

## 810-27-1-.13 Payroll Factor: In General

(1) The payroll factor of the apportionment formula for each trade or business of the taxpayer shall include the total amount paid by the taxpayer in the regular course of its trade or business for compensation during the tax period.

(2) Definitions. For purposes of Rule 810-27-1-.13, the following terms have the following meanings unless the context requires otherwise.

(a) Employee generally means any person who, under the usual common-law rules applicable in determining the employer-employee relationship, has the status of an employee. Generally, a person will be presumed to be an employee if such person is included by the taxpayer as an employee for purposes of the payroll taxes imposed by the Federal Insurance Contributions Act. However, for purposes of this rule, a leased employee is an employee of the client (lessee) organization. A leased employee is also treated as an employee of the employee leasing company.

(b) Employee Leasing Company means a business that contracts with a client company to supply workers to perform services for the client company. The term "employee leasing company" does not include private employment agencies that provide workers to employers on a temporary help basis or entities such as driver-leasing companies which lease employees to another business to perform a specific service unless the total amount of compensation paid to the employee leasing company during the tax period exceeds 5% of compensation paid everywhere during the tax period. This threshold should be calculated excluding the amount of compensation paid to the employee leasing company.

(c) Independent contractor means any person who performs services for a taxpayer but who is not an employee of the taxpayer, and who is not otherwise subject to the supervision or control of the taxpayer in the performance of the services. In general, a person is treated as an independent contractor with respect to a taxpayer if that person's actions would not represent an employer-employee relationship for federal tax purposes.

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

connected with the production of nonbusiness income shall be excluded from the factor.

(4) Payroll Factor: Denominator. The denominator of the payroll factor is the total compensation paid everywhere during the tax period. Accordingly, compensation paid to employees whose services are performed entirely in a state where the taxpayer is immune from taxation, for example, Public Law 86-272, is included in the denominator of the payroll factor.

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

(5) Payroll Factor: Numerator. The numerator of the payroll factor is the total amount paid in Alabama during the tax period by the taxpayer for compensation in the production of business income. The tests in Code of Alabama 1975, § 40-27-1, Article IV.14 and Rule 810-27-1-.14 should be applied in determining whether compensation is paid in Alabama.

(6) Items Included. Compensation in the payroll factor includes wages, salaries, commissions, and any other form of remuneration paid to employees for personal services rendered.

(7) Treatment of Leased and Temporary Employees.

(a) Leased Employees. Compensation paid for personal services rendered by leased employees is includible in the payroll factor of the taxpayer if the taxpayer is the recipient of the services of the leased employee. Compensation for personal services rendered by leased employees to client companies is also included in the payroll factor of employee leasing companies.

(b) Temporary Employees. Compensation paid for personal services rendered to client companies by employees of temporary help agencies is included in the payroll factor of the temporary agency and is generally excluded from the payroll factor of the client company. If compensation paid to temporary employees is included in the payroll factor of a client company (see subparagraph (2)(b)), such compensation shall be eighty-five percent of the payments during the taxable year by the client company to the temporary help agency or agencies providing the temporary employees. Any adjustment to the payroll factor of a client company shall not affect the payroll factor of the temporary help agency or agencies providing the temporary employees.

(8) Items Excluded. For purposes of the payroll factor, compensation excludes payments that are not made by a taxpayer to its employees for personal services rendered. The following items are excluded without limitation:

(a) Payments to or on behalf of employees (including amounts paid for insurance or annuities) for sickness or accident disability, hospitalization, or death.

(b) Payments to or from qualified trusts under 26 U.S.C. § 401(a) (other than employer contributions under qualified cash or deferred arrangements as defined in 26 U.S.C. § 401(k)), payments to or from qualified annuity plans or contracts under 26 U.S.C. § 403, and payments to or from simplified employee pensions under 26 U.S.C. § 408(k).

(c) Employer's payments of employee's FICA taxes.

(d) Tips paid in any medium other than cash, and cash tips which are less than \$20 a month and not reported to the employer pursuant to 26 U.S.C. § 6053(a).

(e) Non-cash payments to employees for services not in the course of the taxpayer's trade or business.

(f) Payments made to independent contractors, retirees, or other persons not properly classified as employees.

(9) Affiliated Corporations. In order to prevent distortions in the payroll factor, the Commissioner may require compensation paid to a related member's employee to be included in the payroll factor of a taxpayer regardless of which entity actually paid the compensation or if the related member was reimbursed if there is evidence that a related member's employees provided services to or maintained the property of a taxpayer and the payroll factor is inconsistent with the other components of the apportionment factor. A related member is any person considered a "related member" pursuant to Code of Alabama 1975, § 40-18-1.

(10) Payroll Consistency. A taxpayer must use the same rules for determining compensation paid in both the numerator and the denominator of the payroll factor. If a taxpayer changes its method of determining compensation paid, including, but not limited to, its method of accounting of such compensation, from the method used in its return for the prior year, the taxpayer must disclose in the return for the current year the presence of the change, the nature and extent of the change, and the reason for the change. The Commissioner may disregard changes in the current year or in future tax years if they have not been adequately disclosed.

(11) *Payroll Factor: Under the Completed Contract Method of Accounting.* For taxpayers utilizing the completed contract method of accounting, the payroll factor shall include all payroll costs attributed to the contracts completed during the tax period. Payroll costs not directly attributed to the completed contract projects, such as administrative salaries, shall be reported as otherwise provided in this rule.

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Authority: §§40-2A-7(a)(5) and 40-18-57, Code of Alabama 1975.

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