

**OFFICE OF TAX AND REVENUE
NOTICE OF PROPOSED RULEMAKING**

The Office of Tax and Revenue (OTR), pursuant to the authority set forth in Section 201(a) of the 2005 District of Columbia Omnibus Authorization Act, approved October 16, 2006 (120 Stat. 2019; P.L. 109-356, D.C. Official Code § 1-204.24d(10) (2011 Supp.)) of the Home Rule Act, and the Office of the Chief Financial Officer Financial Management and Control Order No. 00-5, effective June 7, 2000, hereby gives notice of its intent to amend chapter 1, Income and Franchise Taxes, of title 9 of the District of Columbia Municipal Regulations (DCMR), by adding new sections 156, *et seq.*

Legislation on combined reporting became effective on September 14, 2011, in the Fiscal Year 2012 Budget Support Act of 2011 (D.C. Law 19-21; 58 DCR 6226), which requires combined reporting in the District of Columbia. The combined reporting provisions were incorporated into the Income and Franchise Taxes statutes, chapter 18 of title 47 of the District of Columbia Official Code.

Combined reporting is a tax reporting method where all of the members of a unitary group are required to determine their net income based on the activities of the unitary group as a whole. Unitary group members that have nexus with the District of Columbia apportion the total group income to District of Columbia through an apportionment formula.

OTR hereby gives notice of its intent to take final rulemaking action to adopt these regulations in not less than thirty (30) days from the date of publication of this notice in the *D.C. Register*.

The regulations on Income and Franchise Taxes contained in chapter 1 of title 9 DCMR are amended as follows:

New sections 156, *et seq.*, are added to read as follows:

156 COMBINED REPORTING: PURPOSE, GENERAL RULE, AND DEFINITIONS

156.1 *Purpose.* The combined reporting regulations require a person subject to tax under chapter 18 of title 47 of the D.C. Official Code that is engaged in a unitary business with one (1) or more persons to compute its share of the combined unitary income or loss attributable to the District using a combined report.

156.2 *General rule.* A taxpayer is required to file a combined report when it is subject to tax under chapter 18 of title 47 of the District of Columbia Official Code and is engaged in a unitary business with one or more other persons that are required to be included in a combined report pursuant to section 8002(c) of the Fiscal Year 2012 Budget Support Act of 2011, effective September 14, 2011 (D.C. Law 19-21; to be codified at D.C. Official Code § 47-1805.02a) and the combined

reporting regulations. The combined report shall be filed with the taxpayer's tax return, and shall include the income and apportionment information of all persons that are members of the combined group and such other information as required by the Chief Financial Officer.

156.3 *Revocation of election to file consolidated return.* Any taxpayer election made under D.C. Official Code § 47.1805.02(5)(B) and (C) (2005 Repl.) and § 109 is revoked for tax years beginning after December 31, 2010, and any such prior election shall have no further effect.

156.4 *Definitions of terms and phrases.* For purposes of combined reporting, the following terms and phrases shall have the meanings ascribed:

- (a) **Combined group** - the group of all persons whose income and apportionment factors are required to be taken into account pursuant to D.C. Official Code § 47-1810.02 (2005 Repl.) and the District of Columbia Municipal Regulations in determining the taxpayer's share of the net business income or loss apportionable to the District;
- (b) **Combined group member** - a person for which any part of such person's net income or loss is subject to combination and is, therefore, required to be included in a combined report;
- (c) **Combined report** - a computational schedule or schedules, as required by section 8002(c) of the Fiscal Year 2012 Budget Support Act of 2011, effective September 14, 2011 (D.C. Law 19-21; to be codified at D.C. Code § 47-1805.02a), and the combined reporting regulations or any other rules or procedures established by the Chief Financial Officer, which are to be attached to a taxpayer's annual franchise tax return and which report the income and apportionment information of all persons that are members of the taxpayer's combined group, as well as any supporting information required by the Chief Financial Officer;
- (d) **Combined reporting regulations/rules** – the rules provided under §§ 156 *et seq.*;
- (e) **Combined unitary income** - the combined group's net income or loss attributable to the unitary business which is subject to combination under section 8002(c) of the Fiscal Year 2012 Budget Support Act of 2011, effective September 14, 2011 (D.C. Law 19-21; to be codified at D.C. Official Code § 47-1805.02a) before apportionment. Combined unitary income excludes any amounts that are not subject to combination pursuant to the water's edge rules unless the taxpayer has made a valid worldwide election;

- (f) **Commonly owned or controlled** - where more than fifty percent (50%) of the voting control of each member of the group is directly or indirectly owned by a common owner or owners, either corporate or non-corporate. In determining common ownership or control, the Chief Financial Officer may take into account any plan or arrangement, whether existing by operation of law, by contract, or otherwise, for bestowing or shifting ownership or voting control, in addition to the terms of any actual stock ownership or control;
- (g) **Commonly controlled group** – a commonly controlled group exists where there is common ownership or control of stock representing more than fifty percent (50%) of the voting power of the corporations in the group. *See* § 158.3;
- (h) **Corporation** – Any entity or organization of any kind treated as a corporation for tax purposes under the laws of the District, wherever located, which, were it doing business in the District, would be subject to the tax imposed under chapter 18 of title 47 of the D.C. Official Code. A corporation includes any S corporation as defined in I.R.C. § 1361(a);
- (i) **Designated agent** - the taxable member of the combined group who is responsible for acting on behalf of the group for matters relating to the combined report. *See* § 168;
- (j) **Person** - a partnership, limited liability company, registered limited liability partnership, foreign limited partnership, association, corporation (whether or not the corporation is, or would be if doing business in the District, subject to the chapter 18 of title 47 of the D.C. Official Code this chapter) or organization of any kind. A "person" within the meaning of the combined reporting regulations does not include individuals;
- (k) **Unitary business income** - the net income or loss derived from the unitary business, whether or not the income or loss is subject to combination;
- (l) **Water's edge rules** - the rules provided under § 162 under which some or all of a corporation's items attributable to a unitary business are not subject to combination because of the degree of the corporation's activity outside the United States; and
- (m) **Worldwide election** - an election by the designated agent of the combined group on behalf of all of the taxable members of the group to treat as the combined group, for purposes of §§ 156, *et seq.*, all persons that are engaged in the unitary business, wherever located, on such terms and in keeping with such requirements as are further explained by the combined

reporting rules, forms, instructions or other notices that the Chief Financial Officer issues.

157 COMBINED REPORTING: ENTITIES REQUIRED COMBINED REPORTING

157.1 *General rule.* Where a corporation subject to tax under chapter 18 of title 47 of the D.C. Official Code, is engaged in a unitary business with one (1) or more other entities that are related by common ownership, the taxpayer entity must determine its tax liability based upon the income and apportionment information of all corporations included in the combined group using a combined report.

157.2 *Included corporations.* Corporations that are required to be included in a combined group and therefore required to be included in a combined report filed by a taxable member of a combined group shall include all entities of the kind that are subject to tax or would be subject to tax if doing business in the District, under chapter 18 of title 47 of the D.C. Official Code. The corporations to be included in a combined group include, but are not limited to, any financial institution, utility company, transportation company, S corporation as defined in I.R.C. § 1361(a), a real estate investment trust (REIT) as referenced under I.R.C. §§ 856 through 859, and a regulated investment company (RIC) as referenced under I.R.C. §§ 851 through 855.

157.3 *Excluded corporations.* Corporations that are not included in a combined group and therefore not included in a combined report filed thereby, irrespective of whether they are engaged in a unitary business with a taxable member of such group, include, unless such corporations are otherwise required to be included under section 8002(c) of the Fiscal Year 2012 Budget Support Act of 2011, effective September 14, 2011 (D.C. Law 19-21; to be codified at 47-1805.02a), insurance companies, or as otherwise provided in chapter 18 of title 47 of the D.C. Official Code.

158 COMBINED REPORTING: DETERMINATION OF A UNITARY BUSINESS

158.1 Section 8002(c) of the Fiscal Year 2012 Budget Support Act of 2011, effective September 14, 2011 (D.C. Law 19-21; to be codified at D.C. Official Code § 47-1805.02a(a)) provides that a corporation that is doing business in the District and that is engaged in an unitary business with one (1) or more other corporations in the same commonly controlled group is required to determine its share of income from that unitary business using a combined report, unless it is excluded corporation under § 157.3.

158.2 *Determination of unitary business.* The term “unitary business” is defined in section 8002(b) of the Fiscal Year 2012 Budget Support Act of 2011, effective September 14, 2011 (D.C. Law 19-21; to be codified at D.C. Official Code § 47-

1801.04(55)(A)) as a single economic enterprise that is made up either of (1) separate parts of a single business entity or (2) a commonly owned or controlled group of business entities that are sufficiently interdependent, integrated, and interrelated through their activities so as to provide synergy and mutual benefit that produces a sharing or exchange of value among them and a significant flow of value to the separate parts. Under section 8002(b) of the Fiscal Year 2012 Budget Support Act of 2011, effective September 14, 2011 (D.C. Law 19-21; to be codified at D.C. Official Code § 47-1801.04(55)(A)), the definition of “unitary business” shall be construed to the broadest extent permitted by the U.S. Constitution.

- 158.3 *Commonly controlled.* A unitary business may consist of a single entity or of a group of two (2) or more related entities. A group of related entities may satisfy the commonly controlled requirement of a unitary business if they are related in any of the following ways:
- (a) The entities are related within the meaning of the provisions of I.R.C. § 267. By reference, this includes the rules in I.R.C. § 707(b), relating to partnerships;
 - (b) The entities are related under I.R.C. § 1563, which defines a "controlled group of corporations" for federal income tax purposes; and
 - (c) The entities are corporations in the same "commonly controlled group" for District purposes. "Commonly controlled group" has the stated meaning in § 156.3(g) "commonly controlled group" includes any of the following:
 - (1) A parent corporation and any one (1) or more corporations or chains of corporations that are related to the parent corporation by direct or indirect ownership, if the parent corporation owns stock representing more than fifty percent (50 %) of the voting power of at least one of the related corporations or if the parent corporation or any of the related corporations owns stock that cumulatively represents more than fifty percent (50 %) of the voting power of each of the related corporations; or
 - (2) Any two (2) or more corporations if a common owner, regardless of whether the owner is a corporate entity, directly or indirectly owns stock representing more than fifty percent (50 %) of the voting power of the corporations or related corporations.
- 158.4 *Stock attribution rules.* A shareholder is considered to have indirect ownership of stock or to indirectly own stock if the shareholder has constructive ownership of the stock within the meaning of I.R.C. § 318, except as provided in (a) and (b) below.

Example: Corporation A owns stock representing forty percent (40%) of the voting power of Corporation B and has a fifty percent (50%) interest in Partnership C. Partnership C owns stock representing thirty percent (30%) of the voting power of Corporation B. Pursuant to I.R.C. § 318, Corporation A constructively owns stock representing fifty-five percent (55%) (40% + (50% x 30%)) of the voting power of Corporation B.

158.5 In applying I.R.C. §318(a)(2), if a partnership, estate, trust, or corporation owns, directly or indirectly, more than fifty percent (50 % of an entity, it shall be considered to own all of the stock or other ownership or control interests owned by that entity.

Example: Corporation D owns stock representing ten percent (10%) of the voting power of Corporation E and has a seventy-five percent (75%) interest in Partnership F. Partnership F owns stock representing forty-five percent (45%) of the voting power of Corporation E. Corporation D is considered to constructively own stock representing fifty-five percent (55%) (10% + 45%) of the voting power of Corporation E. This is because Corporation D owns more than fifty percent (50%) of Partnership F and is therefore considered to own all of the Corporation E stock owned by Partnership F.

158.6 If a person has an option to acquire stock or other ownership interests in an entity, the stock or ownership interests are not considered owned by the person unless the Chief Financial Officer determines it to be necessary to prevent tax avoidance.

158.7 *Voting power.*

- (a) A shareholder has ownership or control of stock representing more than 50 percent of the voting power of a corporation only if the shareholder has ownership or control of more than fifty percent (50 %) of the total combined voting power of all classes of stock of the corporation entitled to vote'
- (b) A group of two (2) or more corporations need not be commonly owned to be commonly controlled. A group of corporations may be a commonly controlled group if stock representing more than fifty percent (50 %) of the voting power in each corporation are interests that cannot be separately transferred. If a group of two (2) or more corporations would be considered stapled entities under I.R.C. § 269B and the regulations applicable thereto, without regard to whether the corporations are foreign or domestic, the corporations shall be considered part of a commonly controlled group;
- (c) The mere ownership of stock entitled to vote does not by itself mean that the shareholder owning the stock has the voting power of the stock. If there is any agreement, whether express or implied, that any shareholder

will not vote its stock or will vote it only in a specified manner, or that shareholders owning stock having fifty percent (50 %) or less of the total combined voting power will exercise voting power normally possessed by a majority of stockholders, the Chief Financial Officer may presume that the nominal ownership of the voting power is not determinative of which shareholders actually hold the voting power and may disregard the nominal ownership. This presumption may be rebutted by the taxpayer; and

- (d) If a shareholder owns shares of stock of a corporation which has another class of stock outstanding, the voting power of that other class of stock will be deemed owned by any person or persons on whose behalf it is exercised if the facts indicate that the shareholders of that other class of stock do not exercise their voting rights independently or fail to exercise their voting rights. If the voting power in that other class of stock is not exercised and the percentage of voting power of that class of stock is substantially greater than its proportionate share of the corporate earnings, the Chief Financial Officer may presume that the principal purpose of the arrangement was to avoid the inclusion of the corporation in the commonly controlled group and may disregard the voting power.

158.8 *Common owner or owners.* The common owner or owners need not be combined group members, and the common owner or owners may be persons other than corporations.

158.9 *Multiple unitary businesses.* A commonly controlled group may be engaged in one or more unitary businesses. Therefore, a commonly controlled group may contain more than one (1) combined group.

158.10 *Sufficiently interdependent, integrated, and interrelated.*

- (a) In general, the segments in a commonly owned or controlled trade or business are considered a unitary business if their activities generate synergy and a mutual benefit that produces a sharing or exchange of value among them and a significant flow of value to the separate parts. For example, the segments in a commonly controlled trade or business may be considered a unitary business when the operations of the segments contribute to or depend upon each other in such a way as to result in functional integration between the segments; and
- (b) “Functional integration” refers to, but is not limited to, transfers between or pooling among business segments of such items as products or services, technical information, marketing information, distribution systems, purchasing and intangibles (such as patents, copyrights, formulas, processes, trade secrets, and the like) in a manner which substantially affects the segments' business operations related to such activities as

development, manufacture, production, extraction, distribution or sale of its products or services.

158.11 *Sharing, exchange, and flow of value.* Segments in a commonly controlled economic enterprise have sharing or exchange of value among them and a significant flow of value to the separate parts, and thus are a unitary business, if any of the following are true:

- (a) The segments in the enterprise contribute or are expected to contribute in a nontrivial way to each other's profitability;
- (b) Each segment in the enterprise is either dependent on, or is relied upon by, one (1) or more other segments in the enterprise for achieving one (1) or more nontrivial business objectives;
- (c) The enterprise offers one (1) or more segments, some economies of scale, or economies of scope that benefit the trade or business; or
- (d) The prices charged on transactions between segments in the enterprise are inconsistent with the arms-length principle. However, if these prices are consistent with the arms-length principle, that fact does not negate, in any way, the existence of a unitary business.

158.12 *Examples of flow of value.* Activities between segments that constitute a flow of value between them include any of the following:

- (a) Common or centralized purchasing, advertising, employees (including sales force), executive force, accounting, legal support, compliance, data management, insurance coverage, marketing, cash management, research and development, offices, manufacturing facilities, computer systems and support, management, distribution system (including but not limited to transportation facilities, warehousing facilities, or order fulfillment systems, inventory control systems or other distribution systems or subsystems), pooling of technical information, general operational guidance, or overall operational strategic advice, or any combination thereof;
- (b) Intercorporate sales, leases (including equipment and real estate), exchanges, or transfers;
- (c) Intercorporate debts, lending funds, guaranteeing loans, or pledging assets;
- (d) Intercorporate use of proprietary materials, including trade names, trademarks, service marks, patents, copyrights, and trade secrets; and

- (e) Centralized executive force; interlocking directorates or corporate officers; intercompany employee transfers; or common employee and executive training programs, hiring and personnel policies, recruiting programs, employee handbooks, and employee benefit programs.

158.13 *Evidence of unitary business factors.* The determination of whether or not the operations of business segments are a unitary business will turn on the facts and circumstances of the case. Several factors may evidence that the operations of business segments are a unitary business. Generally, several functionally integrating factors will exist in a unitary business, although a unitary business may exist as a result of few factors or even one (1) factor, if the factor or factors involved are particularly significant. In determining whether a unitary business exists, factors should not be examined in isolation. Instead, it should be determined whether the factors which are present, in combination, result in a functionally integrated business. In addition, the presence or absence of any one (1) factor or any particular factors is not necessarily determinative as to whether a unitary business exists, although absence of all of the factors will generally result in a finding that a unitary business does not exist.

158.14 *Inferences and Presumptions.* Presence of a unitary business will be inferred or presumptively shown by the presence of the following:

- (a) *Same type of business.* Business activities that are in the same general line of business generally constitute a single unitary business, as, for example in the case of multiple corporations that comprise a multistate grocery chain;
- (b) *Steps in a vertical process.* Business activities that comprise different steps in a vertically structured business almost always constitute a single unitary business. For example, a business engaged in the exploration, development, extraction, and processing of a natural resource and the subsequent sale of a product based upon the extracted natural resource, is engaged in a single unitary business, regardless of the fact that the various steps in the process are operated substantially independently of each other with only general supervision from the business's executive offices; and
- (c) *Strong centralized management.* Business activities which might otherwise be considered as part of more than one (1) unitary business may constitute one (1) unitary business when there is a strong central management, coupled with the existence of centralized departments for such functions as financing, advertising, research, or purchasing. Strong centralized management exists when a central manager or group of managers makes substantially all of the operational decisions of the business. For example, some businesses conducting diverse lines of business may properly be considered as engaged in only one (1) unitary business when the central executive officers are actively involved in the

operations of the various business activities and there are centralized offices which perform for the business activities the normal matters which a truly independent business would perform for itself, such as personnel, purchasing, advertising, financing; or research and development.

159 COMBINED REPORTING: DETERMINATION OF UNITY

- 159.1 *Newly formed corporations.* When a corporation that is a member of a unitary group forms another corporation, a presumption of unity arises between the two (2) corporations as of the date of formation. Any party may rebut the presumption by proving that the corporations or entities are not unitary or became unitary at a later date. For purposes of this rule, a newly formed corporation or entity includes but is not limited to:
- (a) A corporation that is formed through a corporate reorganization, a corporate divestiture, split-up or split-off;
 - (b) One (1) or more new subsidiaries is acquired and substantially all of the assets and operations of an existing division or operation are placed into or under the administrative or operational responsibility of the acquired corporation;
 - (c) A partnership is created or formed; or
 - (d) An existing corporation changes its form of doing business from one (1) organizational structure to a new organizational structure or merges into an existing or newly formed entity.
- 159.2 *Newly acquired corporations.* When a corporation acquires another corporation so that the acquired corporation is a member of a commonly controlled group for the first time, it shall be presumed that the acquiring and acquired corporations are not engaged in a unitary business for the purchaser's taxable year that includes the acquisition. If the purchaser is already a combined group member, the taxable year that includes the acquisition is the taxable year of the combined group.
- 159.3 The presumption may be rebutted by proving that the corporations are unitary. If the presumption is rebutted, then the corporations shall be considered unitary as of the date of acquisition, unless the evidence shows that unity was established as of another date.
- 159.4 In the succeeding reporting period after the first reporting period subsequent to an acquisition whereby a corporation that is a member of a unitary group acquires another corporation, and for all reporting periods thereafter, a presumption of a unitary relationship exists. The presumption may be rebutted by proving that the corporations are not unitary.

- 159.5 *Pre-existing relationship.* The presumption against unity shall not apply if, immediately preceding the acquisition, the acquiring and acquired corporations were engaged in a unitary business apart from being in the same commonly controlled group.
- 159.6 *Refusal to provide information.* In all cases, the Chief Financial Officer's determination of whether an entity is engaged in a unitary business is presumed to be correct if the taxpayer unreasonably refuses to provide information pertinent to the determination of a unitary business.
- 159.7 *Noncontrolling factors.* Where evidence of a unitary business relationship exists as between two (2) or more corporations such evidence is not negated by:
- (a) The use of arms-length pricing for sales, exchanges, or transfers between entities; or
 - (b) The fact that a business uses a separate accounting system, including separate accounting division, by entity, by geographical area, by business function, or by business segment.
- 159.8 Unitary members compute their liability relating to a year when a member is added to or ceases to be a member of the unitary group as follows: if a corporation becomes a member of a unitary group during the group's common accounting period, or ceases to be a member during the period, the other members shall take into account the appropriate portion of the part year member's income and the property, payroll, and sales attributes of the part-year member in computing their tax liabilities. *See* § 167.
- 159.9 *Part-year unitary member.* Business income attributable to the portion of the year during which the part-year unitary member was a unitary group member is combined with business income of the other unitary group members for the same portion of the year, and the total income is apportioned to the District on a combined apportionment basis. *See* § 167.
- 159.10 Where the part-year unitary member is taxable in the District, business income attributable to the portion of the year during which such unitary member was not a unitary member is apportioned to the District on the basis of the part-year member's separate property, payroll, and sales attributes for the part of the year during which the part-year unitary member was not a unitary member. The corporation is required to file a separate return for this portion of its income.

160 COMBINED REPORTING: PASSIVE HOLDING COMPANIES

- 160.1 *Passive holding companies.* A passive holding company that is in a commonly controlled trade or business and holds intangible assets that are used by the trade

or business in a unitary business shall be deemed to be engaged in the unitary business, even if the holding company's activities are primarily passive.

- 160.2 A passive parent holding company that directly or indirectly controls one (1) or more operating company subsidiaries engaged in a unitary business shall be deemed to be engaged in a unitary business with the subsidiary or subsidiaries, even if the holding company's activities are primarily passive.

161 COMBINED REPORTING: STATUTE OF LIMITATIONS

- 161.1 *Statute of limitations.* If the statute of limitations applicable to refund claims and assessments is open with respect to a particular member of the combined group, the statute of limitations is open with respect to that particular taxpayer notwithstanding the fact that the statute of limitations may have expired for one (1) or more other members of the combined group.

- 161.2 The statute of limitations applicable to refund claims and assessments for members of a combined reporting group which have filed their tax return based on a fiscalized reporting period matched to the accounting period of the designated agent shall be the statute of limitations determined and computed based on the fiscalized accounting period.

- 161.3 If a return is filed pursuant to a combined report, the Chief Financial Officer may examine and audit that return, and collect any deficiency from a combined group member for whom the statute of limitations for assessments has not expired, even if the statute of limitations for other members which filed pursuant to the same combined report has expired. Any deficiency assessed pursuant to the audit or examination will not cause a reopening of the statute of limitations for those other members for which the statute of limitations has expired who filed pursuant to the same combined report.

162 COMBINED REPORTING: WATER'S EDGE AND WORLDWIDE REPORTING; AND INITIATION AND WITHDRAWAL OF ELECTION

- 162.1 *General rule.* A corporation, regardless of its place of incorporation or formation, is required to file a combined report when it is subject to tax under chapter 18 of title 47 of the D.C. Official Code and is engaged in a unitary business with one (1) or more corporations that are required to be included in a combined report. The taxable member or members of the combined group engaged in a unitary business may elect to determine their apportioned share of the aggregate taxable net income or loss derived from the unitary business pursuant to a worldwide election under which each taxable member shall take into account the income and apportionment factors of all the members, wherever located, includible in the combined group. However, if the taxable members of a combined group do not make this election, each taxable member shall determine its apportioned share of such income on a basis as determined under § 162.2.

- 162.2 *Water's edge determination.* Absent an election to report based upon a worldwide unitary combined reporting basis, taxable members of a unitary group shall determine each of their apportioned shares of the net business income or loss of the combined group on a water's edge unitary combined reporting basis. In determining tax on a water's edge unitary combined reporting basis, taxable members shall take into account all or a portion of the income and apportionment factors as required under D.C. Official Code § 47-1810.02 (2005 Repl.).
- 162.3 *Mechanics for making the worldwide election.* A worldwide election shall be made by the designated agent of the combined group. The election shall be made on an original, timely filed return or as otherwise required by the Chief Financial Officer to be in writing. A return shall be considered timely if it is filed on or before the earliest due date or extended due date for the filing of the designated agent's return. No return filed after this date, shall constitute a valid worldwide election. The election, to be valid, must indicate in the manner that the Chief Financial Officer requires that every corporation that is a member of the combined group has agreed to be bound by such election, including an agreement by each member of the group that such election shall apply to any member that subsequently enters the group and an agreement that each member continues to be bound by the election in the event that such member is subsequently the subject of a reverse acquisition described in *Treas. Reg. § 1.1502-75(d)(3)*.
- 162.4 *Effect of election in subsequent tax years.* A worldwide election shall be binding for and applicable to the taxable year for which it is made and for the next nine (9) taxable years. Any corporation entering the unitary combined group after the year of the election shall be deemed to have consented to the application of the election and to have waived any objection thereto. Reverse acquisition rules based on the federal rules set forth in *Treas. Reg. § 1.1502-75(d)(3)* shall be applied in determining whether a corporation is bound by a worldwide election in fact patterns described in such rules.
- 162.5 *Revocation, renewal of election.* A worldwide election, once made, cannot be revoked until after it has been effective for ten (10) taxable years. When an election is made it may be renewed after ten (10) taxable years for another ten (10) taxable years. The revocation or renewal of an election shall be made on an original, timely filed return by the combined group's designated agent or as otherwise required in writing by the Chief Financial Officer. A revocation or renewal shall be effective for the first taxable year after the completion of the ten (10) taxable years for which the prior election was in place. Any revocation or renewal, to be valid, must indicate, in the manner required by the Chief Financial Officer that every corporation that is a member of the combined group has agreed to be bound by such revocation or renewal. If a prior worldwide election is neither affirmatively revoked nor renewed after ten (10) taxable years, the election shall terminate for the subsequent taxable year, but a new worldwide election may be made for any ten (10)-year period thereafter by election.

162.6 *Change in reporting method.* If either the water's edge or worldwide method was used to account for the combined group member's income and apportionment data in the preceding tax year and the other method is to be used for the combined group's combined report for the current tax year, adjustments to the income and apportionment data of the group members shall be made to prevent income and apportionment data from being omitted, or duplicated.

162.7 *Agreement to provide documents.* An election under § 162 shall constitute consent to the production of documents or other information that the Chief Financial Officer reasonably requires. For example, for purposes of verifying the appropriate members of the combined group, that the requirements of the worldwide election have been met, and that the tax computation and tax reporting are proper. The documents shall be provided in language and form acceptable to the Chief Financial Officer.

163 COMBINED REPORTING: DETERMINATION OF TAXABLE INCOME OR LOSS USING COMBINED REPORT

163.1 The use of a combined report does not disregard the separate identities of the taxable members of the combined group. Each taxable member is responsible for tax based on its taxable income or loss apportioned or allocated to the District, which shall include, in addition to other types of income, the taxable member's apportioned share of business income of the combined group, where business income of the combined group is calculated as a summation of the individual net business incomes of all members of the combined group. A member's net business income is determined by removing all except business income, expense and loss from that member's total income, as provided in section 8002(d) of the Fiscal Year 2012 Budget Support Act of 2011, effective September 14, 2011 (D.C. Law 19-21; to be codified at D.C. Official Code §§ 47-1810.04- 47-1810.05).

164 COMBINED REPORTING: COMBINING SPECIAL APPORTIONMENT METHODS

164.1 Unitary groups which include some members which are required to use the four (4)-factor apportionment formula and other members which are required to use a special apportionment method, such as financial institutions and transportation companies are subject to apportionment as described below:

- (a) Unitary group members who use the four (4)-factor formula and those that use special apportionment methods shall be separated into subgroups for purposes of allocation and apportionment. The subgroup of unitary group members who use the four (4)-factor formula and the subgroup of those that use special apportionment methods must separately calculate their modified federal taxable income. This calculation must be made as

though all members of both subgroups are included in the same federal consolidated pro-forma return, including the elimination of all intercompany transactions, regardless of whether between or among unitary group member who use the four (4)-factor formula and/or those that use special apportionment methods;

- (b) Each subgroup must separately allocate any allocable income or loss applying the relevant rules contained in either the D.C. Official Code or the District of Columbia Municipal Regulations;
- (c) For the business income or loss portion of the modified federal taxable income of each subgroup, each subgroup shall separately compute its District apportionment factor(s) and then apply the factor(s) to its business income or loss;
- (d) All income or loss allocated and apportioned to the District by each of the subgroups should be added together to produce an aggregated District tax base; and
- (e) The District's income tax rate should be applied to this tax base to determine the proper District tax due.

165 COMBINED REPORTING: NET OPERATING LOSS

165.1 *Post-apportioned net operating losses.* A taxable member may carry forward its net operating losses, which may include an apportioned loss derived from its activities as part of the combined group, subject to the net operating loss limitations, and carryover provisions of the D.C. Official Code. A net operating loss carryforward is an attribute of the separate corporation rather than of the combined group. A taxable member may not share all or a portion of its net operating loss carryforward with other members of its combined group. The carryforward will be utilized only by that taxable member which is part of the unitary group in offsetting the taxable member's District taxable income.

165.2 *Pre-combination net operating losses.* Net operating losses which originated in a taxable year beginning before January 1, 2011, that are carried forward by a taxable member of a combined group, cannot be shared with other taxable members. If the net operating loss carryforward was generated during a tax year in which the taxable member filed a consolidated return, the net operating loss shall be determined on a separate entity basis. The carryforward will be utilized only by that taxable member which is part of the unitary group in offsetting the taxable member's District taxable income.

166 COMBINED REPORTING: CREDITS

166.1 A tax credit generated by a taxable member of a combined group is an attribute of the taxable member rather than of the combined group, and credits are to be computed for each taxpayer separately. Therefore, a tax credit earned by a member of the combined group that is not fully used by or allowed to that member shall not be used in either whole or in part by any other member of the combined group or applied in whole or in part against the total income of the combined group.

166.2 A tax credit carryforward of a member of a combined group that was derived from a credit earned by the member either during a year in which the member was subject to combined reporting or a prior year when the member was not subject to combined reporting shall not be used in either whole or in part by any other member of the combined group or applied in whole or in part against the total income of the combined group.

167 **COMBINED REPORTING: TAXABLE YEAR OF COMBINED REPORT**

167.1 *Combined group's taxable year.* The combined group's taxable year is the taxable year of the designated agent.

167.2 *Method for members with differing taxable years.* If the taxable year of a combined group member differs from the taxable year of the combined group, the designated agent shall include that member's net income or loss and apportionment factors in the combined report by using the *pro rata method*; however the Chief Financial Officer may require use of the interim closing method in certain instances.

167.3 *Pro rata method.* Under the *pro rata* method, the income and apportionment data of the member as adjusted to reflect the determination of income under District law is assigned to the respective portion of the combined group's taxable year based on the ratio of months in common with the tax year of the combined group.

(a) In the event that the *pro rata* method requires the determination of income and apportionment data of a corporation whose taxable year has not yet closed, and the information cannot be obtained in time for the other members to file an accurate return, the income and apportionment data for that period shall be estimated based on available information. If the use of actual income and apportionment data results in a material misstatement of income apportioned to the District by the combined group, the taxable members must file an amended return to reflect the change.

(b) *Material misstatement.* For the purpose of determining whether a re-determination of income made with respect to the *pro rata* method results in a material misstatement of income apportioned to the District by the combined group, it is presumed that there is such material misstatement where the aggregate tax liability of the combined group members that filed

returns based on a *pro rata* estimate is found to have understated the aggregate correct liability for such members by the greater of ten thousand dollars (\$10,000) or ten percent (10%) or, where the change in the apportioned group income for any one taxable member of the group increases or decreases by more than one hundred thousand dollars (\$100,000).

167.4 The designated agent shall use the *pro-rata* method in each subsequent taxable year unless it obtains written approval from the Chief Financial Officer to use another method.

167.5 *Part-year members.* If, during a combined group's taxable year, a corporation ceases to be a member of the combined group or a new corporation becomes a member, the designated agent shall include that corporation's items attributable to the portion of the taxable year that the corporation was a member in the combined return covering the combined group's entire taxable year. For the portion of the taxable year when the corporation was not a member of the combined group, the corporation shall file a separate return or file in the combined report of another combined group, as applicable.

168 COMBINED REPORTING: DESIGNATED AGENT, LIABILITY

168.1 *Designated agent.* In the event that there are two (2) or more taxable members of a combined group, as a filing convenience, and without changing the respective liability of the group members, the taxable members of a combined group shall designate one taxable member of the combined group to file a single return in the form and manner prescribed by the Chief Financial Officer, in lieu of filing their own respective returns. Except as otherwise approved in writing by the Chief Financial Officer, the designated agent shall be the taxable member of the combined group that is either the combined group's common parent corporation, or, where there is no such common parent corporation or the parent corporation is not a taxable member of the combined group, the taxable member of the combined group that the group reasonably expects will have the largest amount of District taxable net income (District apportionment factors) on a recurring basis.

168.2 *Duties of designated agent.* The designated agent agrees to act as the agent on behalf of the taxable members of the combined group for all tax matters relating to the combined group, including, but not limited to: estimated tax payments, assessments; requesting extensions of time to file returns; making, renewing or revoking an election such as the worldwide election; filing a refund claim; accepting of refunds or notices; executing waivers and powers of attorney; and providing access to tax and other relevant records of all members of the combined group as reasonably requested by the Chief Financial Officer.

168.3 *Continuity of agency into future years.* Once a member of the combined group is appointed as the designated agent, it shall remain the designated agent of that

group for all future tax years. If the designated agent (a) leaves the combined group, (b) is acquired by another combined group, or (c) ceases to exist, a new designated agent will be determined under § 168.1.

168.4 *Liability.* Every member of a combined group shall be jointly and severally liable for any tax due from any member of the combined group subject to tax under chapter 18 of title 47 of the D.C. Official Code, including any interest, additions to tax, and penalties, to the extent permitted under the Constitution of the United States. An assessment against any member of a combined group for the tax attributable to the group's income in a particular taxable year, including any interest, additions to tax, or penalties, shall be deemed to constitute an assessment against all members of the combined group for that year.

169 COMBINED REPORTING: CALCULATING THE APPORTIONMENT FACTOR NUMERATOR AND DENOMINATOR

169.1 Each taxable combined group member shall determine its share of combined group income attributable to the District using apportionment factor numerators that reflect only that member's own property, payroll, and sales attributable to the District pursuant to D.C. Official Code § 47-1810.02 (2005 Repl.) Each taxable combined group member's denominator shall contain the property, payroll, and sales of the entire combined group wherever those property, payroll and sales are attributed.

170 COMBINED REPORTING: UNINCORPORATED BUSINESS ENTITIES / PARTNERSHIPS

170.1 Notwithstanding any other provision of chapter 18 of title 47 of the D.C. Official Code or the combined reporting rules, if the combined group includes or any member of the combined group owns an unincorporated business that would be subject to the tax imposed under D.C. Code § 47-1808.03 (2005 Repl.), the income or loss of such unincorporated business shall be apportioned to the District using apportionment factors of the unincorporated business, and the combined group member's distributive share of income from the Schedule K-1 (K-1) shall be added to the combined group member's taxable income as computed for the District. The *pro rata* share of that income that was actually taxed at the unincorporated business level by the District shall be subtracted.

170.2 The income which is not subject to the unincorporated business tax under D.C. Official Code § 47-1808.03 (2005 Repl.) shall be included in the combined report.

170.3 If the unincorporated business is not included in the combined group, the unincorporated business shall file its own stand-alone return using form D-30 (District unincorporated business franchise tax return), and be subject to tax under D.C. Official Code § 47-1808.03 (2005 Repl.).

170.4 *Examples.*

- (a) A combined group member owns one hundred percent (100%) of a partnership or limited liability company (LLC). The partnership or LLC is considered disregarded for federal income tax purposes and files no unincorporated business franchise tax return. The owner of the disregarded entity files a District tax return and reports all income and expenses, including income and expenses of the disregarded entity. In the owner of disregarded entity's return apportionment factors, the owner of disregarded entity includes the payroll, property and sales of the disregarded partnership or LLC in both the numerator and denominator.
- (b) A combined group member owns less than one hundred percent 100% but more than fifty percent (50%) of a partnership or LLC. The partnership files an unincorporated business franchise tax return. The combined group member owner of the partnership or LLC includes the gross distribution (K-1) of the partnership or LLC income in its income and deducts its distributive share of income that was actually taxed at unincorporated business level. The combined group member includes the partnership's K-1 income in the apportionment sales numerator and denominator. No payroll or property is included in the apportionment factor of the partnership in the combined group member's own property and payroll factor.
- (c) If the combined group member owns less than a controlling interest of the partnership or LLC, the partnership or LLC may not meet the criteria to be included in combined reporting. However, the combined group member shall nevertheless add its distributive share of income from the partnership or LLC in its income and subtract its distributive share of income that has been taxed at the unincorporated business level. It shall also add its distributive share of income to its sales factor denominator and numerator based on its unincorporated franchise tax apportionment factors.

171 COMBINED REPORTING: MINIMUM TAX PAYABLE

171.1 The minimum tax payable as provided under D.C. Official § 47-1807.02(c) (2005 Repl.) applies to each taxable member of the combined reporting group and the minimum tax of each taxable member shall be included in the combined report.

172 COMBINED REPORTING: ESTIMATED TAX PAYMENTS

172.1 *Combined estimated tax payments.* In general, only the designated agent of a combined group may make the estimated tax payments that must be made by the taxable members included in the combined report.

172.2

Exception: When separate estimated payments are allowed. Although the designated agent is always authorized to make estimated payments on behalf of any and all of the combined group members, a combined group member other than the designated agent may make estimated payments on its own behalf if any of the following apply:

- (a) For the first taxable year for which a combined group files a combined return, any member of the group may make estimated payments on its own behalf; and
- (b) For the first taxable year for which a corporation is a member of a combined group, that corporation may make estimated payments on its own behalf.

Comments on this proposed rulemaking should be submitted in writing to Aaishah Hashmi, Assistant General Counsel, Office of Tax and Revenue, 1101 4th Street, S.W., 7th Floor, Washington, D.C. 20024, or via email at aaishah.hashmi@dc.gov no later than thirty (30) days after publication of this notice in the *D.C. Register*. Copies of this rule and related information may be obtained by writing to the person at the address stated herein.