



COLORADO
Department of Revenue
Taxation Division

Office of Tax Policy
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PLR 23-002

March 13, 2023

XXXXXXXXXX
XXXXXXXXXX
XXXXXXXXXX

Re: Exclusion of Gain from Apportionment Factor

Dear XXXXXXXXXXXX:

You submitted a request for a private letter ruling on behalf of XXXXXXXXXXXX (the “Company”), to the Colorado Department of Revenue (“Department”) pursuant to 1 CCR 201-1, Rule 24-35-103.5. This letter is the Department’s private letter ruling. This ruling is binding on the Department to the extent set forth in 1 CCR 201-1, Rule 24-35-103.5. It cannot be relied upon by any taxpayer other than the taxpayer to whom the ruling is made.

Issue

Whether the gross receipts from Company’s sale of Colorado real estate must be included in Company’s receipts for purposes of apportioning income under section 39-22-303.6(4)(a), C.R.S.

Conclusion

The gross receipts from Company’s sales of Colorado real estate must not be included in Company’s receipts for purposes of apportioning income under section 39-22-303.6(4)(a), C.R.S.

Background¹

Company is a [State] limited partnership that files federal form 1065, XXXXXXXXXXXX, and Colorado form DR 0106 partnership returns. For Colorado income tax purposes, Company will make the election allowed by section 39-22-203(1) to apportion and allocate the partnership’s income pursuant to section 39-22-303.6, C.R.S.

Company is a real estate rental company organized in and operated from [State] since [year]. Company has consistently held its real estate for long-term rental with very few property sales throughout its history. Company has always reported its rental income as unitary business

¹ Paragraph (4)(b)(ii) of 1 CCR 201-1, Rule 24-35-103.5 requires the request for a private letter ruling to include a statement of facts. This section generally recites the statement of facts provided in the request, which is not an indication that the Department found such facts relevant to its analysis. Some relevant facts may be omitted to ensure confidentiality as required by section 24-35-103.5(5), C.R.S. The terms used in this section to describe the factual background are generally those of the requester.

income, subject to apportionment. Prior to 2022, Company had completed three dispositions of real property, all of which were section 1031 exchanges with the gains deferred.

In [year] Company acquired commercial real estate in Colorado as the replacement property in a section 1031 exchange. This was Company's first Colorado real estate acquisition. The Colorado property was under lease when acquired, and Company continued to lease the Colorado property. Company included the rental income as receipts in the receipts factor formula. Company had one real property sale between the dates it acquired and sold the Colorado property. Company sold [State] real property in a section 1031 exchange with the acquisition of [State] real property as the replacement. In 2022, taxpayer sold two properties, including the Colorado property.

Discussion

The gross receipts from Company's sales of Colorado real estate must not be included in Company's receipts for purposes of apportioning income under section 39-22-303.6(4)(a), C.R.S. The Colorado income tax imposed upon a nonresident partner of a partnership includes only the portion of the nonresident partner's distributive share of items of partnership income, gain, loss, deduction, or credit derived from sources within Colorado.² At the partnership's election, such sourcing may be determined by apportioning or allocating those items to Colorado pursuant to section 39-22-303.6, C.R.S., which provides for the market-based apportionment and allocation of income.³ Company states that it will make this election for tax year 2022.

Section 39-22-303.6(4)(a), C.R.S., requires a taxpayer's apportionable income to be apportioned to Colorado by multiplying such apportionable income by a fraction. The numerator of the fraction is the receipts of the taxpayer in Colorado during the tax period.⁴ The denominator of the fraction is the total receipts of the taxpayer everywhere during the tax period.⁵ Apportionable income includes:

- (A) Income arising from transactions and activity in the regular course of a taxpayer's trade or business; and
- (B) Income arising from tangible and intangible property if the acquisition, management, employment, development, or disposition of the property is or was related to the operation of the taxpayer's trade or business.⁶

In this case, Company's trade or business is real estate rental. As such, the rents received are transactions in the regular course of the Company's trade or business. Rents are customary receipts for a real estate rental company, and Company receives rents on a frequent, recurring basis.⁷ Conversely, Company's history demonstrates that the 2022 sales of real property were

² Section 39-22-203(1)(a), C.R.S.

³ *Id.*

⁴ Section 39-22-303.6(4)(a), C.R.S.

⁵ *Id.*

⁶ Section 39-22-303.6(1)(a)(II), C.R.S.

⁷ 1 CCR 201-2, Rule 39-22-303.6-2(3)(a)(ii) explains, "Most, but not all, frequently occurring transactions or activities will be in the regular course of that trade or business and will, therefore, satisfy the transactional test. It is sufficient to

infrequently occurring dispositions of Company's property.⁸ These transactions were not in the regular course of Company's trade or business. The two properties sold in 2022 were, however, related to the operation of the taxpayer's trade or business. Indeed, the properties produced apportionable income in the form of rents. Therefore, the income arising from the sale of the properties is apportionable income under 39-22-303.6(1)(a)(II)(B).

Nevertheless, the amounts received by Company from the 2022 property sales are not "receipts" within the meaning of section 39-22-303.6(1)(d), C.R.S. "Receipts" means all gross receipts of the taxpayer that are not allocated under [sections 39-22-303.6(7) or (9), C.R.S.], and that are received from transactions and activity in the regular course of the taxpayer's trade or business"⁹ As discussed above, the amounts received from the two property sales were not from activity in the regular course of Company's real estate rental business.¹⁰ Therefore, the gross receipts from Company's sales of Colorado real estate must not be included in Company's receipts.

Miscellaneous

This ruling is premised on the assumption that Company has completely and accurately disclosed all material facts, that all representations are true and complete, and that Company has otherwise complied with the requirements of section 24-35-103.5, C.R.S., and the rules promulgated pursuant thereto. The Department reserves the right, among others, to independently evaluate Company's facts, representations, and assumptions. The ruling is null and void if any such fact, representation, or assumption is incorrect and has a material bearing on the conclusions reached in this ruling. This ruling is binding on the Department and is subject to modification or revocation, in accordance with 1 CCR 201-1, Rule 24-35-103.5.

Thank you for your request.

Sincerely,

Office of Tax Policy
Colorado Department of Revenue

This ruling cannot be relied upon by any other taxpayer other than the taxpayer to whom the ruling is made.

classify a transaction or activity as being in the regular course of a trade or business, if it is reasonable to conclude transactions of that type are customary in the kind of trade or business being conducted or are within the scope of what that kind of trade or business does."

⁸ Paragraph (3)(b)(iv)(B) of the rule states, "Income that is derived from isolated sales, leases, assignments, licenses, and other infrequently occurring dispositions, transfers, or transactions involving property, including transactions made in the full or partial liquidation or the winding-up of any portion of the trade or business, is apportionable income if the property is or was related to the taxpayer's trade or business." 1 CCR 201-2, Rule 39-22-303.6-2.

⁹ Section 39-22-303.6(1)(d), C.R.S.

¹⁰ The exceptions for amounts allocated under sections 39-22-303.6(7) or (9), C.R.S., are inapplicable here. Subsection (7) deals with the allocation of nonapportionable income, which is inapplicable because we conclude above that the income from the sales is apportionable. Subsection (9) provides alternative apportionment rules applicable in cases where the standard allocation and apportionment rules do not fairly represent the taxpayer's business activities in Colorado. Company asks us to consider whether the inclusion of the sales in the receipts factor would be distortive, but because we conclude that the sales are not "receipts," we decline to conduct such an analysis.