

810-9-1-.05 Apportionment and Allocation of Net Income of Financial Institutions.

(1) SCOPE. This rule applies to financial institutions subject to the Alabama financial institution excise tax and to any determination of net income from multistate operations to which Section 40-16-1, Code of Alabama 1975, applies and to the related supporting statements required to be filed pursuant to the Department's authority under Section 40-16-3.

(2) APPORTIONMENT AND ALLOCATION.

(a) Business and Nonbusiness Income Defined.

1. "Business income" is income arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, management, and disposition of the property constitute integral parts of the taxpayer's regular trade or business operations. In essence, all income which arises from the conduct of trade or business operations of a taxpayer is business income. For purposes of administration of Section 40-16-1, the income of the taxpayer is business income unless clearly classifiable as nonbusiness income.

2. Nonbusiness income means all income other than business income.

3. The classification of income by the labels occasionally used, such as manufacturing income, compensation for services, sales income, interest, dividends, rents, royalties, gains, operating income, nonoperating income, etc., is of no aid in determining whether income is business or non-business income. Income of any type or class and from any source is business income if it arises from transactions and activity occurring in the regular course of a trade or business. Accordingly, the critical element in determining whether income is "business income" or "nonbusiness income" is the identification of the transactions and activity which are the elements of a particular trade or business. In general all transactions and activities of the taxpayer which are dependent upon or contribute to the operations of the taxpayer's economic enterprise as a whole constitute the taxpayer's trade or business and will be transactions and activity arising in the regular course of, and will constitute integral parts of, a trade or business.

(b) Business and Nonbusiness Income: Application of Definitions. The following are rules and examples for determining whether particular income is business or nonbusiness income:

1. Rents and Royalties from real and tangible personal property. Rental and royalty income from real and tangible property is business income if the property with respect to which the income was received is used in the taxpayer's trade or business

or incidental thereto and therefore is includable in the property factor under paragraph (5).

(i) EXAMPLE: The taxpayer is a financial institution and also operates a multistate car rental/leasing business. The income from car rentals/leases is business income.

(ii) EXAMPLE: The taxpayer is a multistate lender and also engages in the business of leasing heavy construction equipment such as cranes, tractors, and earth-moving vehicles. The rental income is business income.

(iii) EXAMPLE: The taxpayer operates a multistate chain of branch offices. The taxpayer purchases a five-story office building for use in connection with its trade or business. It uses the street floor as one of its public offices and the second and third floors for its general corporate headquarters. The taxpayer manages and leases the remaining two floors to others. The rental of the two floors is incidental to the operation of the taxpayer's trade or business. The rental income is business income.

(iv) EXAMPLE: The taxpayer operates a multistate chain of consumer loan offices. It purchases as an investment an office building in another state with surplus funds and hires an unrelated property management company to manage and lease the entire building to others. The net rental income is not business income of the loan trade or business. Therefore, the net rental income is nonbusiness income.

(v) EXAMPLE: The taxpayer is a bank and operates branch offices in several states. The taxpayer invests in a 20-story office building and uses the street floor as one of its branch offices and the second floor for its general corporate headquarters. The taxpayer hires an unrelated property management company to manage and lease the remaining 18 floors to others. The rental of the eighteen floors is not incidental to but rather is separate from the operation of the taxpayer's trade or business. The net rental income is not business income of the banking trade or business. Therefore, the net rental income is nonbusiness income.

(vi) EXAMPLE: The taxpayer constructed a branch office for use in its multistate banking business and 20 years later the branch was closed and put up for sale. The branch office was rented for a temporary period from the time it was closed by the taxpayer until it was sold 18 months later. The rental income is business income and the gain on the sale of the plant is business income.

(vii) EXAMPLE: The taxpayer operates a multistate chain of loan offices. It owned an office building, which it occupied as its corporate headquarters. Because of inadequate space, the taxpayer acquired a new and larger building elsewhere for its corporate headquarters. The taxpayer hired an unrelated property management company to manage and lease the old building. The property management company leased the building to an unrelated investment company under a five-year lease. Upon expiration of the lease, taxpayer sold the building at a gain (or loss). The net

rental income received over the lease period is nonbusiness income and the gain (or loss) on the sale of the building is nonbusiness income.

(viii) EXAMPLE: The taxpayer acquires undeveloped land for future expansion of its multistate lending business. The expansion plans are later discarded and mineral rights under the land are leased to others. The corporation receives royalties based on units extracted. The royalty income is nonbusiness income.

2. Gains or losses from sales of assets. Gain or loss from the sale, exchange or other disposition of real property or of tangible or intangible personal property constitutes business income if the property while owned by the taxpayer was used in the taxpayer's trade or business. However, if the property was utilized for the production of nonbusiness income or otherwise was removed from the property factor before its sale, exchange or other disposition, the gain or loss will constitute nonbusiness income.

(i) EXAMPLE: In conducting its multistate banking business, the taxpayer systematically replaces automobiles, machines, and other equipment used in the business. The gains or losses resulting from those sales constitute business income.

(ii) EXAMPLE: The taxpayer constructed a building for use in its multistate lending business and 20 years later sold the property at a gain while it was in operation by the taxpayer. The gain is business income.

(iii) EXAMPLE: Same as (ii) except that the building was closed and put up for sale but was not in fact sold until a buyer was found 18 months later. The gain is business income.

(iv) EXAMPLE: Same as (ii) except that the building was rented while being held for sale. The rental income is business income and the gain on the sale of the building is business income.

(v) EXAMPLE: The taxpayer operates a multistate chain of branch banking offices. It owned an office building, which it occupied as its corporate headquarters. Because of inadequate space, taxpayer acquired a new and larger building elsewhere for its corporate headquarters. The taxpayer hired an unrelated property management company to manage and lease the old building. The property management company leased the building to an unrelated investment company under a five-year lease. Upon expiration of the lease, taxpayer sold the building at a gain (or loss). The gain (or loss) on the sale is nonbusiness income and the rental income received over the lease period is nonbusiness income.

(vi) EXAMPLE: The taxpayer is a multistate lender and also issues credit cards. The taxpayer sells its loans and credit card accounts receivable. The gain or loss is business income.

3. Interest. Interest income is business income where the intangible with respect to which the interest was received arises out of or was created in the regular course of the taxpayer's trade or business operations or where the purpose for acquiring and holding the intangible is related to or incidental to such trade or business operations.

(i) EXAMPLE: The taxpayer is a multistate mortgage lender and also issues credit cards. The taxpayer receives interest income from its secured and unsecured loans. These amounts are business income.

(ii) EXAMPLE: The taxpayer conducts a multistate lending business. During the year the taxpayer receives a federal income tax refund and collects a judgment against a debtor of the business. Both the tax refund and the judgment bear interest. The interest income is business income.

(iii) EXAMPLE: The taxpayer is engaged in a multistate lending and financing business. In connection with that business, the taxpayer maintains special accounts to cover such items as workmen's compensation claims, rain and storm damage, machinery replacement, etc. The moneys in those accounts are invested at interest. Similarly, the taxpayer temporarily invests funds intended for payment of federal, state and local tax obligations. The interest income is business income.

(iv) EXAMPLE: The taxpayer is engaged in a multistate money order and traveler's check business. In addition to the fees received in connection with the sale of the money orders and traveler's checks, the taxpayer earns interest income by the investment of the funds pending their redemption. The interest income is business income.

(v) EXAMPLE: The taxpayer is engaged in a multistate banking business. The taxpayer usually has working capital and extra cash totaling \$200,000.00 which it regularly invests in short-term interest bearing securities. The interest income is business income.

(vi) EXAMPLE: In January, the taxpayer sold all of the stock of a subsidiary not involved in the same trade or business of the taxpayer for \$20,000,000. The funds are placed in an interest-bearing account pending a decision by management as to how the funds are to be utilized. The interest income is nonbusiness income.

4. Dividends. Dividends are business income where the stock with respect to which the dividends are received arises out of or was acquired in the regular course of the taxpayer's trade or business operations or where the purpose of acquiring and holding the stock is related to or incidental to such trade or business operations.

(i) EXAMPLE: The taxpayer operates a multistate chain of stock brokerage houses. During the year, the taxpayer receives dividends on stock that it owns. The dividends are business income.

(ii) EXAMPLE: The taxpayer is engaged in a multistate lending business. In connection with that business, the taxpayer maintains special accounts to cover such items as workmen's compensation claims, etc. A portion of the moneys in those accounts is invested in interest-bearing bonds. The remainder is invested in various common stocks listed on national stock exchanges. Both the interest income and any dividends are business income.

(iii) EXAMPLE: The taxpayer and several unrelated corporations own all of the stock of a corporation whose business operations consist solely of providing services or products for delivery or use to or by the corporate owners. The taxpayer acquired the stock in order to obtain a resource for services or products for use in its business. The dividends are business income.

(iv) EXAMPLE: The taxpayer is engaged in a multistate banking business. The taxpayer is chartered under the auspices of the federal government and/or various state governments. Under state and federal laws applicable to the taxpayer, the taxpayer must maintain minimum ratios of certain assets to liability in order to comply with regulatory rules. As a result the taxpayer holds various stocks and interest-bearing securities. Both the interest income and any dividends received are business income.

(v) EXAMPLE: The taxpayer receives dividends from the stock of its subsidiary or affiliate which acts as the marketing agency for products manufactured for or services provided to the taxpayer. The dividends are business income.

5. Patent and copyright royalties. Patent and copyright royalties are business income where the patent or copyright with respect to which the royalties were received arises out of or was created in the regular course of the taxpayer's trade or business operations or where the purpose for acquiring or holding the patent or copyright is related to or incidental to such trade or business operations.

(i) EXAMPLE: The taxpayer is engaged in the multistate business of banking. In connection with that business, the taxpayer obtained patents and copyrights, directly or indirectly, in the course of making loans to customers. The royalties received by the taxpayer are business income.-

(c) Proration of Deductions. In most cases, an allowable deduction of a taxpayer will be applicable to only the business income arising from a particular trade or business or to a particular item of nonbusiness income. In some cases, an allowable deduction may be applicable to business income or several items of nonbusiness income. In such cases, the deduction shall be prorated among those items of nonbusiness income in a manner which fairly distributes the deduction among the classes of income to which it is applicable. Any allowable deduction that is applicable both to business and nonbusiness income of the taxpayer shall be

prorated to each class of income in determining income subject to tax as provided below:

1. Interest Expense. Interest expense shall be prorated to nonbusiness assets by multiplying total interest expense by the ratio of average cost of the nonbusiness assets to the average cost of the total assets. If any assets were acquired with stock of the taxpayer corporation, the value of such assets to the extent attributed to the taxpayer's stock shall be excluded from the computations.

2. Other Expenses. Other type expenses applicable both to business and nonbusiness income shall be prorated in such a manner as to equitably assign such expenses to business or nonbusiness categories, as appropriate.

3. Year to year consistency. In filing returns with this state, if the taxpayer departs from or modifies the manner of prorating any such deduction used in returns for prior years, the taxpayer shall disclose in the return for the current year the nature and extent of the modification.

4. State to state consistency. If the returns or reports filed by a taxpayer with all states to which the taxpayer reports under the Recommended Formula for the Apportionment and Allocation Of Net Income of Financial Institutions, as adopted November 17, 1994, are not uniform in the application or proration of any deduction, the taxpayer shall disclose in its return to this state the nature and extent of the variance.

(d) Except as otherwise specifically provided, a financial institution whose business activity is taxable both within and without this state shall allocate and apportion its net income as provided in this rule. All items of nonbusiness income (income which is not includable in the apportionable income tax base) shall be allocated pursuant to the provisions of Paragraph (7) of this rule. A financial institution organized under the laws of a foreign country, the Commonwealth of Puerto Rico, or a territory or possession of the United States whose effectively connected income (as defined under the Federal Internal Revenue Code) is taxable both within this state and within another state, other than the state in which it is organized, shall allocate and apportion its net income as provided in this rule.

(e) All business income (income which is includable in the apportionable income tax base) shall be apportioned to this state by multiplying such income by the apportionment percentage. The apportionment percentage is determined by adding the taxpayer's receipts factor (as described in Paragraph (4) of this rule), property factor (as described in Paragraph (5) of this rule), and payroll factor (as described in Paragraph (6) of this rule) together and dividing the sum by three. If one of the factors is missing, the two remaining factors are added and the sum is divided by two. If two of the factors are missing, the remaining factor is the apportionment percentage. A factor is missing if both its numerator and denominator are zero, but it is not missing merely because its numerator is zero.

(f) Each factor shall be computed according to the method of accounting (cash or accrual basis) used by the taxpayer for the taxable year.

(g) If the allocation and apportionment provisions of this rule do not fairly represent the extent of the taxpayer's business activity in this state, the taxpayer may petition for or the Commissioner may require, in respect to all or any part of the taxpayer's business activity, if reasonable:

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 an equitable allocation and apportionment of the taxpayer's income.

(3) DEFINITIONS. As used in this rule, unless the context otherwise requires:

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

(b) Borrower or credit card holder located in this state.

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

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

(d) Commercial domicile.

1. The headquarters of the trade or business, that is, the place from which the trade or business is principally managed and directed; or
2. if a taxpayer is organized under the laws of a foreign country, or of the Commonwealth of Puerto Rico, or any territory or possession of the United States, such taxpayer's commercial domicile shall be deemed for the purposes of this rule to

be the state of the United States or the District of Columbia from which such taxpayer's trade or business in the United States is principally managed and directed. It shall be presumed, subject to rebuttal, that the location from which the taxpayer's trade or business is principally managed and directed is the state of the United States or the District of Columbia to which the greatest number of employees are regularly connected or out of which they are working, irrespective of where the services of such employees are performed, as of the last day of the taxable year.

(e) Compensation. Wages, salaries, commissions and any other form of remuneration paid to employees for personal services that are included in such employee's gross income 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 payments would constitute gross income to such employees under the Federal Internal Revenue Code shall be made as though such employees were subject to the Federal Internal Revenue Code.

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

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

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

(i) Gross rents. The actual sum of money or other consideration payable for the use or possession of property. "Gross rents" shall include, but not be limited to:

1. any amount payable for the use or possession of real property or tangible property whether designated as a fixed sum of money or as a percentage of receipts, profits or otherwise,

2. any amount payable as additional rent or in lieu of rent, such as interest, taxes, insurance, repairs or any other amount required to be paid by the terms of a lease or other arrangement, and

3. a proportionate part of the cost of any improvement to real property made by or on behalf of the taxpayer which reverts to the owner or lessor upon termination of a lease or other arrangement. The amount to be included in "gross rents" is the amount of amortization or depreciation allowed in computing the taxable income base for the taxable year. However, where a building is erected on leased land by or on behalf of the taxpayer, the value of the land is determined by multiplying the gross rent by eight and the value of the building is determined in the same manner as if owned by the taxpayer.

4. The following are not included in the term “gross rents”:

(i) reasonable amounts payable as separate charges for water and electric service furnished by the lessor;

(ii) reasonable amounts payable as service charges for janitorial services furnished by the lessor;

(iii) reasonable amounts payable for storage, provided such amounts are payable for space not designated and not under the control of the taxpayer; and

(iv) that portion of any rental payment which is applicable to the space subleased from the taxpayer and not used by it.

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

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

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

(m) Participation. An extension of credit in which an undivided ownership interest is held on a pro rata basis in a single loan or pool of loans and related collateral. In a loan participation, the credit originator initially makes the loan and then subsequently resells all or a portion of it to other lenders. The participation may or may not be known to the borrower.

(n) Person. An individual, estate, trust, partnership, corporation and any other business entity.

(o) Principal base of operations.

1. With respect to transportation property, the place of more or less permanent nature from which said property is regularly directed or controlled.

2. With respect to an employee, the place of more or less permanent nature from which the employee regularly:

(i) starts his or her work and to which he or she customarily returns in order to receive instructions from his or her employer, or

(ii) communicates with his or her customers or other persons, or

(iii) performs any other functions necessary to the exercise of his or her trade or profession at some other point or points.

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

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

(r) State. A state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, any territory or possession of the United States or any foreign country.

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

(t) Taxable. When either:

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

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

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

(4) RECEIPTS FACTOR.

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

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

(c) Receipts from the lease of tangible personal property.

1. Except as described in subparagraph 2. of this subparagraph, the numerator of the receipts factor includes receipts from the lease or rental of tangible personal property owned by the taxpayer if the property is located within this state when it is first placed in service by the lessee.

2. Receipts from the lease or rental of transportation property owned by the taxpayer are included in the numerator of the receipts factor to the extent that the property is used in this state. The extent an aircraft will be deemed to be used in this state and the amount of receipts that is to be included in the numerator of this state's receipts factor is determined by multiplying all the receipts from the lease or rental of the aircraft by a fraction, the numerator of which is the number of landings of the aircraft in this state and the denominator of which is the total number of landings of the aircraft. If the extent of the use of any transportation property within this state cannot be determined, then the property will be deemed to be used wholly in the state in which the property has its principal base of operations. A motor vehicle will be deemed to be used wholly in the state in which it is registered.

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

1. The numerator of the receipts factor includes interest, fees, and penalties imposed in connection with loans secured by real property if the property is located within this state. If the property is located both within this state and one or more other states, the receipts described in this subparagraph are included in the numerator of the receipts factor if more than fifty percent of the fair market value of the real property is located within this state. If more than fifty percent of the fair market value of the real property is not located within any one state, then the receipts described in this subparagraph shall be included in the numerator of the receipts factor if the borrower is located in this state.

2. The determination of whether the real property securing a loan is located within this state shall be made as of the time the original agreement was made and any and all subsequent substitutions of collateral shall be disregarded.

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

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

1. The amount of net gains (but not less than zero) from the sale of loans secured by real property included in the numerator is determined by multiplying such net gains by a fraction the numerator of which is the amount included in the numerator of the receipts factor pursuant to subparagraph (d) of this paragraph and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans secured by real property.

2. The amount of net gains (but not less than zero) from the sale of loans not secured by real property included in the numerator is determined by multiplying such net gains by a fraction the numerator of which is the amount included in the numerator of the receipts factor pursuant to subparagraph (e) of this paragraph and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans not secured by real property.

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

(h) Net gains from the sale of credit card receivables. The numerator of the receipts factor includes net gains (but not less than zero) from the sale of credit card receivables multiplied by a fraction, the numerator of which is the amount

included in the numerator of the receipts factor pursuant to subparagraph (g) of this paragraph and the denominator of which is the taxpayer's total amount of interest and fees or penalties in the nature of interest from credit card receivables and fees charged to card holders.

(i) Card issuer's reimbursement fees. The numerator of the receipts factor includes:

(I) all credit card issuer's reimbursement fees multiplied by a fraction, the numerator of which is the amount of fees, interest, and penalties charged to credit card holders included in the numerator of the receipts factor pursuant to subparagraph (g) of this paragraph and the denominator of which is the taxpayer's total amount of fees, interest, and penalties charged to credit card holders.

(II) all debit card issuer's reimbursement fees multiplied by a fraction, the numerator of which is the amount of fees, interest, and penalties charged to debit card holders included in the numerator of the receipts factor pursuant to subparagraph (g) of this paragraph and the denominator of which is the taxpayer's total amount of fees, interest, and penalties charged to debit card holders.

(III) all other card issuer's reimbursement fees multiplied by a fraction, the numerator of which is the amount of fees, interest, and penalties charged to all other card holders included in the numerator of the receipts factor pursuant to subparagraph (g) of this paragraph and the denominator of which is the taxpayer's total amount of fees, interest, and penalties charged to all other card holders.

(j) Receipts from merchant discount.

1. If the taxpayer can readily determine the location of the merchant and if the merchant is in this state, the numerator of the receipts factor includes receipts from merchant discount.

2. If the taxpayer cannot readily determine the location of the merchant, the numerator of the receipts factor includes such receipts from the merchant discount multiplied by a fraction:

(i) in the case of a merchant discount related to the use of a credit card, the numerator of which is the amount of fees, interest, and penalties charged to credit card holders that is included in the numerator of the receipts factor pursuant to subparagraph (g) of this paragraph and the denominator of which is the taxpayer's total amount of fees, interest, and penalties charged to credit card holding, and

(ii) in the case of a merchant discount related to the use of a debit card, the numerator of which is the amount of fees, interest, and penalties charged to

debit card holders that is included in the numerator of the receipts factor pursuant to subparagraph (g) of this paragraph, and the denominator of which is the taxpayer's total amount of fees, interest, and penalties charged to debit card holders.

(iii) in the case of a merchant discount related to the use of all other types of cards, the numerator of which is the amount of fees, interest, and penalties charged to all other card holders that is included in the numerator of the receipts factor pursuant to subparagraph (g) of this paragraph, and the denominator of which is the taxpayer's total amount of fees, interest, and penalties charged to all other card holders.

3. The taxpayer's method for sourcing each receipt from a merchant discount must be consistently applied to such receipt in all states that have adopted sourcing methods substantially similar to subparagraphs 1. and 2. of this paragraph and must be used on all subsequent returns for sourcing receipts from such merchant unless the Commissioner permits or requires application of the alternative method.

(k) Receipts from ATM fees. The receipts factor includes all ATM fees that are not forwarded directly to another bank.

1. The numerator of the receipts factor includes fees charged to a cardholder for the use at an ATM of a card issued by the taxpayer if the cardholder's billing address is in this state.

2. The numerator of the receipts factor includes fees charged to a cardholder, other than the taxpayer's cardholder, for the use of such card at an ATM owned or rented by the taxpayer, if the ATM is in the state.

(l) Loan servicing fees.

1. The numerator of the receipts factor includes:

(i) loan servicing fees derived from loans secured by real property multiplied by a fraction the numerator of which is the amount included in the numerator of the receipts factor pursuant to subparagraph (d) of this paragraph and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans secured by real property, and

(ii) loan servicing fees derived from loans not secured by real property multiplied by a fraction the numerator of which is the amount included in the numerator of the receipts factor pursuant to subparagraph (e) of this paragraph and the denominator of which is the total amount of interest and fees or penalties in the nature of interest from loans not secured by real property.

2. In circumstances in which the taxpayer receives loan servicing fees for servicing either the secured or the unsecured loans of another, the numerator of the receipts factor shall include such fees if the borrower is located in this state.

(m) Receipts from services. The numerator of the receipts factor includes receipts from services not otherwise apportioned under this rule, which receipts shall be sourced in accordance with Alabama Administrative Rule 810-27-1-.17.

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

1. Interest, dividends, net gains (but not less than zero) and other income from investment assets and activities and from trading assets and activities that are reported on the taxpayer's financial statements, call reports, or similar reports shall be included in the receipts factor. Investment assets and activities and trading assets and activities include but are not limited to: investment securities; trading account assets; federal funds; securities purchased and sold under agreements to resell or repurchase; options; futures contracts; forward contracts; notional principal contracts such as swaps; equities; and foreign currency transactions. With respect to the investment and trading assets and activities described in subparagraphs (i) and (ii) of this paragraph, the receipts factor shall include the amounts described in such subparagraphs.

(i) The receipts factor shall include the amount by which interest from federal funds sold and securities purchased under resale agreements exceeds interest expense on federal funds purchased and securities sold under repurchase agreements.

(ii) The receipts factor shall include the amount by which interest, dividends, gains and other income from trading assets and activities, including but not limited to assets and activities in the matched book, in the arbitrage book, and foreign currency transactions, exceed amounts paid in lieu of interest, amounts paid in lieu of dividends, and losses from such assets and activities.

2. The numerator of the receipts factor includes interest, dividends, net gains (but not less than zero) and other income from investment assets and activities and from trading assets and activities described in subparagraph 1. of this subparagraph that are attributable to this state.

(i) The amount of interest, dividends, net gains (but not less than zero) and other income from investment assets and activities in the investment account to be attributed to this state and included in the numerator is determined by multiplying all such income from such assets and activities by a fraction, the numerator of which is the average value of such assets which are properly assigned to a regular place of business of the taxpayer within this state and the denominator of which is the average value of all such assets.

(ii) The amount of interest from federal funds sold and purchased and from securities purchased under resale agreements and securities sold under repurchase agreements attributable to this state and included in the numerator is determined by multiplying the amount described in subparagraph (i) of subparagraph 1. of this subparagraph from such funds and such securities by a fraction, the numerator of which is the average value of federal funds sold and securities purchased under agreements to resell which are properly assigned to a regular place of business of the taxpayer within this state and the denominator of which is the average value of all such funds and such securities.

(iii) The amount of interest, dividends, gains and other income from trading assets and activities, including but not limited to assets and activities in the matched book, in the arbitrage book and foreign currency transactions, (but excluding amounts described in subparagraphs (i) or (ii) of this subparagraph), attributable to this state and included in the numerator is determined by multiplying the amount described in subparagraph (ii) of subparagraph 1. of this subparagraph by a fraction, the numerator of which is the average value of such trading assets which are properly assigned to a regular place of business of the taxpayer within this state and the denominator of which is the average value of all such assets.

(iv) For purposes of this paragraph, average value shall be determined using the rules for determining the average value of tangible personal property set forth in subparagraphs (c) and (d) of Paragraph (5).

3. In lieu of using the method set forth in subparagraph 2. of this subparagraph, the taxpayer may elect, or the Commissioner may require in order to fairly represent the business activity of the taxpayer in this state, the use of the method set forth in this paragraph.

(i) The amount of interest, dividends, net gains (but not less than zero) and other income from investment assets and activities in the investment account to be attributed to this state and included in the numerator is determined by multiplying all such income from such assets and activities by a fraction, the numerator of which is the gross income from such assets and activities which are properly assigned to a regular place of business of the taxpayer within this state and the denominator of which is the gross income from all such assets and activities.

(ii) The amount of interest from federal funds sold and purchased and from securities purchased under resale agreements and securities sold under repurchase agreements attributable to this state and included in the numerator is determined by multiplying the amount described in subparagraph (i) of subparagraph 1. of this subparagraph from such funds and such securities by a fraction, the numerator of which is the gross income from such funds and such securities which are properly assigned to a regular place of business of the taxpayer within this state and the denominator of which is the gross income from all such funds and such securities.

(iii) The amount of interest, dividends, gains and other income from trading assets and activities, including but not limited to assets and activities in the matched book, in the arbitrage book and foreign currency transactions (but excluding amounts described in subparagraphs (i) or (ii) of this subparagraph), attributable to this state and included in the numerator is determined by multiplying the amount described in subparagraph (ii) of subparagraph 1. of this subparagraph by a fraction, the numerator of which is the gross income from such trading assets and activities which are properly assigned to a regular place of business of the taxpayer within this state and the denominator of which is the gross income from all such assets and activities.

4. If the taxpayer elects or is required by Commissioner to use the method set forth in subparagraph 3. of this subparagraph, it shall use this method on all subsequent returns unless the taxpayer receives prior permission from the Commissioner to use, or the Commissioner requires a different method.

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

(o) All other receipts. The numerator of the receipts factor includes all other receipts pursuant to the rules set forth in Alabama Administrative Rule 810-27-1-.16 and Alabama Administrative Rule 810-27-1-.17.

(p) Attribution of certain receipts to commercial domicile. All receipts which would be assigned under this rule to a state in which the taxpayer is not taxable shall be included in the numerator of the receipts factor, if the taxpayer's commercial domicile is in this state.

(5) PROPERTY FACTOR.

(a) General. The property factor is a fraction, the numerator of which is the average value of real property and tangible personal property rented to the taxpayer that is located or used within this state during the taxable year, and the average value of the taxpayer's loans and credit card receivables that are located within the state during the taxable year, and the average value of the taxpayer's real and tangible personal property owned that is located or used within this state during the taxable year, and

the denominator of which is the average value of all such property located or used within and without this state during the taxable year.

(b) Property included. The property factor shall include only property the income or expenses of which are included (or would have been included if not fully depreciated or expensed, or depreciated or expensed to a nominal amount) in the computation of the apportionable income base for the taxable year.

(c) Value of property owned by the taxpayer

1. The value of real property and tangible personal property owned by the taxpayer is the original cost or other basis of such property for Federal income tax purposes without regard to depletion, depreciation or amortization.

2. Loans are valued at their outstanding principal balance, without regard to any reserve for bad debts. If a loan is charged-off in whole or in part for Federal income tax purposes, the portion of the loan charged off is not outstanding. A specifically allocated reserve established pursuant to regulatory or financial accounting guidelines which is treated as charged-off for Federal income tax purposes shall be treated as charged-off for purposes of this paragraph.

3. Credit card receivables are valued at their outstanding principal balance, without regard to any reserve for bad debts. If a credit card receivable is charged-off in whole or in part for Federal income tax purposes, the portion of the receivable charged-off is not outstanding.

(d) Average value of property owned by the taxpayer. The average value of property owned by the taxpayer is computed on an annual basis by adding the value of the property on the first day of the taxable year and the value on the last day of the taxable year and dividing the sum by two. If averaging on this basis does not properly reflect average value, the Commissioner may require averaging on a more frequent basis. The taxpayer may elect to average on a more frequent basis. When averaging on a more frequent basis is required by the Commissioner or is elected by the taxpayer, the same method of valuation must be used consistently by the taxpayer with respect to property within and without this state and on all subsequent returns unless the taxpayer receives prior permission from the Commissioner or the Commissioner requires a different method of determining average value.

(e) Average value of real property and tangible personal property rented to the taxpayer.

1. The average value of real property and tangible personal property that the taxpayer has rented from another and which is not treated as property owned by the taxpayer for Federal income tax purposes, shall be determined annually by multiplying the "gross rents" payable during the taxable year by eight.

2. Where the use of the general method described in this subparagraph results in inaccurate valuations of rented property, any other method which properly reflects the value may be adopted by the Commissioner or by the taxpayer when approved in writing by the Commissioner. Once approved, such other method of valuation must be used on all subsequent returns unless the taxpayer receives prior approval from the Commissioner or the Commissioner requires a different method of valuation.

(f) Location of real property and tangible personal property owned by or rented to the taxpayer.

1. Except as described in subparagraph 2. of this subparagraph, real property and tangible personal property owned by or rented to the taxpayer is considered to be located within this state if it is physically located, situated or used within this state.

2. Transportation property is included in the numerator of the property factor to the extent that the property is used in this state. The extent an aircraft will be deemed to be used in this state and the amount of value that is to be included in the numerator of this state's property factor is determined by multiplying the average value of the aircraft by a fraction, the numerator of which is the number of landings of the aircraft in this state and the denominator of which is the total number of landings of the aircraft everywhere. If the extent of the use of any transportation property within this state cannot be determined, then the property will be deemed to be used wholly in the state in which the property has its principal base of operations. A motor vehicle will be deemed to be used wholly in the state in which it is registered.

(g) Location of loans. A loan is considered to be located in this state if the interest receipts associated with such loan are or would be sourced to this state pursuant to paragraph (4) RECEIPTS FACTOR of this rule.

(6) PAYROLL FACTOR.

(a) General. The payroll factor is a fraction, the numerator of which is the total amount paid in this state during the taxable year by the taxpayer for compensation and the denominator of which is the total compensation paid both within and without this state during the taxable year. The payroll factor shall include only that compensation which is included in the computation of the apportionable income tax base for the taxable year.

(b) Compensation relating to nonbusiness income and independent contractors. The compensation of any employee for services or activities which are connected with the production of nonbusiness income (income which is not includable in the apportionable income base) and payments made to any independent contractor or any other person not properly classifiable as an employee shall be excluded from both the numerator and denominator of the factor.

(c) When compensation paid in this state. Compensation is paid in this state if any one of the following tests, applied consecutively, is met:

1. The employee's services are performed entirely within this state.

2. The employee's services are performed both within and without the state, but the service performed without the state is incidental to the employee's service within the state. The term "incidental" means any service which is temporary or transitory in nature, or which is rendered in connection with an isolated transaction.

3. If the employee's services are performed both within and without this state, the employee's compensation will be attributed to this state:

(i) if the employee's principal base of operations is within this state; or

(ii) if there is no principal base of operations in any state in which some part of the services are performed, but the place from which the services are directed or controlled is in this state; or

(iii) if the principal base of operations and the place from which the services are directed or controlled are not in any state in which some part of the service is performed but the employee's residence is in this state.

(7) NONBUSINESS ALLOCATION. The various items of nonbusiness income, rents and royalties from real property or tangible personal property, capital gains, interest, dividends, or royalties from intangible property, to the extent that they constitute nonbusiness income, are directly allocated to specific jurisdictions as provided below:

(a) Rents and royalties from real property or tangible personal property.

1. Rental and royalty income from real and tangible property is business income if the property with respect to which the income was received is used in the taxpayer's trade or business or incidental thereto and therefore is includable in the property factor under this rule.

2. Net rents and royalties from real property located in this state are allocable to this state.

3. Net rents and royalties from tangible personal property are allocable to this state:

(i) if and to the extent that the property is utilized in this state, or

(ii) in their entirety if the taxpayer's commercial domicile is in this state and the taxpayer is not organized under the laws of or taxable in the state in which the property is utilized.

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

(b) Capital gains and losses.

1. Gain or loss from the sale, exchange or other disposition of real property or of tangible or intangible personal property constitutes business income if the property while owned by the taxpayer was used in the taxpayer's trade or business. However, if the property was utilized for the production of nonbusiness income or otherwise was removed from the property factor before its sale, exchange or other disposition, the gain or loss will constitute nonbusiness income.

2. Capital gains and losses from sales of real property located in this state are allocable to this state.

3. Capital gains and losses from sales of tangible personal property are allocable to this state if:

(i) the property had a situs in this state at the time of the sale, or

(ii) the taxpayer's commercial domicile is in this state and the taxpayer is not taxable in the state in which the property had a situs.

4. Capital gains and losses from sales of intangible personal property are allocable to this state if the taxpayer's commercial domicile is in this state.

(c) Interest and dividends.

1. Interest income is business income where the intangible with respect to which the interest was received arises out of or was created in the regular course of the taxpayer's trade or business operations or where the purpose for acquiring or holding the intangible is related to or incidental to such trade or business operations.

2. Dividends are business income where the stock with respect to which the dividends are received arises out of or was acquired in the regular course of the

taxpayer's trade or business operations or where the purpose of acquiring or holding the stock is related to or incidental to such trade or business operations.

3. Interest and dividends are allocable to this state if the taxpayer's commercial domicile is in this state.

(d) Royalties from intangible property.

1. Royalties are business income where the intangible property with respect to which the royalties were received arises out of or was created in the regular course of the taxpayer's trade or business operations or where the purpose for acquiring or holding the intangible property is related to or incidental to such trade or business operations.

2. Royalties from intangible property are allocable to this state:

(i) if and to the extent that the related intangible property is utilized by the payer in this state, or

(ii) if and to the extent that the related intangible property is utilized by the payer in a state in which the taxpayer is not taxable and the taxpayer's commercial domicile is in this state.

3. A patent is utilized in a state to the extent that it is employed in the production, fabrication, manufacturing, or other processing in the state or to the extent that a patented product is produced in the state. If the basis of receipts from patent royalties does not permit allocation to states or if the accounting procedures do not reflect states of utilization, the patent is utilized in the state in which the taxpayer's commercial domicile is located.

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

(8) APPLICABILITY. This rule without the amendments made in 2016 and further amended in 2017, shall apply to all operating years beginning after December 31, 1999, and before January 1, 2017. This rule, as amended in 2016 and as further amended in 2017, shall become effective December 31, 2017, and shall apply to all operating years beginning on or after January 1, 2017.

(a) Example. Bank B has an operating year that begins January 1, 2016 and ends December 31, 2016. Bank B operates in several states. Bank B will file its excise tax return for operating year 2016, on April 15, 2017, and use the rules of

allocation and apportionment contained in this rule without the amendments made in 2016 and 2017 to determine income attributable to this state. Bank C has an operating year that begins January 1, 2017, and ends December 31, 2017. Bank C operates in several states. Bank C will file its excise tax return for operating year 2017, on April 15, 2018, and use the rules of allocation and apportionment contained in this rule as amended in 2016 and 2017 to determine income attributable to this state.

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Authority: Sections 40-2A-7(a)(5), 40-16-1, and 40-16-4, **Code of Alabama 1975**.
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