



Update on Combined Reporting

Revenue Laws Study Committee

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[Combined Reporting]

- **WHAT IS IT?**

It is a method of calculating the income of a group of affiliated corporations for tax purposes

- **HOW?**

It looks beyond the legal structure of separate incorporations to determine whether two or more affiliated corporations are engaged in a **single unitary business**

- **WHY?**

To ensure the income of a multiple entity unitary business computed and apportioned in the same manner as a single corporate business

[Single Entity Reporting State]

- Vulnerability of **single entity reporting state** to income shifting strategies
 - IHC in a low tax or no tax state
 - IHC in a combined reporting state
 - “Embedded royalty”
 - Interest expense
 - Transfer prices
 - Other inter-company transactions

[NC Legislative Efforts]

- **2001:** Royalty add-back
- **2002:** Broad definition of business income
- **2005:** Consideration of “throwout” rule
- **2006:** Patent and copyright add-back
- **2007:** Captive REITs

[Revenue Laws Goals]

- Provide comprehensive way to nullify income shifting strategies
- Modernize state tax code to adapt to the growth of multi-state corporations
- Broaden the corporate tax base
- Reduce uncertainty about when corporations need to file combined returns
- Provide a more level playing field

Revenue Laws Recommended

- Mandatory combined reporting
- By affiliated corporations of a unitary business
- In a worldwide combination, with a water's edge election,
- Using the Joyce method of apportionment

[**SB 244 and HB 462**]

- Recommendation needs further development
 - Franchise tax issues
 - Special apportionment formula issues
 - Transitional & administrative issues
- Fiscal impact determination
- Corporate rate determination

[Also Recommended by ...]

- **2001:** Governor's Commission to Modernize State Finances
- **2007:** Income Tax Modernization Subcommittee of the State and Local Fiscal Modernization Commission
- **2007:** Governor Easley recommended combined reporting in his budget proposal

[Combined Reporting in US]

- **Prior to 1980s:** 16 states required combined reporting
- **2004:** VT enacted combined reporting
- **2006:** MTC adopted model combined reporting statute
- **2007-2008:** 5 additional states enacted some form of combined reporting (22)
- **2007-2008:** Considered by several other states

