

Insurance Code §2054.507 requires that, if a safety consultant identifies a hazardous condition or practice, an accident plan will be developed for the policyholder.

Labor Code §402.00111 provides that the commissioner of workers' compensation shall exercise all executive authority, including rulemaking authority under Title 5 of the Labor Code.

Labor Code §402.00116 provides that the commissioner of workers' compensation shall administer and enforce this title, other workers' compensation laws of this state, and other laws granting jurisdiction to or applicable to DWC or the commissioner.

Labor Code §402.061 provides that the commissioner of workers' compensation shall adopt rules as necessary to implement and enforce the Texas Workers' Compensation Act.

CROSS-REFERENCE TO STATUTE. Section 165.1 implements Insurance Code §§2054.354, 2054.504, and 2054.507, which were amended to apply to Texas Mutual by HB 3458, 77th Legislature, Regular Session (2001) and recodified by HB 2017, 79th Legislature, Regular Session (2005).

§165.1. Identification and Notification of Certain Policyholders Insured by the Texas Mutual Insurance Company Acting as the Insurer of Last Resort.

(a) The Texas Mutual Insurance Company must [shall] provide the division a list [a listing] of the policyholders requiring accident prevention services (rejected risk employers) [(Rejected Risk employers) to the Texas Workers' Compensation Commission's Division of Worker's Health and Safety (the division)]. This list must [shall] include rejected risk employers that meet the criteria in Texas Insurance Code Chapter 2054, Subchapters H and K [those employers identified by the Texas Mutual Insurance Company through application of the criteria found in the Texas Insurance Code, art. 5.76-3, §8, and art. 5.76-4].

(b) A policyholder subject to Texas Insurance Code §2054.504 [the Texas Insurance Code, art. 5.76-3, §8(e) or §8(d)], whose corporate office is located outside [the state] of Texas must, on [shall, upon] receipt of notification by the Texas Mutual Insurance Company of the requirement to get [obtain] a safety consultation as a condition of insurance, provide the Texas Mutual Insurance Company the following information:

(1) the name and title of the senior official in Texas with the authority to commit funds and to establish policy, procedures, and actions required to implement the accident prevention plan and address the exposures identified in the hazard exposure survey;

(2) the official's mailing address; and

(3) the official's business telephone number.

(c) Information required by subsection (b) of this section must [shall] be mailed to the Texas Mutual Insurance Company at 2200 Aldrich Street, Austin, Texas 78723-3474 [the appropriate address].

The agency certifies that legal counsel has reviewed the proposal and found it to be within the state agency's legal authority to adopt.

Filed with the Office of the Secretary of State on January 2, 2023.

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Earliest possible date of adoption: February 19, 2023

For further information, please call: (512) 804-4703

TITLE 34. PUBLIC FINANCE

PART 1. COMPTROLLER OF PUBLIC ACCOUNTS

CHAPTER 3. TAX ADMINISTRATION

SUBCHAPTER V. FRANCHISE TAX

34 TAC §3.591

The Comptroller of Public Accounts proposes amendments to §3.591, concerning margin: apportionment. The amendments are in response to the Texas Supreme Court opinion in *Sirius XM Radio, Inc. v. Hegar*, No. 20-0462 (Tex. March 25, 2022).

In its opinion, the Supreme Court stated: "We see no reason for the 'receipt-producing, end-product act' test to play any role in our decision." Accordingly, the comptroller deletes the receipt-producing, end-product act discussion and examples in subsection (e)(26)(A) and removes references to the deleted examples throughout the section.

The comptroller also amends subsection (e)(26)(A) to incorporate the Supreme Court decision that the most natural reading of 'service performed in this state' supports locating the performance of the service at the place where the taxpayer's personnel or equipment is physically doing useful work for the customer." The proposed rule interprets the Court's phrase "useful work for the customer" to mean "work that the customer hired the taxable entity to perform," and that the phrase does not include "activities that enable the taxable entity to do business in general or are not directly used in the provision of a service to the customer." The proposed rule replaces "equipment" with "property" to recognize that, in some cases, property may be used to perform services, and the property may not be equipment. For example, a beekeeper that offers pollination services to agricultural customers uses honeybees to perform the useful work for the customer. While honeybees are property, it is not clear that they would be considered "equipment."

The comptroller similarly amends subsection (e)(26)(B) to provide additional guidance for determining the fair value of services when they are performed both inside and outside of Texas for a single charge.

Brad Reynolds, Chief Revenue Estimator, has determined that during the first five years that the proposed amendments are in effect, the rules: will not create or eliminate a government program; will not require the creation or elimination of employee positions; will not require an increase or decrease in future legislative appropriations to the agency; will not require an increase or decrease in fees paid to the agency; will not increase or decrease the number of individuals subject to the rules' applicability; and will not positively or adversely affect this state's economy.

Mr. Reynolds also has determined that the proposed amended rule would benefit the public by updating the rule to reflect the guidance from the Texas Supreme Court ruling in *Sirius*. This rule is proposed under Tax Code, Title 2, and does not require a statement of fiscal implications for small businesses or rural communities. The proposed amendments would have no fiscal implications for the state government, units of local government, or individuals. There would be no significant anticipated economic cost to the public.

You may submit comments on the proposal to Jenny Burleson, Director, Tax Policy Division, P.O. Box 13528 Austin, Texas 78711 or to the email address: tp.rule.comments@cpa.texas.gov. The comptroller must receive your comments no later than 30 days from the date of publication of the proposal in the *Texas Register*.

The amendments are proposed under Tax Code, §111.002 (Comptroller's Rules; Compliance; Forfeiture), which provides the comptroller with the authority to prescribe, adopt, and enforce rules relating to the administration and enforcement of the provisions of Tax Code, Title 2 (State Taxation).

The amendments implement Tax Code, §171.103 (Determination of Gross Receipts from Business Done in this State for Margin).

§3.591. Margin: Apportionment.

(a) Effective date. The provisions of this section apply to franchise tax reports originally due on or after January 1, 2008, except as otherwise noted.

(b) Definitions. The following words and terms, when used in this section, shall have the following meanings, unless the context clearly indicates otherwise.

(1) Capital asset--Any asset that is held for use in the production of income, and that is subject to depreciation, depletion or amortization.

(2) Employee retirement plan--A plan or other arrangement that qualifies under Internal Revenue Code (IRC), §401(a) (Qualified pension, profit-sharing, and stock bonus plans), or that satisfies the requirement of IRC, §403 (Taxation of employee annuities), or a government plan described in IRC, §414(d) (Definitions and special rules).

(3) Gross receipts--Revenue as determined under §3.587 of this title (relating to Margin: Total Revenue), except as provided in subsection (e)(2) (concerning capital assets and investments) and subsection (e)(17) (concerning loans and securities) of this section. Non-receipt items excluded from total revenue under §3.587 of this title are not included in the calculation of total revenue under that section and are not deducted from gross receipts. These non-receipt items include the exclusion for uncompensated care, the \$500 exclusion per pro bono services case, the exclusion for the direct cost of providing waterway transportation, the exclusion for the direct cost of providing agricultural aircraft services, and the exclusion for the cost of a vaccine. See subsection (d)(5) of this section for gross receipts that are excluded from the apportionment calculation.

(4) Internal Revenue Code--The Internal Revenue Code of 1986 in effect for the federal tax year beginning on January 1, 2007, not including any changes made by federal law after that date, and any regulations adopted under that code applicable to that period.

(5) Inventory--Property held primarily for sale to customers in the ordinary course of a trade or business. Securities and loans held for investment, hedging, or risk management purposes are not inventory.

(6) Investment--Any non-cash asset that is not a capital asset or inventory.

(7) Legal domicile--The legal domicile of a corporation or limited liability company is its state of formation. The legal domicile of a partnership, trust, or joint venture is the principal place of business of the partnership, trust, or joint venture.

(8) Location of payor--The legal domicile of the payor.

(9) Principal place of business--The place where an entity's management directs, controls, and coordinates the entity's activities.

(10) Regulated investment company--Any domestic corporation defined under IRC, §851(a) (Definition of regulated investment company), including a taxable entity that includes trustees or sponsors of employee benefit plans that have accounts in a regulated investment company.

(11) Security--An instrument defined under IRC, §475(c)(2) (Mark to market accounting method for dealers in securities). This term includes instruments described by §475(e)(2)(B), (C), and (D) of that code.

(12) Tax reporting period--The period upon which the tax is based under Tax Code, §171.1532 (Business on Which Tax on Net Taxable Margin Is Based) or §171.0011 (Additional Tax).

(13) Taxable entity--Any entity upon which tax is imposed under Tax Code, §171.0002(a) (Definition of Taxable Entity) and not specifically excluded under Tax Code, §171.0002(b) or §171.0002(c). See also §3.581 of this title (relating to Margin: Taxable and Nontaxable Entities).

(14) Texas gross receipts--The portion of a taxable entity's gross receipts that is from business done in Texas.

(c) Apportionment formula. Except as provided in paragraphs (1) and (2) of this subsection, a taxable entity's margin is apportioned to Texas to determine the amount of franchise tax due by multiplying the taxable entity's margin by a fraction, the numerator of which is the taxable entity's Texas gross receipts and the denominator of which is the taxable entity's gross receipts from its entire business.

(1) Regulated investment company services. A taxable entity's margin derived, directly or indirectly, from the sale of management, distribution, or administration services to or on behalf of a regulated investment company, is apportioned to Texas by multiplying that portion of the taxable entity's total margin by a fraction:

(A) the numerator of which is the average of the sum of shares owned at the beginning of the year and the sum of the shares owned at the end of the year by the investment company shareholders whose principal place of business is in this state or, if the shareholders are individuals, are residents of this state; and

(B) the denominator of which is the average of the sum of shares owned at the beginning of the year and the sum of shares owned at the end of the year by all investment company shareholders.

(2) Employee retirement plan services. A taxable entity's margin derived, directly or indirectly, from the sale of management, administration, or investment services to an employee retirement plan is apportioned to Texas by multiplying that portion of the taxable entity's total margin by a fraction:

(A) the numerator of which is the average of the sum of beneficiaries domiciled in Texas at the beginning of the year and the sum of beneficiaries domiciled in Texas at the end of the year; and

(B) the denominator of which is the average of the sum of all beneficiaries at the beginning of the year and the sum of all beneficiaries at the end of the year.

(d) General rules for reporting gross receipts.

(1) A taxable entity that files an annual report must report gross receipts based on the business done by the taxable entity beginning with the day after the date upon which the previous report was based, and ending with the last accounting period ending date for fed-

eral income tax purposes ending in the calendar year before the calendar year in which the report is originally due.

(2) A taxable entity with a beginning date prior to October 4, 2009 that files an initial report must report gross receipts based on its activities commencing with the beginning date, as described in §3.584 of this title (relating to Margin: Reports and Payments), and ending on the last accounting period ending date for federal income tax purposes that is at least 60 days before the original due date of the initial report. A taxable entity with a beginning date on or after October 4, 2009 that files a first annual report must report gross receipts based on its activities commencing with the beginning date and ending on the last accounting period ending date for federal income tax purposes in the same calendar year as the beginning date.

(3) Taxable entities that are members of an affiliated group that are part of a unitary business must file a combined franchise tax report. See §3.590 of this title (relating to Margin: Combined Reporting), for determining gross receipts for a combined report.

(4) When a taxable entity computes gross receipts for apportionment, the taxable entity is deemed to have elected to use the same methods that the taxable entity used in filing its federal income tax return.

(5) Any item of revenue that is excluded from total revenue under Texas law or United States law is excluded from gross receipts from an entity's entire business and Texas gross receipts as provided by Tax Code, §171.1055(a) (Exclusion of Certain Receipts for Margin Apportionment). For example, any amount that is excluded from total revenue under the IRC, §78 (Dividends received from certain foreign corporations by domestic corporations choosing foreign tax credit) or §951 - 964 (26 U.S. Code Subpart F - Controlled Foreign Corporations), is excluded from gross receipts. Non-receipt items that are excluded from total revenue under §3.587 of this title, such as \$500 per pro bono services case; the actual cost of uncompensated care; the direct cost of providing waterway transportation; the direct cost of providing agricultural aircraft services and the cost of a vaccine, are not deducted from gross receipts under this section. See subsection (b)(3) of this section, concerning definition of gross receipts. For example, under Tax Code, §171.1011(g-3) (Determination of Total Revenue from Entire Business), an attorney may exclude \$500 from total revenue for handling a pro bono case. Since the \$500 is not a receipt, there is no exclusion for pro bono work when calculating gross receipts. Therefore, if a taxable entity starts with its total revenue amount to calculate its gross receipts, the taxable entity must add back the \$500 per pro bono services case.

(6) A taxable entity that uses a 52 - 53 week accounting year end and that has an accounting year that ends during the first four days of January of the year in which the report is originally due may use the preceding December 31 as the date through which margin is computed.

(7) Any item of allocated revenue excluded under §3.587(c)(9) of this title is excluded from Texas gross receipts and gross receipts from an entity's entire business.

(e) Computation and sourcing of gross receipts.

(1) Advertising services. Gross receipts from the dissemination of advertising are sourced to the locations of the advertising audience. The locations of the advertising audience should be determined in good faith using the most reasonable method under the circumstances, considering the information reasonably available. The method should be consistently applied from year to year and supported by records retained by the service provider. Locations that may be reasonable include the physical locations of the advertising, advertising

audience locations recorded in the books and records of the service provider, and locations listed in published rating statistics. If the locations of nationwide advertising audiences cannot otherwise be reasonably determined, then 8.7% of the gross receipts are sourced to Texas. For reports originally due prior to January 1, 2021, advertising receipts attributable to a radio or television station transmitter in Texas may be sourced to Texas.

(2) Capital assets and investments.

(A) Except as provided in subparagraph (C) of this paragraph, only the net gain from the sale of a capital asset or investment is included in gross receipts. A net loss from the sale of a capital asset or investment is not included in gross receipts.

(B) The net gain or net loss from the sale of a capital asset or investment is the amount realized from the sale less the adjusted basis for federal income tax purposes.

(C) For reports originally due prior to January 1, 2021, a taxable entity may add the net gains and losses from sales of investments and capital assets to determine the total gross receipts from such transactions. If both Texas and out-of-state sales have occurred, then a separate calculation of net gains and losses on Texas sales must be made. If the combination of net gains and losses results in a loss, the taxable entity may not net the loss against other receipts.

(D) The net gain from the sale of a capital asset or investments is sourced based on the type of asset or investment sold. The net gain from the sale of an intangible asset is sourced to the location of the payor as provided in paragraph (21)(B) of this subsection, concerning gross receipts from the sale of intangible assets, and paragraph (25) of this subsection, concerning securities, of this subsection. Examples of intangible assets include, but are not limited to, stocks, bonds, commodity contracts, futures contracts, patents, copyrights, licenses, trademarks, franchises, goodwill, and general receivable rights. The net gain from the sale of real property is sourced as provided in paragraph (23) of this subsection, concerning real property. The net gain from the sale of tangible personal property is sourced as provided in paragraph (29) of this subsection, concerning tangible personal property.

(E) Examples.

(i) Example 1. During a report year, a real estate investment company sells two Texas investment properties, reporting a gain on sale of one property and a loss on the sale of the other property. The company should include the net gain on the profitable sale in gross receipts from its entire business but should not include the net loss on the unprofitable sale. The company should not offset the net loss against the net gain. To determine Texas gross receipts, the asset should be sourced based on its nature. Receipts from the sale of real property are sourced to the location of the property, as provided in paragraph (23) of this subsection. The company should include only the net gain on the sale of the Texas investment property in Texas gross receipts and should not include the net loss on the sale of the other Texas investment property.

(ii) Example 2. The facts are the same as in Example 1, except the real estate investment company also had net gains and net losses from the sale of out-of-state properties. For reports originally due prior to January 1, 2021, the real estate investment company may offset all of the net losses from these sales against all of the net gains. If the result is a net gain, the net gain is included in gross receipts from its entire business. If the result is a net loss, the net loss may not be included in gross receipts from its entire business. To determine Texas gross receipts, the company may offset the net loss from the sale of the one Texas property against the net gain from the sale of the other

Texas property. If the result is a net gain, the net gain is included in Texas gross receipts. If the result is a net loss, the net loss may not be included in Texas gross receipts.

(3) Computer hardware and digital property.

(A) Gross receipts from the sale of computer hardware together with any software installed on the hardware are sourced as the sale or lease of tangible personal property under paragraph (29) of this subsection.

(B) Gross receipts from the lease of computer hardware together with any software installed on the hardware are sourced as the leasing of tangible personal property under paragraph (14)(B) of this subsection.

(C) Gross receipts from the sale of digital property (computer programs and any content in digital format that is either protected by copyright law or no longer protected by copyright law solely due to the passage of time) that is transferred by fixed physical media are sourced as the sale of tangible personal property under paragraph (29) of this subsection.

(D) Gross receipts from lease of digital property that is transferred by fixed physical media are sourced as the leasing of tangible personal property under paragraph (14)(B) of this subsection.

(E) Gross receipts from the sale or lease of digital property that is transferred by means other than by fixed physical media are sourced as the sale of intangible property under paragraph (21)(B) of this subsection.

(F) Gross receipts from the delivery of digital property as a service are sourced under paragraph (26) of this subsection, unless otherwise provided in this subsection.

(G) Gross receipts from the delivery of digital property as part of an internet hosting service are sourced as internet hosting receipts under paragraph (13) of this subsection. See paragraph (13)(D) of this subsection for factors distinguishing the purchase of access over the internet to computer services from the purchase or lease of digital property.

(H) Gross receipts from the use (as opposed to the sale or licensing) of digital property are sourced under paragraph (21)(A) of this subsection.

(I) Examples.

(i) Example 1. Movie Studio produces a copyrighted movie in digital format and successively sells the theatrical rights to Movie Theater Chain Company, the broadcast rights to Cable Company, the internet streaming rights to Internet Company A, the internet rental rights to Internet Company B, the digital versatile disc (DVD) sale rights to DVD Company, DVD rental rights to Kiosk Company, and the permanent download sale rights to Download Company. In each instance, Movie Studio's receipts are from the right to use its copyrighted digital property and sourced to where the copyright is used under paragraph (21)(A) of this subsection. Movie Theater Chain Company receipts from ticket sales are from the sale of a service and sourced ~~[to the audience location]~~ under paragraph (26) ~~[(26)(A)(i)]~~ of this subsection. Cable Company subscription receipts from broadcasting the movie are from the sale of a service and sourced ~~[to the audience location]~~ under paragraph (26) ~~[(26)(A)(i)]~~ of this subsection. Internet Company A's subscription receipts for its streaming service using its website are from an internet hosting service and sourced to the location of the customer under paragraph (13) of this subsection. Internet Company B's receipts from the rental (access for a limited time) of the movie using the company's website are from an internet hosting service and sourced to the location of the

customer under paragraph (13) of this subsection. DVD Company's receipts from the sale of DVDs are from the sale of tangible personal property and sourced under paragraph (29) of this subsection. Kiosk Company's receipts from the rental of DVDs are from the rental of property and sourced to the location of the property under paragraph (14) of this subsection. Download Company's receipts from the sale of permanent downloads of the movie are from the sale intangibles and sourced to the location of payor under paragraph (21)(B) of this subsection.

(ii) Example 2. Software Company designs bookkeeping software for personal use. Software Company licenses the software to Computer Company to include in the software sold with its computers. Software Company sells digital versatile discs (DVDs) of the bookkeeping software to Retail Company for resale to end users. Software Company sells downloads of its bookkeeping software directly to end users. Software Company sells an on-line version of its bookkeeping software in which end users can enter and store data on-line using the Software Company's website for a periodic fee. Software Company receipts from licensing the software to Computer Company are from the use of its digital product and sourced to the location of use under paragraph (21)(A) of this subsection. Computer Company's receipts from the sale of computers with pre-loaded software are from the sale of tangible personal property and sourced under paragraph (29) of this subsection. Software Company's receipts from the sale of DVDs to Retail Company are from the sale of tangible personal property and sourced under paragraph (29) of this subsection. Software Company's receipts from the sale of downloads to end users are from the sale of intangible property and sourced to the location of payor under paragraph (21)(B) of this subsection. Software Company's receipts from the sale of its on-line version are from the sale of an internet hosting service and sourced to the location of the customer under paragraph (13) of this subsection.

(4) Condemnation. Gross receipts from condemnation of property are sourced to the location of the property condemned.

(5) Debt forgiveness. If a creditor releases any part of a debt, then the amount that the creditor forgives is a gross receipt that is sourced to the legal domicile of the creditor.

(6) Debt retirement. Gross receipts from the retirement of a taxable entity's own indebtedness, such as through the taxable entity's purchase of its own bonds at a discount, are sourced to the taxable entity's legal domicile. The indebtedness is treated as an investment in the determination of the amount of gross receipts.

(7) Dividends.

(A) Dividends that are recognized as a reduction of the taxpayer's basis in stock of a taxable entity for federal income tax purposes are not gross receipts. Dividends that exceed the taxpayer's basis for federal income tax purposes that are recognized as a capital gain are treated as dividends for apportionment purposes.

(B) The following are excluded from Texas gross receipts and gross receipts from an entity's entire business:

(i) dividends from a subsidiary, associate, or affiliated taxable entity that does not transact a substantial portion of its business or regularly maintain a substantial portion of its assets in the United States;

(ii) Form 1120, Schedule C special deductions that are excluded from total revenue; and

(iii) dividends on federal obligations that are excluded from total revenue.

(C) Dividends that are received from a corporation or other sources are sourced to the location of the payor.

(D) Dividends received from a national bank are sourced to Texas if the bank's principal place of business is located in Texas. Dividends received from a bank that is organized under the Texas Banking Code are sourced to Texas.

(8) Exchanges of property. Exchanges of property are included in gross receipts to the extent that the exchange is recognized as a taxable transaction for federal income tax purposes. Such exchange must be included in gross receipts based on the gross exchange value, unless otherwise required under this section.

(9) Federal enclave. Gross receipts from a taxable entity's sales, services, leases, or other business activities that are transacted on a federal enclave that is located in Texas are sourced to Texas, unless otherwise excepted by this section.

(10) Financial derivatives. Gross receipts from the settlement of financial derivatives contracts, including hedges, options, swaps, futures, and forward contracts, and other risk management transactions are sourced to the location of the payor.

(11) Insurance proceeds.

(A) Business interruption insurance proceeds are gross receipts when the proceeds are intended to replace lost profits. Such receipts are Texas gross receipts when the location of the payor is in Texas.

(B) Gross receipts from fire and casualty insurance proceeds are sourced to the location of the damaged or destroyed property.

(12) Interest.

(A) Except as provided in subparagraph (B) of this paragraph, interest received is sourced to the location of the payor.

(B) Interest received from a national bank is a Texas gross receipt if the bank's principal place of business is located in Texas. Interest received from a bank that is organized under the Texas Banking Code is a Texas gross receipt.

(C) The following are excluded from Texas gross receipts and gross receipts from an entity's entire business:

(i) interest on federal obligations that is excluded from total revenue; and

(ii) interest that is exempt from federal income tax.

(D) A banking corporation may exclude from its Texas gross receipts interest that is earned on federal funds and interest that is earned on securities that are sold under an agreement to repurchase and that are held in a correspondent bank that is domiciled in Texas, but the banking corporation must include the interest in its gross receipts from an entity's entire business.

(13) Internet hosting service. For reports originally due on or after January 1, 2014, receipts from internet hosting are Texas gross receipts if the customer is located in Texas.

(A) Internet hosting service means providing to an unrelated user access over the internet to computer services using property that is owned or leased and managed by the provider and on which the user may store or process the user's own data or use software that is owned, licensed, or leased by the user or provider.

(B) Internet hosting includes real-time, nearly real-time, and on-demand access over the internet to computer services such as:

(i) data storage and retrieval;

(ii) video gaming;

(iii) database search services;

(iv) entertainment streaming services;

(v) processing of data; and

(vi) marketplace provider services.

(C) Internet hosting does not include:

(i) telecommunications service;

(ii) cable television service;

(iii) internet connectivity service;

(iv) internet advertising service; or

(v) internet access solely to download digital content for storage and use on the customer's computer or other electronic device.

(D) The purchase of access over the internet to computer services is distinguished from the purchase or lease of computer hardware or digital property (which are sourced under subsection (e)(3) of this section) by taking into account all relevant factors, the relevance of which may vary depending upon the circumstances. Some relevant factors indicating the purchase of access to a computer service rather than the purchase or lease of computer hardware or digital property include:

(i) the customer is not in physical possession of the property;

(ii) the customer does not control the property, beyond the customer's network access and use of the property;

(iii) the provider has the right to determine the specific property used in the transaction and replace such property with comparable property;

(iv) the property is a component of an integrated operation in which the provider has other responsibilities, including ensuring the property is maintained and updated;

(v) the customer does not have a significant economic or possessory interest in the property;

(vi) the provider bears any risk of substantially diminished receipts or substantially increased expenditures if there is nonperformance under the contract;

(vii) the provider uses the property concurrently to provide significant services to entities unrelated to the customer;

(viii) the provider's fee is primarily based on a measure of work performed or the level of the customer's use rather than the mere passage of time; and

(ix) the total contract price substantially exceeds the rental value of the property for the contract period.

(E) The customer location is determined by the physical location where the purchaser or the purchaser's designee consumes the service. The location should be determined in good faith using the most reasonable method under the circumstances, considering the information reasonably available. Receipts from some services may be sourced to multiple customer locations or to multiple customers. Locations that may be reasonable under the circumstances include the customer's principal place of business, the customer's business unit that is using the computer services, the delivery addresses for individual

units of service provided to the customer, the primary place or places of consumption by the customer, the service address of the customer, the billing address of the customer, or a combination of methods.

(i) Example 1. An individual purchases access to a dating application. The most reasonable customer location for consumption of the service may be the billing address of the individual in the absence of information regarding the individual's physical address.

(ii) Example 2. A benefactor purchases access to a computer service for a charitable organization. The customer is the purchaser's designee for consuming the service - the charitable organization. The most reasonable customer location for consumption of the service may be the physical address of the charitable organization.

(iii) Example 3. An intermediary purchases access to a computer service for resale to a third party. The customer is purchaser's designee for consuming the service - the third party. The most reasonable customer location for consumption of the service may be the physical location of the third party, if known.

(iv) Example 4. A law firm purchases access to a database search program for attorneys in multiple offices. The customers are the purchaser's designees for consuming the service - its attorneys. The most reasonable customer locations for consumption of the service may be physical addresses of each office, with the access fee sourced proportionately based on the number of attorneys in each office.

(v) Example 5. A retailer with multiple sales outlets purchases access to point of sales software that reports to the retailer's central office. The most reasonable customer locations for consumption of the service may be the physical addresses of the central office and each designated point of sale, with the access fee sourced proportionately between the central office and each designated point of sale.

(vi) Example 6. A retailer with multiple sales outlets purchases access to federal income tax preparation software. The most reasonable customer location for consumption of the service may be the principal place of business of the retailer.

(vii) Example 7. An individual pays a fee to an internet ride-sharing service connecting the individual with a driver at a particular location. The most reasonable customer location for consumption of the service may be the physical address of rendezvous point for the ride.

(14) Leases and subleases.

(A) Gross receipts from the lease, sublease, rental, or subrental of real property are sourced to the location of the property.

(B) Gross receipts from the lease, sublease, rental, or subrental of tangible personal property are sourced to the location of the property. If the property is used both inside and outside Texas, then lease payments are sourced based on the number of days that the tangible personal property was used in Texas divided by the number of days that the tangible personal property was used everywhere. If the amount due under the lease is based on mileage, then the lease payments are sourced based on the number of miles in Texas divided by the number of miles everywhere.

(C) If a lump sum is charged for the lease, sublease, rental, or subrental of more than one item of property, and the items are located both inside and outside Texas, the lump-sum is sourced to Texas based on a ratio of the fair rental value of the items located in Texas to the fair value of the items located outside of Texas.

(D) Gross receipts from the lease, sublease, rental, or subrental of a vessel that engages in commerce are sourced to Texas

based on the number of days that the vessel is engaged in commerce in Texas waters divided by the number of days that the vessel is engaged in commerce everywhere.

(E) Gross receipts from a lease, sublease, rental, or subrental of real property or tangible personal property that is treated as a sale for federal income tax purposes are sourced in the same manner as a sale. Any portion of the payments that the contracting parties designate as interest is sourced as provided in paragraph (12) of this subsection, concerning interest.

(15) Litigation awards. Litigation awards are gross receipts that are sourced to the location of the payor; however, if the litigation awards are intended to replace receipts for which another rule provided in this section applies, then the gross receipts are sourced in accordance with that rule. For example, if a taxable entity sues a Delaware corporation to recover on a sale of goods delivered to a Texas location, then a judgment for the amount of that sale would not convert the receipts from Texas gross receipts to Delaware receipts. See subsection (f) of this section, for the sourcing of receipts from judgments, compromises, or settlements that relate to natural gas production.

(16) Loan servicing.

(A) Gross receipts from servicing loans secured by real property are sourced to the location of the collateral real property that secures the loan being serviced.

(B) Gross receipts from servicing loans that are not secured by real property are sourced as provided in paragraph (26) of this subsection, concerning services.

(17) Loans and securities treated as inventory of the seller.

(A) Gross proceeds from the sale of a loan or security treated as inventory of the seller for federal income tax purposes are included in gross receipts even though the tax basis is not included in total revenue under §3.587(e)(4) of this title. Securities and loans held for investment or risk management purposes are not inventory. Gross receipts from the sale of a loan or security treated as inventory of the seller are sourced to the location of the payor as provided in paragraph (25) of this subsection, concerning securities. See paragraph (2) of this subsection, concerning capital assets and investments, or paragraph (10) of this subsection, concerning financial derivatives, for the treatment of gains and losses from sales of loans and securities not treated as inventory of the seller.

(B) If a lending institution categorizes a loan or security as "Securities Available for Sale" or "Trading Securities" under Financial Accounting Standard No. 115, the gross proceeds of the sale of that loan or security are considered gross receipts. In this subparagraph, "Financial Accounting Standard No. 115" means the Financial Accounting Standard No. 115 in effect as of January 1, 2009, not including any changes made after that date.

(18) Membership or enrollment fees paid for access to benefits. Membership or enrollment fees paid for access to benefits are gross receipts from the sale of an intangible asset and are sourced to the location of the payor.

(19) Mixed transactions. If a transaction involves elements of both a sale of tangible personal property and a service, but no documentation exists to show separate charges for the tangible personal property and service elements, then the comptroller may determine the amounts that are allocable to each element based on fair values or on any available evidence.

(20) Net distributive income. The net distributive income or loss from a passive entity that is included in total revenue is sourced to the principal place of business of the passive entity.

(21) Patents, copyrights, and other intangible assets.

(A) Gross receipts from the use of intangible assets.

(i) Revenues from a patent royalty are included in Texas receipts to the extent that the patent is utilized in production, fabrication, manufacturing, or other processing in Texas.

(ii) Revenues from a copyright royalty are included in Texas receipts to the extent that the copyright is utilized in printing or other publication in Texas.

(iii) Gross receipts that the owner of a patent, copyrighted material, trademark, franchise, or license receives from licensing the use of the patent, copyrighted material, trademark, franchise, or license are sourced to Texas to the extent the patent, copyrighted material, trademark, franchise or license is used in Texas.

(iv) Royalties from an affiliated taxable entity that does not transact a substantial portion of its business or regularly maintain a substantial portion of its assets in the United States are excluded from Texas gross receipts and gross receipts from an entity's entire business.

(B) Gross receipts from the sale of intangible assets. Except as otherwise provided in this section, gross receipts from the sale of intangible assets are sourced to the location of payor.

(C) Examples.

(i) Example 1. The owner of seismic data grants a license to an oil company to access the seismic data. Even though a license is part of this transaction, the receipts are from the use of the underlying intangible property, the seismic data (which cannot be copyrighted), not from the use of a license. Accordingly, the receipts are sourced under subparagraph (B) of this paragraph to the location of the payor.

(ii) Example 2. An inventor licenses a patent to a manufacturer. When the manufacturer licensee thereafter produces the patented item, it uses the patent, and its payments to the inventor, owner of the patent, are receipts from the use of a patent under subparagraph (A) of this paragraph. The receipts that the inventor receives are included in Texas receipts to the extent that the patent is used in production, fabrication, manufacturing, or other processing in Texas.

(iii) Example 3. The owner of copyrighted material grants a license to a publisher to publish the copyrighted material. When the publisher publishes the copyrighted material, it uses the copyright, and its payments to the owner are receipts from the use of a copyright under subparagraph (A) of this paragraph. The receipts that the copyright owner receives from the use of its copyright is included in Texas receipts to the extent the copyright is used in Texas.

(22) Qualified stock purchase under IRC, §338(h)(10) (Certain stock purchases treated as asset acquisitions). Receipts that are treated as receipts from the sale of assets by the target taxable entity under IRC, §338(h)(10) are sourced according to the rules that apply to sales of such assets. For the purposes of this paragraph, the purchaser of the target's stock is considered the purchaser of the assets.

(23) Real property. Gross receipts from the sale, lease, rental, sublease, or subrental of real property, including mineral interests, are sourced to the location of the property. Royalties from mineral interests are considered revenue from real property.

(24) Sales taxes. State or local sales taxes that are imposed on the customer, but are collected by a seller are not included in the seller's gross receipts. However, discounts that a seller is allowed to take in remittance of the collected sales tax are gross receipts to the seller.

(25) Securities. Gross receipts from the sale of securities are sourced to the location of the payor. If securities are sold through an exchange, and the payor cannot be identified, then 8.7% of the revenue is a Texas gross receipt. For reports originally due prior to January 1, 2021, a taxable entity may use 7.9% instead of 8.7%.

(26) Services. Except as otherwise provided in this section, gross receipts from a service are sourced to the location where the service is performed.

(A) Location of performance. Except as provided in other subparagraphs, a service is performed at the location or locations where the taxable entity's personnel or property are doing the work that the customer hired the taxable entity to perform. Activities that are not directly used to provide a service are not relevant when determining the location where a taxable entity performs a service [of the receipts-producing, end-product act or acts. If there is a receipts-producing, end-product act, the location of other acts will not be considered even if they are essential to the performance of the receipts-producing acts. If there is not a receipts-producing, end-product act, then the locations of all essential acts may be considered].

~~{(i) Example 1. Admission fees, subscription fees, or other charges for an audience to observe live or pre-recorded performances are sourced to the locations where the recipients observe the performance. The location where the live performance was rehearsed, the location where the pre-recorded performance was recorded, and the location where the admission fee or other charge was paid are not determinative.}~~

~~{(ii) Example 2. Gross receipts from the architectural design of a structure, are sourced to the location or locations where the architect performed the work. The delivery location of any tangible work product, such as a blueprint, is not determinative. However, if the tangible work product of the architect is considered to be the sale of tangible personal property rather than the sale of a service, such as the sale of house plan books, the gross receipts are sourced as provided in paragraph (29) of this subsection, concerning tangible personal property.}~~

(B) If services are performed both inside and outside Texas for a single charge, then receipts from the services are Texas gross receipts on the basis of the fair value of the services that are performed in Texas. In determining fair value, the relative value of each service provided on a stand-alone basis may be considered. Units of service, such as hours worked, may also be considered. The cost of performing a service does not necessarily represent its value. If costs are considered, costs should be limited to the direct costs of doing the work that the customer hired the taxable entity to perform and should not include any costs that are not directly used to provide a service to the customer [directly related to the service and not overhead costs].

(i) Example 1. A law firm with offices in Texas and Louisiana charges a client by the hour. Hours billed for work conducted in Texas are Texas gross receipts.

(ii) Example 2. A law firm with offices in Texas and Louisiana charges a client a lump sum fee of \$5,000 to draft a document. Attorneys in the Texas office recorded 20 hours on the project, and attorneys in the Louisiana office recorded 5 hours on the project at the same billing rate. Texas gross receipts are \$4,000. If the law firm

does not record hours worked on a project, other measures of direct cost may be considered.

(iii) Example 3. A Texas-based landscaper provides grounds maintenance services at its client's four offices in Texas, and one office in Oklahoma, for an annual fee of \$50,000. The landscape services at each of the locations are substantially the same. Texas gross receipts are \$40,000. Although the cost of performing the landscaping maintenance service at the Oklahoma office is higher than the cost of performing the service at the other locations because of the additional travel cost, the additional cost is not considered.

(C) Taxable entities that have margin that is derived, directly or indirectly, from the sale of services to or on behalf of a regulated investment company should refer to subsection (c)(1) of this section for information on apportionment of such margin.

(D) Taxable entities that have margin that is derived, directly or indirectly, from the sale of management, administration, or investment services to an employee retirement plan should refer to subsection (c)(2) of this section for information on apportionment of such margin.

(E) Receipts from services that a defense readjustment project performs in a defense economic readjustment zone are not Texas gross receipts.

(27) Single member limited liability company (SMLLC). For purposes of this section, the sale of a SMLLC by its sole owner is the sale of a membership interest in the SMLLC. The membership interest is an intangible asset, and receipts from the sale of a SMLLC are sourced to the location of payor.

(28) Subsidies or grants. Proceeds of subsidies or grants that a taxable entity receives from a governmental agency are gross receipts, except when the funds are required to be expended dollar-for-dollar (i.e., passed through) to third parties on behalf of the agency. Receipts from a governmental subsidy or grant are sourced in the same manner as the item to which the subsidy or grant was attributed. For example, receipts from a grant to conduct research for the government are receipts from a service and are sourced to the location where the research is performed.

(29) Tangible personal property. Examples of transactions that involve the sale of tangible personal property and result in Texas gross receipts include, but are not limited to, the following:

(A) the sale of tangible personal property that is delivered in Texas to a purchaser. Delivery is complete upon transfer of possession or control of the property to the purchaser, an employee of the purchaser, or transportation vehicles that the purchaser leases or owns. FOB point, location of title passage, and other conditions of the sale are not relevant to the determination of Texas gross receipts;

(B) the sale of tangible personal property that is delivered in Texas to an employee or transportation agent of an out-of-state purchaser. A carrier is an employee or agent of the purchaser if the carrier is under the supervision and control of the purchaser with respect to the manner in which goods are transported;

(C) the sale and delivery in Texas of tangible personal property that is loaded into a barge, truck, airplane, vessel, tanker, or any other means of conveyance that the purchaser of the property leases and controls or owns. The sale of tangible personal property that is delivered in Texas to an independent contract carrier, common carrier, or freight forwarder that a purchaser of the property hires results only in gross receipts everywhere if the carrier transports or forwards the property to the purchaser outside this state;

(D) the sale of tangible personal property with delivery to a common carrier outside Texas, and shipment by that common carrier to a purchaser in Texas;

(E) the sale of oil or gas to an interstate pipeline company, with delivery in Texas;

(F) the sale of tangible personal property that is delivered in Texas to a warehouse or other storage facility that the purchaser owns or leases;

(G) the sale of tangible personal property that is delivered to and stored in a warehouse or other storage facility in Texas at the purchaser's request, as opposed to a necessary delay in transit, even though the property is subsequently shipped outside Texas;

(H) the drop shipment of tangible personal property in Texas. A drop shipment is a shipment of tangible personal property from a seller directly to a purchaser's customer, at the request of the purchaser, without passing through the hands of the purchaser. This results in Texas gross receipts for the seller and the purchaser.

(30) Telecommunication services.

(A) Gross receipts from telephone calls that both originate and terminate in Texas are sourced to Texas.

(B) Gross receipts from telephone calls that originate in Texas but terminate outside of Texas or that originate outside of Texas but terminate in Texas are not sourced to Texas.

(C) Gross receipts from telecommunication services other than those services in subparagraph (A) or (B) of this paragraph are sourced to Texas if the services are performed in Texas. For example, a telephone company that provides a long distance carrier access to the telephone company's local exchange network in Texas is performing a service in Texas. Any fee that the telephone company charges the long distance carrier for access to the local exchange network in Texas is a Texas receipt regardless of whether the access is related to an interstate call. A fee that is charged to obtain access to a local exchange network in Texas and that is based on the duration of an interstate telephone call are not sourced to Texas.

(31) Television broadcaster licensing income. For reports originally due on or after January 1, 2018, a broadcaster's gross receipts from licensing income from broadcasting or otherwise distributing film programming by any means are sourced to Texas if the legal domicile of the broadcaster's customer is in this state. In this subparagraph, the following words and terms shall have the following meaning:

(A) Broadcaster--A taxable entity, not including a cable service provider or a direct broadcast satellite service, that is a television station licensed by the Federal Communications Commission, television broadcast network, cable television network, or television distribution company.

(B) Customer--A person, including a licensee, who has a direct connection or contractual relationship with a broadcaster under which the broadcaster derives revenue.

(C) Film programming--All or part of a live or recorded performance, event, or production intended to be distributed for visual and auditory perception by an audience.

(D) Programming--Includes news, entertainment, sporting events, plays, stories, or other literary, commercial, educational, or artistic works.

(32) Texas waters. Gross receipts from transactions that occur in Texas waters are sourced to Texas. Texas waters are consid-

ered to extend to 10.359 statute miles, or nine nautical miles, from the Texas coastline.

(33) Transportation services. Gross receipts from the transportation of goods or passengers are sourced to Texas by:

(A) including gross receipts from the transportation of goods or passengers that both originates and terminates in Texas; or

(B) the multiplication of total transportation receipts by the ratio of total compensated mileage in the transportation of goods and passengers in Texas to total compensated mileage.

(f) Natural gas production.

(1) Gross receipts that a gas producer realizes from the contract price of gas that the gas producer produces and that the purchaser takes pursuant to the terms of sales are sourced to Texas, if the gas is delivered in Texas.

(2) Gross receipts that a gas producer realizes from a purchaser's payment under a sale or purchase contract for gas to be produced even if no gas is produced and delivered to the purchaser, are sourced to the location of the payor.

(3) Gross receipts that a gas producer realizes from a purchaser's payments to terminate a gas purchase contract are sourced to the location of the payor.

(4) Gross receipts that a gas producer realizes from a contract amendment that relates to the price of the gas sold are treated as gross receipts from the sales of gas and are sourced to Texas if delivery is made to a location in Texas. Gross receipts that the gas producer realizes from a contract amendment that relates to a provision other than the price of gas sold are sourced to the location of the payor.

(5) Gross receipts that a gas producer realizes from litigation awards for a breach of contract, reimbursements for litigation-related expenses (e.g., documented attorney's fees or court costs), or in-

terest (upon which the parties have agreed, that the records of the producer reflects, or in an amount that a court has ordered) are sourced to the location of the payor.

(6) Gross receipts that a gas producer realizes from a judgment, compromise, or settlement relating to the recovery of a contract price of gas produced are sourced to Texas to the extent the contract specified delivery to a location in Texas. Gross receipts that a gas producer realizes from a judgment, compromise, or settlement that relates to several claims or causes of action shall be prorated based upon the documented amounts due under the contract for each claim or cause of action according to the records of the producer. For example, a settlement sum of \$100,000 for a pricing dispute of \$25,000 and for failure to pay for gas not taken in the amount of \$225,000, would result in receipts of \$10,000 from gas sales ($100,000 \times 25,000/250,000$) and receipts from other business of \$90,000 ($100,000 \times 225,000/250,000$). Records of the producer shall include, but are not limited to the following: contracts, settlement agreements, accounting records and entries, court pleadings and worksheets, including calculations reflecting settlement amounts.

The agency certifies that legal counsel has reviewed the proposal and found it to be within the state agency's legal authority to adopt.

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For further information, please call: (512) 475-2220

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