

OFFICE OF TAX AND REVENUE

NOTICE OF FINAL RULEMAKING

The Deputy Chief Financial Officer of the District of Columbia Office of Tax and Revenue (OTR) of the Office of the Chief Financial Officer, pursuant to the authority set forth in D.C. Official Code § 47-1335 (2005 Repl.), 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 (2012 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 this final action 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 for tax years beginning after December 31, 2010. 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 will calculate their taxable net income derived from the unitary business as its apportioned share of the income or loss of the combined group engaged in the unitary business.

These rules were previously published in the *D.C. Register* on January 20, 2012, 59 DCR 343 and again on August 31, 2012, 59 DCR 10509. This final rulemaking shall become effective upon 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: OUTLINE; PURPOSE; GENERAL RULE; EFFECTIVE DATE; AND DEFINITIONS

156.1 *Outline.* 156, *et seq.* is organized as follows:

- 156. Outline, Effective Date, Purpose; General Rule; Revocation of Election to File Consolidated Returns; and Definitions
- 157. Composition of the Combined Group
- 158. Determination of a Unitary Business; Commonly Controlled; and Unitary Presumptions
- 159. Passive Holding Companies
- 160. Statute of Limitations

161. Water's-Edge Determination
162. Worldwide Reporting; and Initiation and Withdrawal of Election
163. Determination of Taxable Income or Loss Using a Combined Report
164. Combining Special Apportionment Formulas
165. Net Operating Losses
166. Tax Credits
167. Taxable Year; Part-Year Members
168. Designated Agent; Liability
169. Apportionment
170. Unincorporated Business Entities / Partnerships
171. Minimum Tax Payable
172. Estimated Tax Payments
173. Real Estate Investment Trusts
174. Regulated Investment Companies
175. FAS 109 Deduction
176. Time and Place for Filing Tax Returns; Extensions; Closing Out Separate Entities

156.2 *Effective date.* The combined reporting regulations shall be effective for tax years beginning after December 31, 2010.

156.3 *Purpose.* The purpose of the combined reporting regulations is to provide rules for the combined reporting of income as required by D.C. Official Code § 47-1805.02a (2005 Repl.) which requires 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 or more persons to compute its share of the combined unitary income or loss attributable to the District using a combined report.

156.4 *General rule.* A person 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 under D.C. Official Code § 47-1805.02a (2005 Repl.) and the combined reporting regulations. The combined report shall be filed with the taxpayer member'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.

156.5 *Revocation of election to file consolidated returns.* Any taxpayer election that was made under D.C. Official Code § 47.1805.02(5)(B) and (C) (2005 Repl.) and 9 DCMR § 109 is revoked for tax years beginning after December 31, 2010.

156.6 *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 under D.C.

Official Code § 47-1810.02 (2005 Repl.) and the DCMR 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 D.C. Official 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 member's tax return and which report the income and apportionment information of all persons that are members of the taxpayer member's combined group, as well as any supporting information required by the Chief Financial Officer;
- (d) **Combined reporting regulations/rules** – the rules provided under 9 DCMR §§ 156 through 175;
- (e) **Combined unitary income** - the combined group's net income or loss attributable to the unitary business which is subject to combination under 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 ownership interest and/or 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 ownership interest and/or voting power of the members in the group;
- (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 taxpayer member of the combined group who is responsible for acting on behalf of the group for matters relating to the combined report including filing the combined report *See* 9 DCMR § 168;
- (j) **Person** – shall have the same meaning as defined under D.C. Official Code § 47-1801-01(39) except a “person” within the meaning of the combined reporting statute and regulations does not include individuals;
- (k) **Taxpayer member** – A member of a combined group that has nexus in the District and is therefore subject to tax on its income under chapter 18 of title 47 of the D.C. Official Code.
- (l) **Unitary business** – shall have the same meaning as defined under D.C. Official Code § 47-1801.04(55)(A). *See* 9 DCMR § 158.1.
- (m) **Water’s-edge rules** - the rules provided under 9 DCMR § 161 under which some or all of a person’s items attributable to a unitary business are not subject to combination because of the degree of the person’s activity outside the United States; and
- (n) **Worldwide election** - an election by the designated agent of the combined group on behalf of all of the members of the group to treat as the combined group, for purposes of 9 DCMR §§ 156 through 175, 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: COMPOSITION OF THE COMBINED GROUP**

- 157.1 *General rule.* Where a person subject to tax under chapter 18 of title 47 of the D.C. Official Code is engaged in a unitary business with one or more other persons that are related by common ownership, the taxpayer member must determine its tax liability based upon the income and apportionment information of all persons included in the combined group using a combined report unless it is an excluded person under 9 DCMR § 157.3.
- 157.2 *Included persons.* Persons that are required to be included in a combined group and therefore required to be included in a combined report filed by the designated agent of a combined group shall include all persons 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, even if those persons do not have nexus. The persons to be included in a combined group include, but are not limited to, any unincorporated business, 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 persons.* Persons 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 member of such group, include, unless such persons are otherwise required to be included under D.C. Official Code § 47-1805.02a: any insurance company subject to premium tax under D.C. Official Code § 47-2608 (2005 Repl.) or § 31-3403.01 (2005 Repl.) exempt organization including an organization that has unrelated business income subject to tax under I.R.C. § 511; Qualified High Technology Company (QHTC); person, regardless of the place incorporated or formed, if the average of its property, payroll, and sales factors outside the U.S. is eighty percent or more; or as otherwise provided in chapter 18 of title 47 of the D.C. Official Code.

158 **COMBINED REPORTING: DETERMINATION OF A UNITARY BUSINESS; COMMONLY CONTROLLED; AND UNITARY PRESUMPTIONS**

158.1 *Determination of unitary business.* The term “unitary business” is defined in D.C. Official Code § 47-1801.04(55)(A) as a single economic enterprise that is made up either of separate parts of a single business entity or of 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 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.

158.2 *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 in the same "commonly controlled group" for District purposes. "Commonly controlled group" has the stated meaning in 9 DCMR § 156.6(g) and 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 (1) 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;
- (2) Any two 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; or
- (3) Any two or more entities including unincorporated businesses or partnerships if a common owner, regardless of whether the owner is a corporate entity, directly or indirectly owns more than fifty percent (50%) of interest in the entities.

158.3

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%) ($40\% + (50\% \times 30\%)$) of the voting power of Corporation B.

- (a) 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.

- (b) 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.

158.4

Voting power.

- (a) A shareholder has ownership or control of stock representing more than fifty 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.
- (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.

158.5 *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.

158.6 *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 combined group.

158.7 *Sufficiently interdependent, integrated, and interrelated.*

- (a) In general, the segments in a commonly owned or controlled economic enterprise are considered a unitary business if their activities generate synergy and 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 economic enterprise 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.

158.8 *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 enterprise; 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.

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

- (a) Assisting in acquisition of assets;
- (b) Assisting with filling personnel needs;
- (c) Lending funds, guaranteeing loans, or pledging assets;
- (d) Interplay in the area of corporate expansion, including but not limited to common future planning or development of the enterprise;
- (e) Providing technical assistance, general operational guidance, or overall operational strategic advice;
- (f) Supervising or common management;
- (g) Common offices, manufacturing facilities, or distribution systems (including but not limited to transportation facilities, warehousing facilities, or order fulfillment systems, inventory control systems or other distribution systems or subsystems);
- (h) Centralized purchasing, marketing, advertising, accounting, or research and development;
- (i) Intercorporate sales or leases, including equipment and real estate;
- (j) Intercorporate services, including administrative, data management, computer support, employee benefits, human resources, such as training and recruiting programs and hiring and personnel policies, insurance, tax compliance, legal, financial, and cash management services;
- (k) Intercorporate use of proprietary materials, including trade names, trademarks, service marks, patents, copyrights, trade secrets or other intellectual property;
- (l) Centralized executive force; and
- (m) Common employees, including sales force;

158.10 *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. 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.

Presumptions. Presence of a unitary business will be 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 entities 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.
- (d) *Newly formed entities.* When an entity that is a member of a unitary group forms another entity, a presumption of unity arises between the two (2) entities as of the date of formation. Any party may rebut the presumption by proving that the entities are not unitary or became unitary at a later date. For purposes of this rule, a newly formed entity includes but is not limited to:
 - (1) A corporation that is formed through a corporate reorganization, a corporate divestiture, split-up, or split-off;
 - (2) 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;

- (3) A partnership or unincorporated business is created or formed; or
- (4) 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.

(e) *Newly acquired entities.*

- (1) When an entity acquires another entity so that the acquired entity is a member of a commonly controlled group for the first time, it shall be presumed that the acquiring and acquired entities 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.
- (2) The presumption may be rebutted by proving that the entities are unitary. If the presumption is rebutted, then the entities shall be considered unitary as of the date of acquisition, unless the evidence shows that unity was established as of another date.
- (3) In the succeeding reporting period after the first reporting period subsequent to an acquisition whereby an entity that is a member of a unitary group acquires another entity, and for all reporting periods thereafter, a presumption of a unitary relationship exists. The presumption may be rebutted by proving that the entities are not unitary.

(f) *Pre-existing relationship.* The presumption against unity shall not apply if, immediately preceding the acquisition, the acquiring and acquired entities were engaged in a unitary business apart from being in the same commonly controlled group.

(g) *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.

(h) *Noncontrolling factors.* Where evidence of a unitary business relationship exists as between two (2) or more entities such evidence is not negated by:

- (1) The use of arms-length pricing for sales, exchanges, or transfers between entities; or

- (2) 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 COMBINED REPORTING: PASSIVE HOLDING COMPANIES

159.1 *Passive holding companies.* A passive holding company that is in a commonly controlled economic enterprise and holds intangible assets that are used by the enterprise in a unitary business shall be deemed to be engaged in the unitary business, even if the holding company's activities are primarily passive.

159.2 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.

160 COMBINED REPORTING: STATUTE OF LIMITATIONS

160.1 *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 or more other members of the combined group.

160.2 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.

160.3 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.

161 COMBINED REPORTING: WATER'S-EDGE DETERMINATION

161.1 *Water's-edge determination.* Absent an election to report based upon a worldwide unitary combined reporting basis, taxpayer 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,

members shall take into account all or a portion of the income and apportionment factors as required under D.C. Official Code § 47-1810.07 (2005 Repl.) as follows:

- (a) *One hundred percent (100%) included.* All the income and apportionment factors must be included for the following members:
 - (1) Domestic corporations and entities.
 - (2) Any member, regardless of where it is incorporated or formed, if the average of its property, payroll, and sales factors within the United States is twenty percent (20%) or more;
 - (3) Domestic international sales corporations (DISC) described in I.R.C. §§ 991-994, foreign sales corporations (FSC) described in I.R.C. §§ 921-927, and export trade corporations (ETC) described in I.R.C. §§ 970-972; and
 - (4) Any member doing business in a tax haven, as defined in D.C. Official Code § 47-1801.04(49) (2005 Repl.).
- (b) *Partially included.* The following members that are not described above are included only to the extent of any U.S. source income and factors:
 - (1) Any member shall include its business income that is effectively connected or treated as effectively connected with the conduct of a trade or business within the United States and, for that reason, is subject to federal income taxation;
 - (2) Controlled foreign corporation (CFC) defined in I.R.C. § 957, if they have Subpart F income defined in I.R.C. § 952.
 - (3) Any member that is a resident of a country that does not have a comprehensive income tax treaty with the United States and earns more than twenty percent (20%) of its income, directly or indirectly, from intangible property or service-related activities that are deductible against the business income of the other members of the water's-edge group, to the extent of that income and the apportionment factors related thereto.

162

COMBINED REPORTING: WORLDWIDE REPORTING AND INITIATION AND WITHDRAWAL OF ELECTION

162.1

Worldwide reporting. The 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 member shall take into account the income and apportionment factors of all the members, wherever located, includible in the combined group. If the members of a combined group do not make this election, each member shall determine its apportioned share of such income on a water's-edge basis.

162.2 *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 election form and shall be attached to an original, timely filed return. The election, to be valid, must indicate, in the manner that the Chief Financial Officer requires, that every entity that is a member of the combined group has agreed to be bound by such election. This election must include 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)*.

162.3 *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 taxable years. Any person 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 person is bound by a worldwide election in fact patterns described in such rules.

162.4 *Change in reporting method.* If either the water's-edge or worldwide method was used to account for the combined group members' 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.

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 taxpayer members of the combined group. Each taxpayer 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 taxpayer 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 D.C. Official Code §§ 47-1810.04 and 47-1810.05.

163.2

Example: General computation of the taxpayer member's income.

Taxpayer's federal taxable income (determined without regard to federal consolidated rules)
+ or – District adjustments
– Taxpayer's nonbusiness income
– Taxpayer's business income from another unitary business (separately apportioned)
= Taxpayer's unitary business income

+ Other group members' similarly calculated unitary business income
= Total unitary business income

x Taxpayer's apportionment percentage (where each factor numerator is taxpayer's in
District factor, and each factor denominator is the sum of all group members' factors)
= Taxpayer's District unitary business income

+ Taxpayer's nonbusiness income allocated to the District
+ Taxpayer's business income from another unitary business (separately apportioned)
= Taxpayer's District taxable income

x Tax rate
= Taxpayer's gross District tax

– Taxpayer's District tax credits

= Taxpayer's District tax liability

See also 9 DCMR §170 for inclusion of unincorporated business and partnership income in the above calculation and 9 DCMR §171 for minimum tax due.

164

COMBINED REPORTING: COMBINING SPECIAL APPORTIONMENT FORMULAS

164.1

Combined 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 are subject to apportionment as described below:

- (a) Combined group members who use the four (4)-factor formula and those that use special apportionment methods for purposes of allocation and apportionment shall prepare a federal consolidated pro forma return consisting of all combined group members, including the elimination of all intercompany transactions, regardless of whether between or among combined group members who use the four (4)-factor formula and/or those that use special apportionment formulas;
- (b) Each member shall separately compute its District apportionment factor numerators, determine its District apportionment factor based on the group's denominators, and then apply its factors to the group's business income or loss subject to apportionment to arrive at net income or loss

apportioned to the District;

- (c) Each member shall compute its nonbusiness income separately subject to the allocation rules;
- (d) All income or loss allocated and apportioned to the District by each member shall be added together to arrive at District taxable income for each member; and
- (e) Each member shall apply the appropriate District income tax rate to determine the proper District tax due.

164.2 *Example: Financial Institutions*

| DISCRIPTION | | COMBINED REPORT | CORPORATION A | FINANCIAL INSTITUTION |
|--------------------------------|------------|-----------------|---------------|-----------------------|
| Sales | District | \$3,000,000 | \$2,000,000 | \$1,000,000 |
| Sales | Everywhere | \$20,000,000 | \$10,000,000 | \$10,000,000 |
| District Weighted Sales Factor | | | 20.00% | 5.00% |
| | | | | |
| Property | District | \$20,000 | \$20,000 | |
| Property | Everywhere | \$250,000 | \$250,000 | |
| | | | 8.00% | |
| Payroll | District | \$30,000 | \$20,000 | \$10,000 |
| Payroll | Everywhere | \$500,000 | \$250,000 | \$250,000 |
| | | | 4.00% | 2.00% |
| District Apportionment Factor | | | 8.00% | 3.50% |

* The receipt factor for financial institutions is not double-weighted. See 9 DCMR § 129. The sum of the factors (sales/receipts and payroll), excluding property, is divided by two.

165 COMBINED REPORTING: NET OPERATING LOSSES

165.1 *Post-apportioned net operating loss carryforwards.* A combined group member may carry forward its District apportioned net operating loss to the extent the carryforward and offset is consistent with the requirements and limitations of D.C. Official Code § 47-1803.03(a)(14). A District apportioned net operating loss carryforward is an attribute of the separate entity rather than of the combined group. A combined group member may not share all or a portion of its net operating loss carryforward with other members of the combined group or as an offset against the total income of the combined group. A District apportioned net operating loss carryforwards shall be allowed to offset only the District taxable income of the combined group member that created the net operating loss.

165.2 *Pre-combination net operating loss carryforwards.* Each member of a combined group shall have its own net operating loss carryforward deduction (before

apportionment) for loss years prior to 2000 and District apportioned net operating loss deduction (after apportionment) for loss years 2000 and thereafter where:

- (a) Such member filed a separate District franchise tax return for tax years beginning before January 1, 2011; or
- (b) Such member was included in a District consolidated return for tax years beginning before January 1, 2011, in which case, the net operating loss shall be determined on a separate entity basis by using the prorated amount of the consolidated net operating loss assigned to the District consolidated member if that member had a loss.

165.3 *Example: Applying an NOL in a Combined Report.*

| YEAR 1: | Corp. X | Corp. Y | Corp. Z | Combined |
|--|----------------|----------------|----------------|-----------------|
| Unitary business income (loss) subject to apportionment | (400,000) | (10,000) | 60,000 | (350,000) |
| Apportionment percentages | 5% | 1% | 3% | 9% |
| Loss apportioned to D.C. (combined loss x apportionment %) | (17,500) | (3,500) | (10,500) | (31,500) |
| Nonbusiness items wholly attributable to D.C. | 50,000 | (2,500) | 0 | |
| D.C. net income (loss) | 32,500 | (6,000) | (10,500) | |
| NOL available to be carried forward (100% of loss) | 0 | (6,000) | (10,500) | |

| YEAR 2: | Corp. X | Corp. Y | Corp. Z | Combined |
|--|----------------|----------------|----------------|-----------------|
| Unitary business income (loss) subject to apportionment | 50,000 | 80,000 | (5,000) | 125,000 |
| Apportionment percentages | 6% | 4% | 4% | 14% |
| Income apportioned to D.C. (Combined income x apportionment %) | 7,500 | 5,000 | 5,000 | 17,500 |
| Non-business items wholly attributable to D.C. | 2,500 | (10,000) | 0 | |
| D.C. net income (loss) | 10,000 | (5,000) | 5,000 | |
| Application of NOL carryforward from Year 1 | 0 | 0 | (5,000) | |
| D.C. net income (loss) | 10,000 | (5,000) | 0 | |
| NOL available to be carried forward (100% of loss) | 0 | (5,000) | 0 | |

| | Corp. X | Corp. Y | Corp. Z |
|-------------------------------------|----------------|----------------|----------------|
| Remaining NOL from Year 1 | 0 | (6,000) | (5,500) |
| Loss in Year 2 | 0 | (5,000) | 0 |
| NOL available to be carried forward | 0 | (11,000) | (5,500) |

166 COMBINED REPORTING: TAX CREDITS

166.1 *Current year tax credits.* A tax credit generated by a member of a combined group is an attribute of the 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 *Tax credit carryforward.* A tax credit carryforward of a member of a combined group that was derived from a credit generated 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; PART YEAR MEMBERS

167.1 *Taxable year of the combined group.* The combined group's taxable year is determined as follows:

- (a) If two (2) or more members of a group file a federal consolidated return, the group's taxable year is the taxable year of the federal consolidated group; and
- (b) In all other cases, the group's taxable year shall be the taxable year of the designated agent.

167.2 *52 to 53 week tax years.* Where a member files federal income tax returns on the basis of an annual period which varies from fifty-two (52) to fifty-three (53) weeks, its taxable year shall be treated as beginning with the first day of the calendar month beginning nearest to the first day of such taxable year or ending with the last day of the calendar month ending nearest to the last day of such taxable year.

167.3 *Members with different 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.

167.4 *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) The income and apportionment data from the member's recomputed taxable years is then combined with the income and apportionment data of the taxable year of the combined group, along with the income and apportionment data of other members of the combined group for the same period, similarly recomputed if necessary. The combined group's taxable

income is then apportioned to each of the taxable members of the combined group.

- (b) In the event that the pro rata method requires the determination of income and apportionment data of a member 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 taxpayer members must file an amended return to reflect the change.
- (c) *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 taxpayer member of the group increases or decreases by more than one hundred thousand dollars (\$100,000).

167.5 The pro-rata method shall be used in each subsequent taxable year unless the interim closing method is required.

167.6 *Part-year members.* If, during a combined group's taxable year, a member ceases to be a member of the combined group or a new person becomes a member, the designated agent shall include that person's items attributable to the portion of the taxable year that the person was a member in the combined report covering the combined group's entire taxable year. For the portion of the taxable year when the person was not a member of the combined group, the person 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 or more taxpayer members of a combined group, as a filing convenience, and without changing the respective liability of the group taxpayer members, the taxpayer members of a combined group shall designate one taxpayer 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. The designated agent shall be the taxpayer member of the combined group that is either the common parent, or, where there is no such common parent or the parent is not a taxpayer member of the combined

group, the taxpayer member of the combined group that has the greatest District business activity during the first year that the combined report is required to be filed, as measured by the total of the District factors, payroll, sales, and property for that year.

168.2 *Duties of designated agent.* The designated agent agrees to act as the agent on behalf of the taxpayer members of the combined group for all tax matters relating to the combined group, including, but not limited to: making estimated tax payments; assessments; requesting extensions of time to file returns; amending returns; reporting Internal Revenue Service adjustments to returns; renewing or revoking an election such as the worldwide election; filing a refund claim; reporting federal changes; 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 taxpayer 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 leaves the combined group, is acquired by another combined group, or ceases to exist, a new designated agent will be determined under § 168.1.

168.4 *Liability.* The designated agent of a combined group consents to act as surety with respect to the tax liability of all other taxpayer members, including, but not limited to, any interest, additions to tax, and penalties. If for any reason the designated agent is unwilling or unable to perform its responsibilities, tax liability may be assessed against the taxpayer members.

169 COMBINED REPORTING: APPORTIONMENT

169.1 *The Joyce Rule.* For apportionment purposes, the principle established in *Appeal of Joyce, Inc.* (Cal. SBOE 11/23/66) shall apply, in which each taxpayer member of the combined group is treated as a separate taxpayer and that taxpayer’s numerators will include only that taxpayer’s own property, payroll, and sales factor numerators attributable to the District and will not include a share of a non-nexus member’s factors. Each taxpayer member’s denominator shall contain the property, payroll, and sales of the entire combined group wherever those property, payroll, and sales are attributed regardless of nexus. The following example illustrates the *Joyce* method:

| Entity Name | District Receipts | Everywhere Receipts | District Nexus |
|--------------------|--------------------------|----------------------------|-----------------------|
| Entity A | 50 | 100 | Yes |
| Entity B | 100 | 200 | Yes |

| | | | |
|----------|-----|-----|----|
| Entity C | 100 | 200 | No |
| Factor | 150 | 500 | |
| Total | | | |

170 COMBINED REPORTING: UNINCORPORATED BUSINESS ENTITIES / PARTNERSHIPS

- 170.1 *General rule.* Notwithstanding any other provision of chapter 18 of title 47 of the D.C. Official Code or the combined reporting regulations, if the combined group includes or any member owns an unincorporated business (UB) that would be subject to the tax imposed under D.C. Official § 47-1808.03 (2005 Repl.), the income or loss of such UB shall be apportioned to the District using the apportionment factor of the UB, and the combined group member-partner’s distributive share of such income, including separately stated items, shall be added to the combined group member-partner’s “other income.” A combined group member-partner’s distributive share of that income that was actually taxed under D.C. Official Code § 47-1808.03 (2005 Repl.) shall be subtracted from the combined group member-partner as “other deductions” to prevent double taxation. The distributive share of the combined group member-partner shall be added to the numerator and denominator of the combined group member-partner’s sales factor using the apportionment factor of the UB.
- 170.2 *Distributive share.* Distributive share of income means the income reported on the Federal Schedule K-1 (K-1). If applicable, the distributive share of the UB income shall then be adjusted pro-ratably according to the amount attributable to the District.
- 170.3 *Untaxed income at the UB level.* The income which is untaxed at the UB level under D.C. Official Code [§ 47-1808.03](#) (2005 Repl.), including, but not limited to, the reasonable allowance for salaries under D.C. Official Code [§ 47-1808.03\(11\)](#) and (11)(b) (2005 Repl.), the exemption under D.C. Official Code § 47-1808.04 (2005 Repl.), or separately stated items such as guaranteed payments, shall be included in the combined group member-partner’s “other income” to the extent of the member-partner’s distributive share whether the UB is part of the combined group or not.
- 170.4 *Presumption of nexus.* If a partner takes a deduction for salary allowance or other distribution for services rendered to the UB or if a combined group member is the general partner or managing member, the partner or member shall be deemed to be actively engaged in the conduct of the business which shall create nexus in the District.
- 170.5 *Nonbusiness income.* If the income from the ownership interest in the partnership or UB is non-business income, then that income will be subject to allocation to the combined group member-partner.

- 170.6 *A UB that is part of the combined group.* If the combined group includes a UB (i.e. meets unitary requirements) that would be subject to the tax imposed under D.C. Official Code § 47-1808.03 (2005 Repl.), the UB shall report *all* its income and apportionment factors on the combined report only and the combined group member-partner shall include in its sales apportionment factor, the numerator which shall include the combined group member-partner's distributive share of District income from the K-1 using the UB's apportionment factor and the denominator which shall include the combined group member-partner's total distributive share of that income from the K-1. The combined group member-partner shall not include its share of the UB's payroll, property, or sales in its apportionment factors.
- 170.7 *A UB that is not part of the combined group.* If the combined group does not include a UB (i.e. does not meet unitary requirements) that would be subject to the tax imposed under D.C. Official Code § 47-1808.03 (2005 Repl.), the UB shall file its own stand-alone return using form D-30 (District unincorporated business franchise tax return) and be subject to the UB tax under D.C. Official Code § 47-1808.03 (2005 Repl.). However, the combined group member-partner shall include, in its sales apportionment factor, the numerator which shall include the combined group member-partner's distributive share of District income from the K-1 using the UB's apportionment factor and the denominator which shall include the combined group member-partner's total distributive share of that income from the K-1. The combined group member-partner shall not include its share of the UB's payroll, property, or sales in its apportionment factors.
- 170.8 *Partnership that is not a UB.* Provided that a combined group member who has an interest in a partnership, that is not a UB as defined by D.C. Official Code § 47-1808.01 (2005 Repl.) and would therefore not be subject to the UB tax imposed under D.C. Official Code § 47-1808.03 (2005 Repl.), the partnership shall file its own stand-alone return using form D-65 (District partnership return). However, the combined group member-partner shall include, in its sales apportionment factor, the numerator which shall include the combined group member-partner's distributive share of the partnership's District income from the K-1 and the denominator which shall include the combined group member-partner's total distributive share of partnership income from the K-1 which shall be added to the combined group member-partner's "other income." There shall be no subtraction of the income because the income was not taxed at the partnership level.
- 170.9 *Single Member Limited Liability Corporation (SMLLC).* If a combined group member owns one hundred percent (100%) of a partnership or limited liability company (LLC), and the partnership or LLC is considered disregarded for federal income tax purposes, the combined group member-owner of the disregarded entity shall include in the combined group member-owner's gross income and deductions of the disregarded entity on the combined report. The combined group

member-owner shall include the payroll, property, and sales of the disregarded entity in both its numerator and denominator.

171 COMBINED REPORTING: MINIMUM TAX PAYABLE

171.1 The minimum tax payable as provided under D.C. Official Code §§ 47-1807.02(b) and 47-1808.03(b) (2005 Repl.), as applicable, applies to each taxpayer member of the combined reporting group that is subject to tax under chapter 18 of title 47 of the District of Columbia Official Code and the minimum tax due of each taxpayer member shall be included in the combined report. If a combined group member's gross District tax is less than the minimum tax due, the minimum tax shall be due.

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

173 COMBINED REPORTING: REAL ESTATE INVESTMENT TRUSTS

173.1 *Dividends-paid deduction.* Under D.C. Official Code § 47-1803.03(a)(13) (2005 Repl.), a real estate investment trust shall be allowed a deduction from gross income of dividends paid by a real estate investment trust which qualify for the dividends-paid deduction under § 857 of the Internal Revenue Code.

174 COMBINED REPORTING: REGULATED INVESTMENT COMPANIES

174.1 *Dividends-paid deduction.* Under D.C. Official Code § 47-1803.03(a)(12) (2005 Repl.), a regulated investment company shall be allowed a deduction of dividends paid by a regulated investment company which qualify for the dividends-paid deduction under § 852 of the Internal Revenue Code.

**175 COMBINED REPORTING: FINANCIAL ACCOUNTING STANDARDS
NO. 109 (FAS 109) DEDUCTION**

175.1 *Eligibility.* If the enactment of combined reporting requirements for unitary businesses in the District results in an increase to a combined group's net deferred tax liability, the combined group is entitled to a FAS 109 deduction. "Net deferred tax liability" is defined as the net increase, if any, in deferred tax liabilities minus the net increase, if any, in deferred tax assets of the combined group, as computed in accordance with Generally Accepted Accounting Principles (GAAP) that would otherwise result from the imposition combined reporting in the District. Only companies that were publicly traded as of January 1, 2011 and that prepare their financial statements in accordance with GAAP qualify for the FAS 109 deduction. The term "publicly traded company" shall mean a company whose stock is publicly traded; a privately held company that issues publicly traded debt is not eligible for the FAS 109 deduction.

175.2 *Timing of the deduction.* The FAS 109 deduction shall be claimed annually over a seven (7)-year period beginning with the combined group's taxable year that begins in 2015 equal to one-seventh (1/7) of the deduction amount.

175.3 *Filing requirements.* Any taxpayer intending to claim the FAS 109 deduction shall file a form with the group's combined report with the Chief Financial Officer on or before the due date for the 2012 District franchise tax returns, specifying the total amount of the deduction which the taxpayer claims. This rule does not limit the authority to the Chief Financial Officer to review or redetermine the proper amount of any deduction claimed, whether on the form required or on a tax return for any taxable year.

175.4 *Recordkeeping requirements.* To facilitate review and potential audit of the taxpayer's form and any claimed deduction, a taxpayer shall maintain records and workpapers necessary to support the calculation and journal entries identified for the full length of taxable years in which the deduction may be claimed, and all additional periods of time for which such taxable years may be subject to audit or adjustment.

**176 TIME AND PLACE FOR FILING TAX RETURNS; EXTENSIONS;
CLOSING OUT SEPARATE ENTITIES**

176.1 *Extension for combined reporting filers for transition year.* Effective for tax years beginning on or after December 31, 2010, a calendar year taxpayer that is a member of a combined group and that must report income derived from the activities of that group in a combined report due on September 17, 2012, may receive an automatic extension until October 15, 2012. This extension applies to all final zero returns. *See* 9 DCMR § 176.2.

176.2 *Closing out separate entities.* If an entity filed a District return on a separate reporting basis or on a District consolidated basis for the tax year beginning prior to December 31, 2010, and that entity will now be filing on a combined reporting basis for the tax year beginning after December 31, 2010, that entity (or entities), except for the designated agent, shall file a separate final zero return along with the combined report.

177 - 185 Reserved for additional combined reporting regulations.