 1981;  
Readopted Eff. May 1, 2018.

## **SECTION .1800 - COMPUTING TAXABLE PERCENTAGES ON DIVIDENDS**

- 17 NCAC 05C .1801 TAXABLE PERCENTAGES/DIVIDENDS**
- 17 NCAC 05C .1802 NO RETURN FILED IN YEAR ENDED SEPTEMBER 30**
- 17 NCAC 05C .1803 TWO RETURNS FILED BY A CORPORATION DURING TWELVE MONTH PERIOD**
- 17 NCAC 05C .1804 CHANGE IN NAME OR IN STATE OF INCORPORATION**
- 17 NCAC 05C .1805 AMENDED AND ADJUSTED RETURNS**
- 17 NCAC 05C .1806 MERGERS**

*History Note:* Authority G.S. 105-130.7; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994; April 1, 1991;  
Repealed Eff. December 1, 1997.

## **SECTION .1900 - FILING OF RETURNS AND PAYMENT OF TAXES**

- 17 NCAC 05C .1901 TIME AND PLACE FOR FILING**
- 17 NCAC 05C .1902 EXTENSION OF FILING DATE**
- 17 NCAC 05C .1903 PAYMENT OF TAXES**

*History Note:* Authority G.S. 105-130.17; 105-130.19; 105-262; 105-263;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1978;  
Repealed Eff. October 31, 1981.

- 17 NCAC 05C .1904 OVERPAYMENTS APPLIED TO NEXT YEAR**

(a) A corporation may elect to have an income tax refund applied to estimated income tax for the following tax year. A return reflecting an election to apply a refund to estimated tax for the following year must be filed by the last allowable date for making estimated tax payments for that year for the election to be valid.

(b) If a corporation makes a valid election, that corporation may not revoke the election after the return has been filed in order to have the amount refunded or applied in any other manner, such as an offset against any subsequently determined tax liability.

*History Note:* Authority G.S. 105-163.39; 105-163.40; 105-262;  
Eff. March 1, 2006;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

#### **17 NCAC 05C .1905 ELECTRONIC FILING OF CORPORATION INCOME TAX RETURNS**

The Department of Revenue participates in the Federal/State Electronic Filing Program and accepts corporation income tax returns filed under that program.

*History Note:* Authority G.S. 105-262;  
Eff. March 1, 2006;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

### **SECTION .2000 - EXTENSION OF TIME FOR FILING RETURN**

#### **17 NCAC 05C .2001 AUTOMATIC EXTENSION**

#### **17 NCAC 05C .2002 APPLICATION FOR AN ADDITIONAL EXTENSION**

*History Note:* Authority G.S. 105-263; 105-262;  
Eff. February 1, 1976;  
Amended Eff. November 1, 1987; October 23, 1977;  
Repealed Eff. April 1, 1991.

#### **17 NCAC 05C .2003 INTEREST AND PENALTIES**

*History Note:* Authority G.S. 105-236; 105-262;  
Eff. February 1, 1976;  
Amended Eff. November 2, 1992; October 23, 1977;  
Repealed Eff. July 1, 2000.

#### **17 NCAC 05C .2004 EXTENSION OF FILING DATE**

For tax years beginning before January 1, 2008, a corporation will receive a seven-month extension of time to file its corporate franchise and income tax return if the corporation timely files Form CD-419, Application for Extension of Time To File Corporate Franchise and Income Tax Return. For tax years beginning on or after January 1, 2008, the extension of time is six months. Payment of tax is not required to obtain an extension; however, interest accrues at the rate set under G.S. 105-241.21(a) on the amount not paid by the original due date of the corporate franchise and income tax return and the failure to pay penalty in G.S. 105-236(4) applies to the amount not paid by the original due date of the return.

*History Note:* Authority G.S. 105-262; 105-263;  
Eff. April 1, 1999;  
Amended Eff. January 1, 2009; July 1, 1999; January 1, 1994;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

### **SECTION .2100 - DISSOLUTIONS AND WITHDRAWALS**

#### **17 NCAC 05C .2101 REQUIREMENTS WHEN CORPORATION ENDS**

A domestic corporation that is dissolved, whether voluntarily, administratively, or judicially, or a foreign corporation that withdraws from the State or has its certificate of authority revoked must file all tax reports and returns due and pay all taxes

due. The final return of a corporation that has been dissolved, has withdrawn, or has had its certificate of authority revoked must include in income any unrealized or unreported profit from installment sales.

*History Note:* Authority G.S. 55-14-01; 55-14-20; 55-14-30; 55-15-20; 55-15-30; 105-130.16; 105-262.  
Eff. February 1, 1976;  
Amended Eff. July 1, 1999; April 1, 1997; January 1, 1995; January 1, 1994; November 1, 1991; April 1, 1991;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

## **17 NCAC 05C .2102 WITHDRAWALS/FILING REQUIREMENTS**

*History Note:* Authority G.S. 55-15-20; 105-130.15; 105-262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1994; November 1, 1991; April 1, 1991;  
Repealed Eff. July 1, 1999.

### **SECTION .2200 - EXEMPT CORPORATIONS**

<b>17 NCAC 05C .2201</b>	<b>PRELIMINARY STATEMENT</b>
<b>17 NCAC 05C .2202</b>	<b>CORPORATIONS FULLY EXEMPT</b>
<b>17 NCAC 05C .2203</b>	<b>CORPORATIONS CONDITIONALLY OR PARTIALLY EXEMPT</b>
<b>17 NCAC 05C .2204</b>	<b>EXCEPTIONS TO EXEMPTION</b>
<b>17 NCAC 05C .2205</b>	<b>REGULATED INVESTMENT COMPANIES</b>
<b>17 NCAC 05C .2206</b>	<b>PROOF OF EXEMPTION</b>
<b>17 NCAC 05C .2207</b>	<b>NOTIFICATIONS OF CHANGE IN PURPOSES OR OPERATIONS</b>

*History Note:* Authority G.S. 105-130.11; 105-130.12; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.

### **SECTION .2300 - REPORTING FEDERAL CHANGES**

<b>17 NCAC 05C .2301</b>	<b>REQUIREMENT FOR REPORTING CHANGES</b>
<b>17 NCAC 05C .2302</b>	<b>ASSESSMENTS OR REFUNDS</b>
<b>17 NCAC 05C .2303</b>	<b>EXTENT OF CHANGES WHICH MAY BE MADE</b>
<b>17 NCAC 05C .2304</b>	<b>FRAUD PROVISIONS ON FEDERAL CHANGES</b>

*History Note:* Authority G.S. 105-130.20; 105-262;  
Eff. February 1, 1976;  
Repealed Eff. October 31, 1981.

### **SECTION .2400 - DOMESTIC INTERNATIONAL SALES CORPORATION**

#### **17 NCAC 05C .2401 DOING BUSINESS ACTIVITIES OF DISC**

A domestic international sales corporation (DISC) is a domestic corporation whose income is derived from export sales. The DISC transacts business by exporting the products of its parent or related companies with the income earned by the DISC deferred for federal income tax purposes. The Tax Reform Act of 1984 left only the interest charge DISC remaining whose tax benefits are limited with an interest charge for tax deferred amounts imposed on DISC shareholders. Since G.S. 105-130.3 imposes an income tax on every corporation unless otherwise exempted, a DISC doing business in this state shall be subject to income tax in this state and subject to the rules in this Subchapter except as provided in this Section.

*History Note:* Authority G.S. 105-130.3; 105-262;  
Eff. December 5, 1976;  
Amended Eff. January 1, 1994;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05C .2402 DETERMINATION OF DISC NET INCOME**

*History Note:* Authority G.S. 105-130.3; 105-262;  
Eff. December 5, 1976;  
Repealed Eff. January 1, 1994.

**17 NCAC 05C .2403 APPORTIONMENT OF DISC NET INCOME**

The net income of a DISC subject to a tax measured by net income both within and without this state shall be apportioned to this state by use of the applicable apportionment formula set out in G.S. 105-130.4. The ratio determined thereunder for apportioning the net income of the DISC shall be computed by including the property, payrolls and sales of the parent corporation and related participants in the respective factors of the DISC.

*History Note:* Authority G.S. 105-130.4; 105-130.6; 105-130.16; 105-262;  
Eff. December 5, 1976;  
Amended Eff. January 1, 1994;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05C .2404 DIVIDENDS RECEIVED FROM DISC**

Dividends received by a corporate shareholder from a DISC must be included in the corporate shareholder's taxable income. Dividends received from a DISC by a corporate shareholder taxable in another state must be included in the corporate shareholder's apportionable income and apportioned to North Carolina. The term "dividends" means all amounts currently taxable under the Internal Revenue Code to corporate shareholders of a DISC whether or not distributed.

*History Note:* Authority G.S. 105-130.4; 105-262;  
Eff. December 5, 1976;  
Amended Eff. January 1, 2005; August 1, 2002;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05C .2405 EARNINGS OF DISC NOT PREVIOUSLY TAXED**

*History Note:* Authority G.S. 105-130.1; 105-130.6; 105-130.15; 105-130.16; 105-262;  
Eff. November 1, 1984;  
Repealed Eff. April 1, 1991.

**SECTION .2500 - FOREIGN SALES CORPORATION (FSC)**

- 17 NCAC 05C .2501 DOING BUSINESS ACTIVITIES/FOREIGN SALES CORPORATION (FSC)**
- 17 NCAC 05C .2502 DETERMINATION OF FSC NET INCOME**
- 17 NCAC 05C .2503 CONSOLIDATED RETURN**
- 17 NCAC 05C .2504 APPORTIONMENT - CONSOLIDATED RETURN**

*History Note:* Authority G.S. 105-130.3; 105-130.4; 105-130.6; 105-130.7; 105-130.15; 105-130.16; 105-262;  
Eff. August 1, 1986;  
Amended Eff. January 1, 1988;  
Repealed Eff. October 1, 1992.

**SECTION .2600 - REINSTATEMENT OF CORPORATE CHARTER**

**17 NCAC 05C .2601 REINSTATEMENT OF CORPORATE CHARTER**

*History Note:* Authority G.S. 105-230; 105-232;  
Eff. November 1, 1991;  
Repealed Eff. October 1, 1993.

## SUBCHAPTER 05D - ALTERNATIVE APPORTIONMENT METHOD

<b>17 NCAC 05D .0101</b>	<b>PRELIMINARY STATEMENT</b>
<b>17 NCAC 05D .0102</b>	<b>WHEN DUE</b>
<b>17 NCAC 05D .0103</b>	<b>PAYMENTS OF ESTIMATED TAX</b>
<b>17 NCAC 05D .0104</b>	<b>PENALTY FOR UNDERPAYMENT OF ESTIMATED TAX</b>
<b>17 NCAC 05D .0105</b>	<b>NO PENALTY TESTS</b>
<b>17 NCAC 05D .0106</b>	<b>OVERPAYMENT OF TAX</b>

*History Note:* Authority G.S. 105-163.25; 105-163.27; 105-163.30; 105-163.32; 105-163.33; 105.262;  
Eff. February 1, 1976;  
Amended Eff. January 1, 1978;  
Repealed Eff. October 31, 1981.

### **17 NCAC 05D .0107 PURPOSE**

The Secretary of Revenue or his designee will consider requests from corporate taxpayers for use of an alternative apportionment formula in determining tax bases for franchise and income taxes.

*History Note:* Authority G.S. 105-122(c1)(2); 105-130.4(t1); 105-262;  
Eff. February 1, 2008;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

### **17 NCAC 05D .0108 WHO MAY SUBMIT REQUEST**

(a) Any C-Corporation, S-Corporation, or Limited Liability Company electing to be treated as either a C-Corporation or S-Corporation for federal income tax purposes, which believes that the method of allocation or apportionment as administered by the Secretary of Revenue has operated or will so operate as to subject it to taxation on a greater portion of its income than is reasonably attributable to business or earnings may request an alternative apportionment method.

(b) Any C-Corporation, S-Corporation, or Limited Liability Company electing to be treated as a C-Corporation for federal income tax purposes, which believes that the method of allocation or apportionment as administered by the Secretary of Revenue has operated or will so operate as to subject it to taxation on a greater portion of its capital stock, surplus and undivided profits than is reasonably attributed to business within the state may also request an alternative apportionment method.

*History Note:* Authority G.S. 105-122(c1)(2); 105-130.4(t1); 105-262;  
Eff. February 1, 2008;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

### **17 NCAC 05D .0109 REQUEST FOR ALTERNATIVE APPORTIONMENT FORMULA**

The corporation shall file a request with the Secretary setting forth the facts upon which the corporation's belief is based and its argument with respect to the application of the allocation formula as set forth under G.S. 105-130.4(t1) or G.S. 105-122(c1)(2). The request:

- (1) shall be in a form generally used in legal drafting, setting forth sections containing the relevant facts, applicable statutory basis, and analysis supporting the request;
- (2) shall be subscribed to by an officer of the corporation having knowledge of the facts;
- (3) shall summarize the business operation of the corporation both within and without North Carolina;
- (4) shall state whether the request is for income tax purposes, for franchise tax purposes, or for both;
- (5) shall include the corporation's argument and contentions respecting the application of the formula prescribed by statute and the method of allocation requested referring to any legal references and other grounds upon which the corporation is basing its positions(s);
- (6) shall disclose the alternative apportionment method of allocation and apportionment being requested and indicate the effect of its application on the corporation's tax liability together with any supporting and supplementing information that will enable the Secretary to fully understand and consider the method of allocation and apportionment requested;

- (7) shall state the taxable periods to be reviewed;
- (8) shall, for income tax purposes, include statements of income and expenses, showing the net income of the corporation subject to apportionment for each taxable period to be reviewed;
- (9) shall, for franchise tax purposes, include statements showing the total net worth subject to apportionment for each taxable period to be reviewed;
- (10) shall include schedules for each taxable period showing the computation of the property, payroll, and sales factors as prescribed by statute in the determination of the apportionment factor as required by G.S. 105-130.4 and rules published by the Department of Revenue;
- (11) shall, for a separate accounting method of reporting the corporation's business operations in this State, submit as support operating statements showing the results of the corporation's operations within North Carolina computed on the separate accounting basis together with similar statements showing the results of the corporation's operations outside North Carolina for each taxable period to be reviewed. A full explanation and description of the separate accounting method employed in the computation must accompany the statements. If there are items of expense or income that are indirectly attributed to the separated operations, the basis for apportioning such items must be disclosed. General overhead expenses must be separately stated in documentation and explained when any portion of this expense is allocated to the separate net income attributed to this State under the requested method;
- (12) shall, for a separate accounting method, submit as support schedules reflecting the apportionment factors applicable to the operations that are conducted in whole or part in this State and the apportionment factor applicable to the business conducted outside of this State. The computations shall be made without regard to nexus requirements that would be considered if the operations were legal separate entities; and
- (13) shall contain any other information relevant to the apportionment formula or the requested method of allocation that the corporation deems appropriate under the circumstances.

*History Note:* Authority G.S. 105-122(c1)(2); 105-130.4(t1); 105-262;  
 Eff. February 1, 2008;  
 Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017;  
 Amended Eff. May 1, 2018.

#### **17 NCAC 05D .0110 TIME FOR FILING**

The request shall be filed with the Secretary not later than 90 days after the regular or extended due date of the tax return.

*History Note:* Authority G.S. 105-122(c1)(2); 105-130.4(t1); 105-262;  
 Eff. February 1, 2008;  
 Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

#### **17 NCAC 05D .0111 NOTICE OF CONFERENCE**

The Secretary shall schedule a conference to hear the corporation's request and will give notice of the time, date and place of the conference to the taxpayer at least 30 days prior thereto. Notice will be by United States Mail sent to the taxpayer's last known address. The date set for the conference must be within 90 days after the timely request of the conference or at a later date mutually agreed upon by the Taxpayer and the Secretary. The date set for the conference may be postponed once at the request of the Taxpayer and once at the request of the Secretary for up to 90 days or for a longer period mutually agreed upon by the Taxpayer and the Secretary.

*History Note:* Authority G.S. 105-122(c1)(2); 105-130.4(t1); 105-262;  
 Eff. February 1, 2008;  
 Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

#### **17 NCAC 05D .0112 WHO SHALL ATTEND THE CONFERENCE**

The Secretary or their designee and the Director of the Corporate Tax Division or their designee, along with any other Department personnel the Secretary or Director shall deem appropriate, shall attend any conference pursuant to a request for an alternative apportionment formula. The taxpayer is not required to personally appear or be represented at the conference. Legal counsel or other tax practitioner may appear with or without the taxpayer on the taxpayer's behalf.

*History Note:* Authority G.S. 105-122(c1)(2); 105-130.4(t1); 105-262;

*Eff. February 1, 2008;*  
*Readopted Eff. May 1, 2018.*

**17 NCAC 05D .0113 CONDUCT OF THE CONFERENCE**

- (a) If the corporation or its representative fails to appear after proper service of notice, the Secretary may proceed with the conference and make his decision in the absence of the party.
- (b) The taxpayer shall be given an opportunity to present arguments on issues of law and policy and an opportunity to present evidence on issues of fact.
- (c) The rules of evidence as applied in the trial division of the General Court of Justice do not apply.
- (d) An informal record containing in substance the evidence, contentions and arguments presented at the conference shall be made.

*History Note: Authority G.S. 105-122(c1)(2); 105-130.4(t1); 105-262;*  
*Eff. February 1, 2008;*  
*Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

**17 NCAC 05D .0114 REMEDY**

- (a) If the Secretary finds that the statutory formula does not fairly represent the corporation's business activity in North Carolina, he may require:
  - (1) separate accounting;
  - (2) the exclusion of any one or more of the factors;
  - (3) the inclusion of one or more additional factors which will fairly represent the taxpayer's business activity in this State, or
  - (4) the employment of any other method to effectuate and equitable allocation and apportionment of the taxpayer's income.
- (b) In the case of a request for relief from the statutory apportionment formula for both franchise tax and income tax, the Secretary shall make separate determinations as to whether an alternative apportionment method is warranted.

*History Note: Authority G.S. 105-122(c1)(2); 105-130.4(t1); 105-262;*  
*Eff. April 1, 2008;*  
*Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

**17 NCAC 05D .0115 FINAL DECISION**

A final decision shall be furnished to the requesting corporation within 60 days from the date of the conference or within 60 days after the date any additional information requested by the Secretary during the conference is provided.

*History Note: Authority G.S. 105-122(c1)(2); 105-130.4(t1); 105-262;*  
*Eff. February 1, 2008;*  
*Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

**SUBCHAPTER 5E - INSURANCE PREMIUMS TAX AND REGULATORY SURCHARGE**

**SECTION .0100 - GENERAL PROVISIONS**

**17 NCAC 05E .0101 REDUCED INSTALLMENT PAYMENTS**

The Secretary may reduce the installment payment requirements for the quarterly insurance gross premiums tax and the regulatory surcharge if an insurer submits a written statement to the Department indicating that the insurer reasonably believes that its total estimated payments made for the current year will exceed the anticipated tax liability for the year.

This written statement must contain the basis for the insurer's belief that its installment payments should be reduced and state the factors supporting that belief, such as changes in the law or a reduction in the insurer's writings. The statement must be submitted at least 45 days before the due date of an installment payment. An insurer that files a timely statement may reduce its next installment payment in accordance with the statement unless the insurer receives written notice from the Department that its request has been denied or adjusted.

*History Note:* Authority G.S. 105-228.5; 105-262;  
Eff. January 1, 1989;  
Transferred and Recodified from 11 NCAC 11E .0110 Eff. January 15, 1998;  
Amended Eff. August 1, 1998;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05E .0102 ADDITIONAL FIRE AND LIGHTNING TAXES**

*History Note:* Authority G.S. 105-228.5; 105-262;  
Eff. February 1, 1976;  
Readopted Eff. February 28, 1978;  
Transferred and Recodified from 11 NCAC 11E .0202 Eff. January 15, 1998;  
Amended Eff. August 1, 1998;  
Repealed Eff. February 1, 2008.

**17 NCAC 05E .0103 PREMIUM FINANCE CHARGES AND OTHER CHARGES**

Gross premiums from business in this State include premium finance charges and installment payment charges or other charges received as a result of the partial payment of premiums by a policyholder. These charges are therefore subject to tax.

*History Note:* Authority G.S. 105-228.5; 105-262;  
Eff. April 1, 1993;  
Transferred and Recodified from 11 NCAC 11E .0203 Eff. January 15, 1998;  
Amended Eff. August 1, 1998;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05E .0104 DIVIDENDS APPLIED TO PURCHASE ADDITIONAL PAID-UP LIFE**

Dividends applied to purchase additional paid-up life insurance are not taxable under G.S. 105-228.5 since gross premiums are deemed to be the amounts specified in the life insurance policy contracts when issued.

*History Note:* Authority G.S. 105-228.5; 105-262;  
Eff. February 1, 1976;  
Readopted Eff. February 28, 1978;  
Transferred & Recodified from 11 NCAC 11E .0302 Eff. January 15, 1998;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05E .0105 GROUP PREMIUMS**

*History Note:* Authority G.S. 105-228.5; 105-262;  
Eff. February 1, 1976;  
Readopted Eff. February 28, 1978;  
Transferred and Recodified from 11 NCAC 11E .0304 Eff. January 15, 1998;  
Amended Eff. August 1, 1998;  
Repealed Eff. February 1, 2008.

**17 NCAC 05E .0106 EMPLOYEE BENEFIT PLAN CONTRIBUTIONS**

Insurance company contributions or subsidies in the self-insurance of life and accident and health insurance coverage as an employee benefit plan are not taxable under G.S. 105-228.5.

*History Note:* Authority G.S. 105-228.5; 105-262;  
Eff. February 1, 1976;  
Readopted Eff. February 28, 1978;  
Transferred & Recodified from 11 NCAC 11E .0305 Eff. January 15, 1998;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**SUBCHAPTER 05F – SECRETARY'S AUTHORITY TO ADJUST NET INCOME OR TO REQUIRE A  
COMBINED RETURN**

**SECTION .0100 - GENERAL**

**17 NCAC 05F .0101 SCOPE**

The rules in this Subchapter apply to the Secretary's authority under G.S. 105-130.5A to adjust net income or to require a combined return for taxable years beginning on or after January 1, 2012.

*History Note: Authority G.S. 105-130.5A; 105-262.1;  
Eff. January 31, 2013;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

**17 NCAC 05F .0102 DEFINITIONS**

As used in G.S. 105-130.5A and this Subchapter, the following definitions shall apply:

- (1) "Centralized cash management" means a process by which an affiliated group of businesses makes all or most cash management decisions from one location, such as a headquarters or designated subsidiary, that results in individual affiliates having little autonomy in making decisions concerning how cash is managed.
- (2) "Economic position" means the status of a taxpayer's assets, liabilities, and equity (whether those items are actual, contingent, or potential) and their interrelationship to one another.
- (3) "Material benefit" means an improvement in the economic position of the taxpayer on a pre-tax basis.
- (4) "Material business activity" means an activity that is both:
  - (a) An integral part of the unitary group's business; and
  - (b) Performed on a regular and continuous basis.
- (5) "Principal member" means a member of the combined group that acts in the group's name in all matters relating to the income tax liability for the combined group, and is the entity responsible for preparing the corporate income tax return and making corporate income tax payments for the combined group.
- (6) "Unitary business" means one or more related business organizations where there is a unity of ownership, operation, and use. It can also exist where there is interdependence in their functions. A determination of whether a corporation is part of a unitary business with another corporation is determined based on the facts and circumstances of each case.

*History Note: Authority G.S. 105-130.5A; 105-262.1;  
Eff. January 31, 2013;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

**SECTION .0200 – ECONOMIC SUBSTANCE**

**17 NCAC 05F .0201 ECONOMIC SUBSTANCE TEST BURDEN OF PROOF**

The taxpayer has the burden of proving that a transaction meets both prongs of the economic substance test as specified in G.S. 105-130.5A(g).

*History Note: Authority G.S. 105-130.5A; 105-262.1;  
Eff. January 31, 2013;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

**17 NCAC 05F .0202 REASONABLE BUSINESS PURPOSES**

(a) In proving that a transaction, or series of transactions of which the transaction is a part, has one or more reasonable business purposes other than the creation of State income tax benefits, the taxpayer must show:

- (1) The business purpose asserted was valid and realistic;
- (2) The transaction was a reasonable and realistic means to accomplish the asserted business purpose;
- (3) Evidence exists that shows the taxpayer took steps to achieve the asserted business purpose; and
- (4) The value of the non-State income tax benefits reasonably anticipated by the taxpayer from the transaction exceeds the additional cost associated with the transaction.

(b) Generally, reasonable business purpose is supported by contemporaneous documentation. Though not conclusive, the absence of contemporaneous documentation weakens the contention that the asserted business purpose is valid.

*History Note:* Authority G.S. 105-130.5A; 105-262.1;  
Eff. January 31, 2013;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

#### **17 NCAC 05F .0203 ECONOMIC EFFECTS**

(a) In proving that a transaction, or series of transactions of which the transaction is a part, has economic effects beyond the creation of State income tax benefits, the taxpayer must show by objective evidence that a reasonable likelihood of material benefit, other than State income tax benefits, from the transaction existed at the time the transaction was initiated and there was a material benefit to the transaction apart from State income tax benefits.

(b) In analyzing whether a transaction has an economic effect, the Secretary shall analyze the economic effect on the taxpayer and on the aggregate economic effect on the parties to the transaction.

*History Note:* Authority G.S. 105-130.5A; 105-262.1;  
Eff. January 31, 2013;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

#### **17 NCAC 05F .0204 ECONOMIC SUBSTANCE DOCTRINE**

The Secretary shall rely on general principles of the common law economic substance doctrine as established under federal and state case law in applying each prong of the two pronged test under G.S. 105-130.5A(g), except where case law conflicts with the statute. General principles of the economic substance doctrine include the following:

- (1) Economic substance is a prerequisite to any provision allowing deductions;
- (2) A taxpayer has the burden of proving that a transaction has both purpose and substance;
- (3) A taxpayer has the burden of showing that the form of the transaction accurately reflects its substance and that deductions claimed are permissible;
- (4) The economic substance of a transaction shall be determined based on documentation and data rather than the subjective opinions of the taxpayer; and
- (5) The transactions, not the entities, shall be examined for economic substance.

*History Note:* Authority G.S. 105-130.5A; 105-262.1;  
Eff. January 31, 2013;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

#### **17 NCAC 05F .0205 ECONOMIC SUBSTANCE FACTORS**

Determining whether or not a transaction has economic substance is a fact-intensive inquiry that is dependent upon the facts and circumstances of each transaction made by a taxpayer. The Secretary shall consider or analyze all the facts and circumstances including the following:

- (1) The reasons for the transaction;
- (2) Whether the transaction was a reasonable means to accomplish the asserted purposes;
- (3) Expectations of benefits obtained from the transactions;
- (4) The effects the transaction had on the taxpayer's profits;
- (5) The existence of a reasonable or realistic potential for profit from making the transaction;
- (6) The objective economic impact of the transaction other than State income tax savings;
- (7) The transaction's effect on the taxpayer's State income tax liability;
- (8) The transaction's effect on the taxpayer's tax liability in other states;
- (9) The transaction's effect on the taxpayer's federal tax liability;
- (10) Whether the method of determining the amount of payment is an industry practice;
- (11) The change in the business operations of the parties, if any, after the transaction;
- (12) Whether assets were transferred between or among related parties;
- (13) Whether the business operations related to specific assets changed after any transfer of those assets;
- (14) Whether the entity transferring assets retained control over the assets;
- (15) The tax consequences of the transfer of assets;
- (16) The party or parties who created or developed the ideas which led to the transaction;

- (17) The party or parties who presented the ideas concerning the transaction to the taxpayer;
- (18) Whether the contemporaneous documentation explaining the transaction to the taxpayer discussed profit potential in addition to tax benefits;
- (19) The party or parties that drafted the agreements relating to the transaction;
- (20) The party or parties that negotiated the agreements relating to the transaction;
- (21) The party or parties that dictated the terms of the agreements relating to the transaction;
- (22) Cost-benefit analyses or other studies conducted related to the transaction;
- (23) Non-tax benefits obtained by the taxpayer as a result of the transaction; and
- (24) Whether the intercompany transaction resulted in a circular cash flow.

*History Note:* Authority G.S. 105-130.5A; 105-262.1;  
 Eff. January 31, 2013;  
 Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05F .0206 WHEN STATE INCOME TAX BENEFITS ARE CONSIDERED**

- (a) State income tax benefits resulting from a transaction are considered by the Secretary in determining whether a transaction has reasonable business purposes and economic substance when the State income tax benefits are consistent with legislative intent, such as when the transaction is made in accordance with laws enacted by the General Assembly to encourage engagement in certain types of activities through tax deductions or tax credits.
- (b) When a transaction that generates targeted tax incentives is, in form and substance, consistent with the State income tax benefits designed by the General Assembly, the State income tax benefits shall be considered by the Secretary in determining whether the transaction has reasonable business purposes and economic substance.

*History Note:* Authority G.S. 105-130.5A; 105-262.1;  
 Eff. January 31, 2013;  
 Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**17 NCAC 05F .0207 CENTRALIZED CASH MANAGEMENT**

Although the existence of a centralized cash management system among members of an affiliated group is not conclusive evidence that a transaction lacks economic substance, the Secretary shall analyze the transactions for reasonable business purposes and economic effects. If the cash management transaction, or series of transactions of which the transaction is a part, results in the creation of unreasonably excessive interest expense when compared to industry practice, shifting of assets, or the reclassification of income as nonapportionable or nonallocable, the transaction may be deemed to lack economic substance.

*History Note:* Authority G.S. 105-130.5A; 105-262.1;  
 Eff. January 31, 2013;  
 Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**SECTION .0300 – FAIR MARKET VALUE**

**17 NCAC 05F .0301 DETERMINATION OF FAIR MARKET VALUE**

- (a) For purposes of determining whether or not transactions between members of an affiliated group were made at fair market value under the standards contained in the regulations adopted under section 482 of the Internal Revenue Code pursuant to G.S. 105-130.5A(h), the Secretary shall consider all facts and circumstances relative to the transactions, including any transfer pricing studies provided by the taxpayer.
- (b) In determining whether or not transactions were made at fair market value, the Secretary will also apply any federal or state case law developed under section 482 of the Internal Revenue Code and its regulations.
- (c) The fact that a taxpayer has a transfer pricing study will not in and of itself be sufficient to establish that a transaction was made at fair market value.

*History Note:* Authority G.S. 105-130.5A; 105-262.1;  
 Eff. January 31, 2013;  
 Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

**SECTION .0400 - ADJUSTMENTS**

#### **17 NCAC 05F .0401      ADJUSTMENTS TO STATE NET INCOME**

Adjustments the Secretary may make to intercompany transactions that are found to lack economic substance or not to be at fair market value include the following:

- (1) Disallowing deductions in whole or in part;
- (2) Attributing income to related corporations;
- (3) Disregarding transactions; and
- (4) Reclassifying income as apportionable or allocable.

*History Note: Authority G.S. 105-130.5A; 105-262.1;  
Eff. January 31, 2013;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

### **SECTION .0500 – COMBINED RETURNS**

#### **17 NCAC 05F .0501      METHODOLOGY WHEN COMBINED RETURN REQUIRED OR PERMITTED**

When the Secretary requires or allows a corporate taxpayer to submit a combined return, the following methodology applies:

- (1) The starting point is the federal taxable income of the pro forma 1120 for each corporation. The 1120s shall represent federal taxable income "as if" each corporation were not part of a consolidated federal 1120;
- (2) The taxpayer shall combine the pro forma 1120s of the corporations to be included in the combined group; this results in a combination of each corporation's line items in determining combined income.
- (3) The taxpayer shall eliminate the intercompany transactions between members of the combined group in arriving at combined federal taxable income.
- (4) The taxpayer shall make North Carolina modifications (additions and subtractions) as provided in G.S. 105-130.5 to determine combined income subject to apportionment.
- (5) The taxpayer shall include in the apportionment factors the property, payroll, and sales of all corporations included in the combined group as provided in G.S. 105-130.4. All sales into North Carolina by entities within the combined group shall be included in the sales factor numerator. Where an intercompany transaction has occurred and been eliminated in the calculation of combined income, this amount shall also be eliminated from the numerator and denominator of the applicable factor.
- (6) Only one apportionment factor is to be calculated by the taxpayer for the combined group. Unless otherwise provided in this section, the standard three factor formula, which uses the apportionment factors of property, payroll, and sales, shall be used. If more than 50 percent of the group's combined income subject to apportionment is generated from a business activity subject to special apportionment under subsections (m) through (s1) of G.S. 105-130.4, then that apportionment formula shall be used for the entire group. If the taxpayer believes the statutory apportionment method that otherwise applies to the combined group subjects a greater portion of the group's income to tax than is attributable to its business in this State, the taxpayer may propose, and the Secretary shall consider, an alternative method of apportionment. The taxpayer shall apply the combined apportionment factor to the combined apportionable income to determine income apportioned to this State.
- (7) The taxpayer shall add any nonapportionable income allocated to North Carolina to the income apportioned to this State to determine total income subject to North Carolina tax.
- (8) The combined group's income subject to tax may be reduced by net economic losses sustained by a corporation that becomes a member of the group, but not fully used by that corporation prior to becoming a member of the combined group, subject to the provisions of G.S. 105-130.8. Net economic losses brought by a corporation into the group remain with that corporation and, to the extent not used by the group during the years the corporation is part of the group, may be claimed by the corporation in the tax years after the corporation ceases to be a part of the group. The tax years that the corporation is part of the combined group count toward the 15-year carryforward period authorized in G.S. 105-130.8. A net economic loss sustained by the group in a combined return year shall be allocated among the members of the group that reported losses on their pro forma 1120s, after elimination of intercompany transactions between members of the combined group. The amount allocated to each member shall be determined by dividing that member's loss (after elimination of intercompany transactions) by the total losses (after elimination of intercompany transactions) of all members of the combined group in that tax year. To the extent not used by the group during the years the corporation is part of the group, the group's net economic losses allocated

to a corporation that is a member of the group may be claimed by the corporation in the tax years after the corporation ceases to be a part of the group. Net economic losses shall be considered used in order beginning with earliest tax year. If more than one corporation brought net economic losses from the same tax year into the combined group and a portion of the losses from that year is used, the amount of used net economic losses shall be prorated among the members bringing losses from that year based on the percentage of each member's losses to the total losses carried forward from that year.

- (9) The combined group's income tax may be reduced by tax credits earned by a member of the combined group, but not fully used by that entity prior to becoming a member of the combined group, subject to the provisions of the specific credits. Because the eligibility for a tax credit is determined at the separate entity level, any unused installment or carryforward of a tax credit earned by a member of the combined group remains with that entity if that entity is no longer a member of the combined group or the group is no longer required to file a combined return. This is applicable whether the credit was earned by the entity before becoming a member of the combined group or while a member of the combined group. For franchise tax purposes, the tax credits may only be used by the entity generating the credit unless the group also files a combined return for franchise tax purposes.

*History Note: Authority G.S. 105-130.4; 105-130.5; 105-130.5A; 105-130.8; 105-262.1; Eff. January 31, 2013; Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

#### **17 NCAC 05F .0502 PROCEDURES FOR FILING A COMBINED INCOME TAX RETURN**

(a) The principal member shall file Form CD-405, The North Carolina C Corporation Tax Return, and all required schedules. The combined tax return replaces the separate entity corporate income tax returns filed by the members of the group that are doing business in this State.

(b) The principal member shall include the following schedules:

- (1) A computation of the North Carolina taxable income of each corporation in the combined return that would have been reported if the member had filed a North Carolina income tax return on a separate company basis;
- (2) A schedule detailing all intercompany eliminations made by and between the members of the unitary group;
- (3) A schedule of all North Carolina income tax estimated payments made by each member of the group;
- (4) A schedule reflecting the computation of the combined apportionment factor as required in 17 NCAC 05F .0501(6). Taxpayers shall not use Schedule O of the CD-405;
- (5) A schedule of eligible net economic losses and the use of same by member entities and the combined group; and
- (6) A schedule of eligible tax credits and the use of same by member entities and the combined group.

*History Note: Authority G.S. 105-130.5A; 105-262.1; Eff. January 31, 2013; Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

#### **17 NCAC 05F .0503 COMBINED RETURN TAX CREDITS**

(a) Any member of the combined group that has activities that qualify for a North Carolina income tax credit shall provide all required information to determine and support the amount of the credit on a separate company basis. This information shall be included with the combined return in each year the qualifying member becomes eligible to claim a credit or an installment of a credit, even if the group's income tax liability for that tax year is not sufficient for the combined group to benefit from the income tax credit.

(b) Combined groups eligible to claim income tax credits shall complete Form CD-425, Corporate Tax Credit Summary, on a combined basis and file it with the group's income tax return. If a member of the combined group is eligible to claim an income tax credit limited by statute to 50 percent of tax, the combined group shall also complete Form NC-478, Summary of Tax Credits Limited to 50 Percent of Tax.

*History Note: Authority G.S. 105-130.5A; 105-262.1; Eff. January 31, 2013; Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.*

## SECTION .0600 – FRANCHISE TAX RETURN

### 17 NCAC 05F .0601 PROCEDURES FOR FILING A FRANCHISE TAX RETURN

(a) The provisions of this Rule apply unless the Secretary authorizes a combined group to file a combined franchise tax return under G.S. 105-122. Each corporation that is doing business in this State pursuant to G.S. 105-114(b)(3) shall file a separate North Carolina franchise tax return and pay any franchise tax due. Any corporation that is included in a combined income tax return but that is not doing business in this State pursuant to G.S. 105-114(b)(3) is not subject to North Carolina franchise tax.

(b) The principal member shall file its franchise tax return on the combined group's CD-405.

(c) All other members' separate returns shall include zero dollars (\$0) on the "Net Taxable Income" and "NC Net Income Tax" lines on the CD-405 and include a statement with the return that:

- (1) Indicates its income is included in the combined income tax return filed by the principal member; and
- (2) Identifies the name and Federal Employer Identification Number of the principal member.

(d) If the corporation filing a franchise tax return is a multistate taxpayer, then it shall calculate an apportionment factor to be used in calculating its capital stock base using its separate entity property, payroll, and sales before intercompany eliminations. Schedule O of the CD-405 must reflect the entity's apportionment factor for franchise tax purposes.

*History Note:* Authority G.S. 105-114(b)(3); 105-122; 105-130.5A; 105-262.1;  
Eff. January 31, 2013;  
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. August 19, 2017.

## SUBCHAPTER 05G – MARKET-BASED SOURCING FOR APPORTIONMENT OF INCOME

### SECTION .0100 – GENERAL RULES

#### 17 NCAC 05G .0101 SCOPE

The rules in this Subchapter shall not apply to receipts from the sale of tangible personal property. Other receipts are in North Carolina when the taxpayer's market for the sales is in North Carolina. The rules of this Subchapter establish uniform rules for:

- (1) determining to what extent the market for a sale 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 G.S. 105-130.4(1); and
- (4) excluding receipts from the denominator of the sales factor where the state or states of assignment cannot be determined or reasonably approximated.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

#### 17 NCAC 05G .0102 DEFINITIONS

In addition to the definitions in G.S. 105-130.4, as used in this Subchapter, the following definitions shall apply:

- (1) "Billing address" means the location stated 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 regular course of business and not for tax avoidance purposes.
- (2) "Business customer" means a customer that is a business operating in any form, including a sole proprietorship. Sales to a non-profit organization; a trust; the U.S. Government; a foreign, state or local government; or to an agency or instrumentality of that government are treated as sales to a business customer.
- (3) "Code" means as defined in G.S. 105-228.90.
- (4) "Department" means the North Carolina Department of Revenue.
- (5) "Good faith" means a state of mind consisting in honesty in belief or purpose, faithfulness to one's duty or obligation, observance of reasonable commercial standards of fair dealing in a given trade or business, or absence of intent to defraud or to seek unconscionable advantage.
- (6) "Individual customer" means a customer that is not a business customer.

- (7) "Intangible property" means property that is not physical or whose representation by physical means is incidental and includes:
- (a) copyrights;
  - (b) patents;
  - (c) trademarks;
  - (d) trade names;
  - (e) brand names;
  - (f) franchises;
  - (g) licenses;
  - (h) trade secrets;
  - (i) trade dress;
  - (j) information;
  - (k) know-how;
  - (l) methods;
  - (m) programs;
  - (n) procedures;
  - (o) systems;
  - (p) formulae;
  - (q) processes;
  - (r) technical data;
  - (s) designs;
  - (t) literary,
  - (u) musical, or artistic compositions;
  - (v) information;
  - (w) ideas;
  - (x) contract rights including broadcast rights;
  - (y) agreements not to compete;
  - (z) goodwill and going concern value;
  - (aa) securities; and
  - (bb) except as otherwise provided in these Rules, computer software.
- (8) "Place of order" means the physical location where a customer places an order for a sale from a taxpayer, resulting in a contract with the taxpayer.
- (9) "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. Census data is hereby incorporated by reference, including subsequent amendments or additions, and is available free of charge at [census.gov/topics/population.html](https://www.census.gov/topics/population.html).
- (10) "Reasonable" or "reasonably" means agreeable to reason; just; proper; ordinary or usual.
- (11) "Related entity" means as defined in G.S. 105-130.7A.
- (12) "Secretary" means the Secretary of Revenue.
- (13) "State where a contract of sale is principally managed by the customer" means the primary location where 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.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

## **SECTION .0200 – GENERAL PRINCIPLES OF APPLICATION**

### **17 NCAC 05G .0201 ASSIGNMENT OF RECEIPTS FROM SALES OF OTHER THAN TANGIBLE PERSONAL PROPERTY**

A taxpayer's assignment of receipts from sales other than of tangible personal property shall comply with the following:

- (1) A taxpayer shall apply the rules set forth in this Subchapter based on objective criteria and shall consider all sources of information reasonably available to the taxpayer at the time of its tax filing including the taxpayer's books and records kept in the regular 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 Secretary upon request, as provided in Article 9 of G.S. 105.

- (2) This Subchapter provides assignment rules that apply sequentially in a hierarchy. For each sale to which a hierarchical rule applies, a taxpayer shall make a reasonable effort to apply the primary rule applicable to the sale before seeking to apply the next rule in the hierarchy and shall continue to do so with each succeeding rule in the hierarchy.
- (3) A taxpayer's method of assigning its receipts shall reflect an attempt to obtain the most accurate assignment of receipts consistent with the rules set forth in this Subchapter, rather than an attempt to lower the taxpayer's tax liability.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

## **SECTION .0300 – RULES OF REASONABLE APPROXIMATION**

### **17 NCAC 05G .0301 IN GENERAL**

The rules of this Subchapter set forth the process of reasonable approximation that apply if the state or states of assignment cannot be determined. In some instances, the reasonable approximation shall be made in accordance with specific rules of approximation prescribed in this Subchapter. In other cases, the applicable rules in this Subchapter permit a taxpayer to reasonably approximate the state or states of assignment to obtain a result similar to those made using a specific rule of approximation.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

### **17 NCAC 05G .0302 APPROXIMATION BASED UPON KNOWN SALES**

When, by applying the rules set forth in Sections .0900 through .1000 of this Subchapter, a taxpayer can ascertain the state or states of assignment of a substantial portion of its receipts from sales of substantially similar services and the taxpayer reasonably believes that the geographic distribution of the remainder of its sales tracks that of the assigned receipts, the taxpayer shall include the receipts from those sales in its sales factor in the same proportion as its assigned receipts. This Rule applies in the context of licenses and sales of intangible property where the substance of the transaction resembles a sale of goods or services.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

### **17 NCAC 05G .0303 RELATED ENTITY TRANSACTIONS**

Where a taxpayer has receipts subject to this Subchapter from transactions with a related entity customer, information that the customer has regarding the sourcing of receipts from these transactions shall be imputed to the taxpayer.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

## **SECTION .0400 – EXCLUSION OF RECEIPTS FROM THE SALES FACTOR**

### **17 NCAC 05G .0401 ALLOCATED GROSS RECEIPTS**

The sales factor includes only gross receipts of the taxpayer that are not allocated under G.S. 105-130.4, and are received from transactions and activity in the regular course of the taxpayer's trade or business. Receipts addressed in G.S. 105-130.4(a)(7) shall be excluded.

*History Note:* Authority G.S. 105-130.4; 105-130.4(a)(7); S.L. 2016-5; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

### **17 NCAC 05G .0402 UNASSIGNABLE GROSS RECEIPTS**

When a taxpayer is unable to ascertain the state or states where receipts of a sale are to be assigned pursuant to the rules set forth in this Subchapter using a reasonable amount of effort undertaken in good faith, the receipts shall be excluded from the denominator of the taxpayer's sales factor pursuant to this Subchapter.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

## **SECTION .0500 - CHANGES IN METHODOLOGY**

### **17 NCAC 05G .0501 ALTERNATIVE APPORTIONMENT**

Nothing in this Subchapter limits the application of G.S. 105-122(c1)(2) or G.S. 105-130.4(t1). If the application of this Subchapter results in the assignment of receipts to the taxpayer's sales factor that the taxpayer believes does not fairly represent the extent of the taxpayer's business activity in North Carolina, the taxpayer may request the use of a different method for assigning those receipts.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

### **17 NCAC 05G .0502 ORIGINAL RETURNS**

When a taxpayer files an original return for a taxable year where it properly assigns its receipts using a method of assignment, including a method of reasonable approximation, in accordance with the rules in this Subchapter, the application of such method of assignment shall be deemed to be a correct determination by the taxpayer of the state or states of assignment to which the method is properly applied. In those cases, neither the Secretary nor the taxpayer may modify the taxpayer's methodology as applied for assigning those receipts for the taxable year, through the form of an audit adjustment, amended return, or abatement application. However, the Secretary and the taxpayer may each subsequently correct factual errors or calculation errors with respect to the taxpayer's application of its filing methodology.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

### **17 NCAC 05G .0503 SECRETARY'S AUTHORITY TO ADJUST A TAXPAYER'S RETURN**

The Secretary's ability to review and adjust a taxpayer's assignment of receipts on a return to assign receipts consistent with the rules of this Subchapter, includes each of the following potential actions:

- (1) when a taxpayer fails to properly assign receipts from a sale in accordance with the rules set forth in this Subchapter, including the failure to apply a hierarchy of rules consistent with the principles of Rule .0201(2) of this Subchapter, the Secretary shall adjust the assignment of the receipts in accordance with the applicable rules in this Subchapter;
- (2) when a taxpayer uses a method of approximation to assign its receipts and the Secretary determines that the method of approximation employed by the taxpayer is not reasonable, the Secretary shall either substitute a method of approximation that the Secretary determines is appropriate, as provided in Article 9 of G.S. 105, or exclude the receipts from the taxpayer's numerator and denominator;
- (3) when the Secretary determines that a taxpayer's method of approximation has not been applied in a consistent manner with respect to similar transactions or year to year, the Secretary may require that the taxpayer apply its method of approximation in a consistent manner;
- (4) when a taxpayer excludes receipts from the denominator of its sales factor on the basis that the assignment of the receipts cannot be reasonably approximated, the Secretary may determine that the exclusion of those receipts is not appropriate, and may instead substitute a method of approximation that the Secretary determines is appropriate, as provided in Article 9 of G.S. 105;
- (5) when a taxpayer fails to retain contemporaneous records that explain the determination and application of its method of assigning its receipts, including its underlying assumptions, or fails to provide those records to the Secretary upon request, the Secretary shall treat the taxpayer's assignment of receipts as unsubstantiated, and shall adjust the assignment of the receipts in a manner consistent with the applicable rules in this Subchapter; or

- (6) when the Secretary concludes that a customer's billing address was selected by the taxpayer for tax avoidance purposes, the Secretary shall adjust the assignment of receipts from sales to that customer in a manner consistent with the applicable rules in this Subchapter.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

#### **17 NCAC 05G .0504 TAXPAYER AUTHORITY TO CHANGE A METHOD OF ASSIGNMENT ON A PROSPECTIVE BASIS**

A taxpayer that seeks to change its method of assigning its receipts shall disclose, in the original return filed for the year of the change, the fact that the taxpayer has made the change. If a taxpayer fails to disclose the change, the Secretary may disregard the taxpayer's change and substitute an assignment method that the Secretary determines is appropriate, as provided in Article 9 of G.S. 105.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

#### **17 NCAC 05G .0505 SECRETARY AUTHORITY TO CHANGE A METHOD OF ASSIGNMENT ON A PROSPECTIVE BASIS**

The Secretary may direct a taxpayer to change its method of assigning its receipts in tax returns that have not yet been filed, including changing the taxpayer's method of approximation, if upon reviewing the taxpayer's filing methodology applied in a prior tax year, the Secretary determines that the change reflects a more accurate assignment of the taxpayer's receipts within the meaning of this Subchapter, and determines that the change can be reasonably adopted by the taxpayer. The Secretary shall provide the taxpayer with a written explanation of the reason for making the change. When a taxpayer fails to comply with the Secretary's direction on future returns, the Secretary shall deem the taxpayer's method of assigning its receipts on those returns to be unreasonable, and shall substitute an assignment method that the Secretary determines is reasonable.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

### **SECTION .0600 - FURTHER GUIDANCE**

#### **17 NCAC 05G .0601 EXAMPLES**

- (a) The Secretary shall publish on the Department's website examples demonstrating the application of rules set forth in this Subchapter. The document shall be available at [www.ncdor.gov](http://www.ncdor.gov).
- (b) The Secretary may issue further public written statements with respect to the rules set forth in this Subchapter. These statements may include guidance with respect to:
- (1) what constitutes a reasonable method of approximation within the meaning of the rules, and
  - (2) the circumstances when a filing change for a taxpayer's method of reasonable approximation will be deemed appropriate.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

### **SECTION .0700 – SALE OF A SERVICE**

#### **17 NCAC 05G .0701 IN GENERAL**

- (a) The receipts from a sale of a service shall be in North Carolina to the extent that the service is delivered to a location in North Carolina. 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.
- (b) 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 Sections .0700 through .1000 of this Subchapter.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

## SECTION .0800 – SALE OF IN-PERSON SERVICES

### 17 NCAC 05G .0801 IN GENERAL

(a) 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 Section includes situations where the services are provided on behalf of the taxpayer by a third-party contractor.

(b) Examples of in-person services include:

- (1) warranty and repair services;
- (2) cleaning services;
- (3) plumbing services;
- (4) carpentry;
- (5) construction contractor services;
- (6) pest control;
- (7) landscape services;
- (8) medical and dental services, including medical testing, x-rays, and mental health care and treatment;
- (9) child care;
- (10) hair cutting and salon services;
- (11) live entertainment and athletic performances; and
- (12) in-person training or lessons.

(c) In-person services include services within the description of this Rule 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.

(d) Professional services as described in Section .1000 of this Subchapter shall not be treated as in-person services within the meaning of this Section.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

### 17 NCAC 05G .0802 ASSIGNMENT OF RECEIPTS FROM SALE OF IN-PERSON SERVICES

Receipts from a sale of in-person services shall be assigned to North Carolina to the extent the customer received the service in North Carolina. The taxpayer shall 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, such as hair cutting or x-ray services, or in the physical presence of the customer in North Carolina, such as 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; or
- (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.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

### 17 NCAC 05G .0803 REASONABLE APPROXIMATION

When the taxpayer cannot determine the state or states where a service was received pursuant to Rule .0802 of this Section, but the taxpayer has information regarding the location of receipt from which the taxpayer can reasonably approximate the state or states where the service is received, the taxpayer shall reasonably approximate such state or states.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

**SECTION .0900 - SERVICES DELIVERED TO A CUSTOMER OR ON BEHALF OF THE CUSTOMER, OR DELIVERED ELECTRONICALLY THROUGH THE CUSTOMER**

**17 NCAC 05G .0901 IN GENERAL**

(a) If the service provided by the taxpayer is not an in-person service as defined in Rule .0801 of this Subchapter or a professional service as defined in Rule .1001 of this Subchapter, 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 to the extent that the service is delivered in North Carolina.

(b) For purposes of this Section, a service:

- (1) "delivered to a customer" is a service where the customer and not a third party is the recipient of the service;
- (2) "delivered on behalf of a customer" is one where a customer contracts for a service but one or more third parties, rather than the customer, is the recipient of the service. This includes fulfillment services, or the direct or indirect delivery of advertising to the customer's intended audience; and
- (3) "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.

(c) A service may be delivered to or on behalf of a customer by physical means or through electronic transmission.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

**17 NCAC 05G .0902 ASSIGNMENT OF RECEIPTS FROM SALES OF SERVICES DELIVERED TO THE CUSTOMER OR ON BEHALF OF THE CUSTOMER, OR DELIVERED ELECTRONICALLY THROUGH THE CUSTOMER**

(a) The assignment of receipts to a state or states when a sale of a service is delivered to the customer or on behalf of the customer, or delivered electronically through the customer, shall depend upon the method of delivery of the service and the nature of the customer. Separate rules of assignment shall 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.

(b) If a rule of assignment set forth in this Section depends upon 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 a business customer, the taxpayer shall treat the customer as a business customer.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

**17 NCAC 05G .0903 DELIVERY TO OR ON BEHALF OF A CUSTOMER BY PHYSICAL MEANS, WHETHER TO AN INDIVIDUAL OR BUSINESS CUSTOMER**

(a) Services delivered to a customer or on behalf of a customer through a physical means include:

- (1) product delivery services where property is delivered to the customer or to a third party on behalf of the customer;
- (2) delivery of brochures, fliers, or other direct mail services;
- (3) delivery of advertising or advertising-related services to the customer's intended audience in the form of a physical medium; and
- (4) sale of custom software, such as 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.

(b) The following rules shall apply whether the taxpayer's customer is an individual customer or a business customer:

- (1) Rule of Determination. In assigning the receipts from a sale of a service delivered to a customer or on behalf of a customer through a physical means, a taxpayer shall 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.
- (2) Rule of Reasonable Approximation. If the taxpayer is unable to determine the state or states where the service is delivered, but has sufficient information regarding the place of delivery that the taxpayer may

reasonably approximate the state or states where the service is delivered, it shall reasonably approximate the state or states.

*History Note: Authority G.S. 105-130.4; S.L. 2016-94; Eff. January 1, 2020 (See S.L. 2019-246, s. 3).*

**17 NCAC 05G .0904 DELIVERY TO CUSTOMER BY ELECTRONIC TRANSMISSION**

(a) Services delivered by electronic transmission include 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.

(b) When a service is delivered by electronic transmission to a customer, the following rules apply:

- (1) Services Delivered By Electronic Transmission to an Individual Customer.
  - (A) Rule of Determination. When a service is delivered to an individual customer by electronic transmission, the service is delivered in North Carolina to the extent that the taxpayer's customer received the service in North Carolina. If the taxpayer is able to determine the state or states where the service is received, it shall assign the receipts from that sale to that state or states.
  - (B) Rules of Reasonable Approximation. If the taxpayer is unable to determine the state or states where the customer received the service, but has sufficient information regarding the place of receipt to 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 to determine or reasonably approximate the state or states where the service is received, it shall reasonably approximate the state or states using the customer's billing address.
- (2) Services Delivered By Electronic Transmission to a Business Customer.
  - (A) Rule of Determination. When a service is delivered to a business customer by electronic transmission, the service is delivered in North Carolina to the extent that the taxpayer's customer received 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 Rule, the state or states where the service is received shall reflect the location where the service was directly used by the employees or designees of the customer.
  - (B) Rule of Reasonable Approximation. If the taxpayer is unable to determine the state or states where the customer received the service, but has sufficient information regarding the place of receipt to reasonably approximate the state or states where the service is received, it shall reasonably approximate the state or states.
  - (C) Secondary Rule of Reasonable Approximation. When a service is delivered to a business customer by electronic transmission where a taxpayer does not have sufficient information to determine or reasonably approximate the state or states where the service is received, the taxpayer shall reasonably approximate the state or states as set forth in this Rule. In these cases, unless the taxpayer uses the safe harbor set forth in Part (D) of this Subparagraph, the taxpayer shall reasonably approximate the state or states where 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. However, if the taxpayer derives more than five percent of its receipts from sales of services from any single customer, the taxpayer shall identify the state where the contract of sale is principally managed by that customer.
  - (D) Safe Harbor. When a service is delivered to a business customer by electronic transmission, a taxpayer may not be able to determine, or reasonably approximate under Part (B) of this Subparagraph, the state or states where the service is received. In these cases, the taxpayer may, in lieu of the rule stated in Part (C) of this Subparagraph, apply the safe harbor stated in this Sub-Item. 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 where the taxpayer engages in substantially similar service transactions with more than 250 customers, whether business or individual, and does not derive more than five percent of its receipts from sales of all services from that customer.

- (E) Related Entity Transactions. When a service is delivered by electronic transmission to a business customer that is a related entity, the taxpayer may not use the secondary rule of reasonable approximation in Part (C) of this Subparagraph but may use the rule of reasonable approximation in Part (B) of this Subparagraph, and the safe harbor in Part (D) of this Subparagraph. The Secretary may aggregate sales to related entities in determining whether the sales exceed five percent of receipts from sales of all services under that safe harbor provision.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

#### **17 NCAC 05G .0905 SERVICES DELIVERED ELECTRONICALLY THROUGH OR ON BEHALF OF AN INDIVIDUAL OR BUSINESS CUSTOMER**

When a service is delivered electronically "on behalf of" or "through" a customer as defined in Rule .0901 of this Subchapter, the methodology provided under this Rule applies.

- (1) 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 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 Sub-Item apply whether the taxpayer's customer is an individual customer or a business customer and whether the end users or other third-party recipients to which the services are delivered through or on behalf of the customer are individuals or businesses.
- (2) Rule of Reasonable Approximation. If the taxpayer cannot determine the state or states where the services are actually delivered to the end users or other third-party recipients either through or on behalf of the customer, but has sufficient information regarding the place of delivery that the taxpayer may reasonably approximate the state or states where the services are delivered, it shall reasonably do so.
  - (3) Select Secondary Rules of Reasonable Approximation.
    - (a) If a taxpayer's service is the direct or indirect electronic delivery of advertising on behalf of its customer to the customer's intended audience, and if the taxpayer lacks sufficient information regarding the location of the audience that the taxpayer may 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 where 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 where the advertising is delivered relative to the total population in that area.
    - (b) 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, and the taxpayer lacks sufficient information regarding the location of the end users or other third party recipients that the taxpayer may 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 where the taxpayer's intermediary resells the services, relative to the total population in that area.
    - (c) When using the secondary reasonable approximation methods provided in Sub-items (3)(a) or (b), 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 shall be presumed that the area where the service was substantially and materially delivered or resold does not include areas outside the United States.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

## **SECTION .1000 - PROFESSIONAL SERVICES**

### **17 NCAC 05G .1001 IN GENERAL**

(a) Except as otherwise provided in this Subchapter, "professional services" are services that require specialized knowledge and may require a professional certification, license, or degree. These services include the performance of technical services that require the application of specialized knowledge.

(b) Professional services include:

- (1) management services;
- (2) bank and financial services;
- (3) financial custodial services;
- (4) investment and brokerage services;
- (5) fiduciary services;
- (6) tax preparation;
- (7) payroll and accounting services;
- (8) lending services;
- (9) credit card services, including credit card processing services;
- (10) data processing services;
- (11) legal services;
- (12) consulting services;
- (13) video production services;
- (14) graphic and other design services;
- (15) engineering services; and
- (16) architectural services.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

### **17 NCAC 05G .1002 OVERLAP WITH OTHER CATEGORIES OF SERVICES**

(a) Certain services that fall within the definition of "professional services" set forth in this Section shall be treated as "in-person services" within the meaning of Section .0800 of this Subchapter, and shall be assigned under the rules of that Section. Specifically, professional services that are physically provided in person by the taxpayer such as carpentry, certain medical and dental services, or child care services when 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 shall be assigned as such, notwithstanding that they may also be considered to be "professional services."

(b) Professional services where the service is of an intellectual or intangible nature, such as legal, accounting, financial, and consulting services, shall be assigned as professional services under the rules of this Section, notwithstanding the fact that these services may involve some amount of in-person contact.

(c) Professional services may include the transmission of documents or other communications by mail or by electronic means. In these cases, the assignment rules that apply are those set forth in this Section, and not those set forth in Section .0900 of this Subchapter, pertaining to services delivered to a customer or through or on behalf of a customer.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94.  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

### **17 NCAC 05G .1003 ASSIGNMENT OF RECEIPTS**

The location of delivery of professional services shall not be determined by a general rule of determination, but shall be reasonably approximated. The assignment of receipts from a sale of a professional service depends on whether the customer is an individual or a business customer. When the taxpayer, acting in good faith, cannot reasonably determine whether the customer is an individual or a 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.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

#### **17 NCAC 05G .1004 PROFESSIONAL SERVICES OTHER THAN ARCHITECTURAL OR ENGINEERING SERVICES**

Receipts from sales of professional services other than those services described in Rules .1005 - .1006 of this Section, shall be assigned as follows:

- (1) Professional Services Delivered to Individual Customers. Except as otherwise provided in Section .1000 of this Subchapter, in any instance where the service provided is a professional service and the taxpayer's customer is an individual customer, the state or states where the service is delivered shall be reasonably approximated as set forth in this Rule. 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. However, when the taxpayer derives more than five percent of its receipts from sales of all services from an individual customer, the taxpayer shall identify the customer's state of primary residence and assign the receipts from the service or services provided to that customer to that state.
- (2) Professional Services Delivered to Business Customers. When the taxpayer provides a professional service to a business customer, the state or states where the service is delivered shall be reasonably approximated as set forth in this Rule. Unless the taxpayer uses the safe harbor set forth in Item (3) of this Rule, the taxpayer shall assign the receipts from the sale as follows:
  - (a) by assigning the receipts to the state where the contract of sale is principally managed by the customer;
  - (b) if the place of customer management is not reasonably determinable, to the customer's place of order; and
  - (c) if the customer place of order is not reasonably determinable, to the customer's billing address. When the taxpayer derives more than five percent of its receipts from sales of all services from a customer, the taxpayer is required to identify the state where the contract of sale is principally managed by the customer.
- (3) Safe Harbor; Large Volume of Transactions. Notwithstanding the rules set forth in Items (1) and (2) of this Rule, a taxpayer may assign its receipts from sales to a particular customer based on the customer's billing address in any taxable year when the taxpayer engages in substantially similar service transactions with more than 250 customers, whether individual or business, and does not derive more than five percent of its receipts from sales of all services from that customer.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

#### **17 NCAC 05G .1005 ARCHITECTURAL OR ENGINEERING SERVICES WITH RESPECT TO REAL OR TANGIBLE PERSONAL PROPERTY**

- (a) Architectural and engineering services with respect to real or tangible personal property shall be professional services within the meaning of this Section. The receipts from a sale of an architectural service shall be assigned to a state or states to the extent that the services are with respect to real estate improvements located, or expected to be located, in the state or states. The receipts from a sale of an engineering service shall be assigned to a state or states 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.
- (b) This Rule shall apply whether or not the customer is an individual or business customer. In any instance in which architectural or engineering services are not described in this Rule, the receipts from a sale of these services shall be assigned under Rule .1004 of this Section.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

#### **17 NCAC 05G .1006 RELATED ENTITY TRANSACTIONS**

When the professional service is sold to a related entity, rather than applying the rule for professional services delivered to business customers in Rule .1004(2) of this Section, the state or states where the service is assigned is the place of receipt by the related entity as reasonably approximated using the following hierarchy:

- (1) if the service primarily relates to specific operations or activities of a related entity conducted in one or more locations, then to the state or states where those operations or activities are conducted in proportion to the related entity's payroll at the locations to which the service relates in the state or states; or
- (2) if the service does not primarily relate to specific operations or activities of a related entity conducted in particular locations, but instead relates to the operations of the related entity generally, then to the state or states where the related entity has employees, in proportion to the related entity's payroll in those states. The taxpayer may use the safe harbor provided by Rule .1004(3) of this Section.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

## **SECTION .1100 – LICENSE OR LEASE OF INTANGIBLE PROPERTY**

### **17 NCAC 05G .1101 IN GENERAL**

- (a) The receipts from the license of intangible property shall be assigned to North Carolina to the extent the intangible is used in North Carolina. The term "use" shall refer to the location of the taxpayer's market for the use of the intangible property that is being licensed and shall not refer to the location of the property or payroll of the taxpayer. This Section sets forth the rules to determine the location of the use of intangible property for several specific types of licensing transactions.
- (b) A license of intangible property that conveys all substantial rights in that property shall be treated as a sale of intangible property for purposes of these rules. For purposes of Sections .1100 and .1200, a sale or exchange of intangible property shall be 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 shall be treated under these rules as the sale or lease of tangible property.
- (d) Nothing in this Section 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 G.S. 105-130.4, or that are excluded from the numerator and the denominator of the sales factor pursuant to G.S. 105-130.4(1)(6). To the extent that the transfer of either a security or business "goodwill" or similar intangible value, including "going concern value" or "workforce in place," is 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.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

### **17 NCAC 05G .1102 LICENSE OF A MARKETING INTANGIBLE**

- (a) If a license is granted for the right to use intangible property in connection with the sale, lease, license, or other marketing of goods, services, or other items, such as a marketing intangible, to a consumer, the royalties or other licensing fees paid by the licensee for that marketing intangible shall be 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 in North Carolina.
- (b) License of a marketing intangible includes the following when it is intended to promote consumer sales:
  - (1) the license of a service mark, trademark, or trade name;
  - (2) copyrights;
  - (3) the license of a film, television or multimedia production or event for commercial distribution; and
  - (4) a franchise agreement.
- (c) 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 shall 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 where 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.

(d) 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 shall 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 where 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 shall be presumed to be derived from within the United States.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

#### **17 NCAC 05G .1103 LICENSE OF A PRODUCTION INTANGIBLE**

(a) Where 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 will be used in a production capacity (a "production intangible"), the licensing fees paid by the licensee for that right shall be assigned to North Carolina to the extent that the use for which the fees are paid takes place in North Carolina.

(b) License of a production intangible includes 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.

(c) Where the actual use of intangible property pursuant to a license of a production intangible takes place in part in North Carolina, the entire use shall be in this State except to the extent that the taxpayer is able to demonstrate that the actual location of a portion of the use takes place outside North Carolina.

(d) When a license of a production intangible to a related entity, the taxpayer shall assign the receipts to where the intangible property is actually used. When a license of a production intangible to a party other than a related entity where the location of actual use is unknown, the use of the intangible property takes place in the state of the licensee's commercial domicile when a business, or the licensee's state of primary residence when an individual.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

#### **17 NCAC 05G .1104 LICENSE OF A MIXED INTANGIBLE**

Where a license of intangible property includes both a license of a marketing intangible and a license of a production intangible (a "mixed intangible") and the fees to be paid in each instance are separately and reasonably stated in the licensing contract, the Secretary shall accept that separate statement for purposes of these Rules. 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, the licensing fees were paid entirely for the license of the marketing intangible, except to the extent that the taxpayer can reasonably establish otherwise.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

#### **17 NCAC 05G .1105 LICENSE OF INTANGIBLE PROPERTY WHEN SUBSTANCE OF THE TRANSACTION RESEMBLES A SALE OF GOODS OR SERVICES**

(a) When the license of intangible property resembles the sale of an electronically-delivered good or service, rather than the license of a marketing intangible or production intangible, the receipts shall be assigned by applying Rules .0904 and .0905 of this Subchapter. Transactions to be assigned under this Rule include the license of:

- (1) database access;
- (2) access to information;
- (3) digital goods; and
- (4) certain software, where the transaction is not the license of pre-written software treated as the sale of tangible personal property.

(b) Sublicenses. The provisions of Rule .0905 of this Subchapter shall 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. Rule .0905 of this Subchapter shall 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 shall 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 where the sublicense transfers a reduced bundle of rights with respect to that property, such as when 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.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

## **SECTION .1200 – SALE OF INTANGIBLE PROPERTY**

### **17 NCAC 05G .1201 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, 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.

- (1) 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 shall be assigned to a state 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.
- (2) In the case of a sale or exchange of intangible property where the receipts from the sale or exchange are contingent on the productivity, use, or disposition of the property, the receipts from the sale shall be assigned by applying the rules set forth in Section .1100 of this Subchapter.
- (3) In the case of a sale or exchange of intangible property where the substance of the transaction resembles a sale of goods or services and where the receipts from the sale or exchange do not derive from payments contingent on the productivity, use, or disposition of the property, the receipts from the sale shall be assigned by applying the rules set forth in Rule .1105 of this Subchapter.
- (4) Receipts from the sale of intangible property shall not be included in the sales factor in any case when the sale does not give rise to receipts within the meaning of Rule .0401 of this Subchapter. In addition, in any case where the sale of intangible property results in receipts within the meaning of Section .0400 of this Subchapter, those receipts shall be excluded from the numerator and the denominator of the taxpayer's sales factor if the receipts are not referenced in G.S. 105.130.4(l). The sale of intangible property that is excluded from the numerator and denominator of the taxpayer's sales factor under this provision includes the sale of business "goodwill," the sale of an agreement not to compete, or similar intangible value.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

## **SECTION .1300 – SPECIAL RULES**

### **17 NCAC 05G .1301 SOFTWARE TRANSACTIONS**

(a) 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 shall be 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 shall be in North Carolina as determined under the rules for the sale of tangible personal property set forth under G.S. 105-130.4 and the rules of this Subchapter.

(b) In all other cases, the receipts from a license or sale of software shall be assigned to North Carolina as determined otherwise under this Subchapter. This determination shall be based on the facts, and:

- (1) the development and sale of custom software as set forth in Section .0900 of this Subchapter;
- (2) the license of a marketing intangible, as set forth in Rule .1102 of this Subchapter;
- (3) the license of a production intangible, as set forth in Rule .1103 of this Subchapter;

- (4) the license of intangible property where the substance of the transaction resembles a sale of goods or services, as set forth in Rule .1105 of this Subchapter; or
- (5) as a sale of intangible property, as set forth in Rule .1201 of this Subchapter.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

### **17 NCAC 05G .1302 SALES OR LICENSES OF DIGITAL GOODS AND SERVICES**

The receipts from the sale or license of digital goods or services, including the sale of video, audio, and software products or similar transactions, shall be assigned by applying the same provisions set forth in Rules .0904 or .0905 of this Subchapter, as if the transaction was 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, the terms of the contractual relationship or the characterization of the sale or the license shall not be relevant.

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).

### **17 NCAC 05G .1303 TELECOMMUNICATIONS COMPANIES**

(a) When a taxpayer that provides telecommunications or ancillary services that are 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 shall be assigned pursuant to this Rule. The taxpayer shall apply Rules .0904 or .0905 of this Subchapter 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. Multistate Tax Commission Reg. IV.18(i) is hereby incorporated by reference, including subsequent amendments or additions, and is available free of charge at <http://www.mtc.gov/Uniformity/Adopted-Uniformity-Recommendations>.

(b) In applying these Rules, if the taxpayer cannot determine the state or states where a customer received the purchased product, the taxpayer 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, MTC Reg. IV.18(i).

*History Note:* Authority G.S. 105-130.4; S.L. 2016-94;  
Eff. January 1, 2020 (See S.L. 2019-246, s. 3).