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STATE OF RHODE ISLAND

IN GENERAL ASSEMBLY

JANUARY SESSION, A.D. 2011

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A N A C T

RELATING TO TAXATION – COMBINED REPORTING

Introduced By: Senator Joshua Miller

Date Introduced: March 10, 2011

Referred To: Senate Finance

It is enacted by the General Assembly as follows:

1 SECTION 1. Title 44 of the General Laws entitled "TAXATION" is hereby amended by  
2 adding thereto the following chapter:

3 CHAPTER 67

4 COMBINED REPORTING

5 **44-67-1. Definitions.** -- As used in this chapter, the following words and terms shall have  
6 the following meanings:

7 (1) "Person" means any individual, firm, partnership, general partner of a partnership,  
8 limited liability company, registered limited liability partnership, foreign limited liability  
9 partnership, association, corporation (whether or not the corporation is, or would be if doing  
10 business in this state, subject to chapter 30 of title 44), company, syndicate, estate, trust, business  
11 trust, trustee, trustee in bankruptcy, receiver, executor, administrator, assignee or organization of  
12 any kind;

13 (2) "Taxpayer" means and includes any corporation subject to the provisions of chapter  
14 44-11;

15 (3) "Corporation" means any corporation as defined by the laws of this state or  
16 organization of any kind treated as a corporation for tax purposes under the laws of this state,  
17 wherever located, which if it were doing business in this state would be a "taxpayer." The  
18 business conducted by a partnership which is directly or indirectly held by a corporation shall be  
19 considered the business of the corporation to the extent of the corporation's distributive share of

1 the partnership income, inclusive of guaranteed payments to the extent prescribed by regulation;

2 (4) “Partnership” means a general or limited partnership, or organization of any kind  
3 treated as a partnership for tax purposes under the laws of this state;

4 (5) “Internal revenue code” means title 26 of the United States code without regard to  
5 application of federal treaties, unless expressly made applicable to states of the United States;

6 (6) “Unitary business” means a single economic enterprise that is made up either of  
7 separate parts of a single business entity or of a commonly controlled group of business entities  
8 that are sufficiently interdependent, integrated and interrelated through their activities so as to  
9 provide a synergy and mutual benefit that produces a sharing or exchange of value among them  
10 and a significant flow of value to the separate parts. Any business conducted by a partnership  
11 shall be treated as conducted by its partners, whether directly held or indirectly held through a  
12 series of partnerships, to the extent of the partner's distributive share of the partnership's income,  
13 regardless of the percentage of the partner's ownership interest or its distributive or any other  
14 share of partnership income. A business conducted directly or indirectly by one corporation is  
15 unitary with that portion of a business conducted by another corporation through its direct or  
16 indirect interest in a partnership if the conditions of the first sentence of this section are satisfied,  
17 to wit; there is a synergy, and exchange and flow of value between the two (2) parts of the  
18 business and the two (2) corporations are members of the same commonly controlled group;

19 (7) “Combined group” means the group of all persons whose income and apportionment  
20 factors are required to be taken into account pursuant to subsection 44-67-2(a) or 44-67-2(b) in  
21 determining the taxpayer’s share of the net business income or loss apportionable to the State of  
22 Rhode Island;

23 (8) “United States” means the fifty (50) states of the United States, the District of  
24 Columbia, and United States’ territories and possessions;

25 (9) “Tax haven” means a jurisdiction that, during the tax year in question:

26 (i) Is identified by the organization for economic co-operation and development (OECD)  
27 as a tax haven or as having a harmful preferential tax regime; or

28 (ii) Exhibits the following characteristics established by the OECD in its 1998 report  
29 entitled “Harmful Tax Competition: An Emerging Global Issue” as indicative of a tax haven or as  
30 a jurisdiction having a harmful preferential tax regime, regardless of whether it is listed by the  
31 OECD as an un-cooperative tax haven:

32 (A) Has a no or nominal effective tax on the relevant income; and

33 (B)(I) Has laws or practices that prevent effective exchange of information for tax  
34 purposes with other governments on taxpayers benefiting from the tax regime;

1 (II) Has a tax regime which lacks transparency. A tax regime lacks transparency if the  
2 details of legislative, legal or administrative provisions are not open and apparent or are not  
3 consistently applied among similarly situated taxpayers, or if the information needed by tax  
4 authorities to determine a taxpayer's correct tax liability, such as accounting records and  
5 underlying documentation, is not adequately available;

6 (III) Facilitates the establishment of foreign-owned entities without the need for a local  
7 substantive presence or prohibits these entities from having any commercial impact on the local  
8 economy;

9 (IV) Explicitly or implicitly excludes the jurisdiction's resident taxpayers from taking  
10 advantage of the tax regime's benefits or prohibits enterprises that benefit from the regime from  
11 operating in the jurisdiction's domestic market; or

12 (V) Has created a tax regime which is favorable for tax avoidance, based upon an overall  
13 assessment of relevant factors, including whether the jurisdiction has a significant untaxed  
14 offshore financial/other services sector relative to its overall economy.

15 **44-67-2. Combined reporting required, when -- Discretionary under certain**  
16 **circumstances. -- (a) A taxpayer engaged in a unitary business with one or more other**  
17 **corporations shall file a combined report which includes the income, determined under subsection**  
18 **44-67-3(c) of this chapter, and apportionment factors, determined under section 44-11-14 through**  
19 **section 44-11-14.6 and subsection 44-67-2(b) of this chapter, of all corporations that are members**  
20 **of the unitary business, and such other information as required by the director;**

21 (b) The director may, by regulation, require the combined report include the income and  
22 associated apportionment factors of any persons that are not included pursuant to subsection 44-  
23 67-2(a), but that are members of a unitary business, in order to reflect proper apportionment of  
24 income of entire unitary businesses. Authority to require combination by regulation under  
25 subsection 44-67-2(b), includes authority to require a combination of persons that are not, or  
26 would not be if doing business in this state, subject to chapter 30 of title 44.

27 In addition, if the director determines that the reported income or loss of a taxpayer  
28 engaged in a unitary business with any person not included pursuant to subsection 44-67-2(a),  
29 represents an avoidance or evasion of tax by such taxpayer, the director may, on a case by case  
30 basis, require all or any part of the income and associated apportionment factors of such person  
31 be included in the taxpayer's combined report.

32 With respect to inclusion of associated apportionment factors pursuant to subsection 44-  
33 67-2(b), the director may require the exclusion of any one or more of the factors, the inclusion of  
34 one or more additional factors which will fairly represent the taxpayer's business activity in this

1 state, or the employment of any other method to effectuate a proper reflection of the total amount  
2 of income subject to apportionment and an equitable allocation and apportionment of the  
3 taxpayer's income.

4 **44-67-3. Determination of taxable income or loss using combined report.** – The use  
5 of a combined report does not disregard the separate identities of the taxpayer members of the  
6 combined group. Each taxpayer member is responsible for tax based on its taxable income or loss  
7 apportioned or allocated to this state, which shall include, in addition to other types of income,  
8 the taxpayer member's apportioned share of business income of the combined group, where  
9 business income of the combined group is calculated as a summation of the individual net  
10 business incomes of all members of the combined group. A member's net business income is  
11 determined by removing all but business income, expense and loss from that member's total  
12 income, as provided in detail below:

13 (A) Components of income subject to tax in this state; application of tax credits and post  
14 apportionment deductions:

15 (i) Each taxpayer member is responsible for tax based on its taxable income or loss  
16 apportioned or allocated to this state, which shall include:

17 (a) Its share of any business income apportionable to this state of each of the combined  
18 groups of which it is a member, determined under subsection 44-67-3(b);

19 (b) Its share of any business income apportionable to this state of a distinct business  
20 activity conducted within and without the state wholly by the taxpayer member, determined  
21 under section 44-11-14 through section 44-11-14.6;

22 (c) Its income from a business conducted wholly by the taxpayer member entirely within  
23 the state;

24 (d) Its income sourced to this state from the sale or exchange of capital or assets, and  
25 from involuntary conversions, as determined under subparagraph 44-67-3(c)(ii)(G), below;

26 (e) Its income or loss allocated or apportioned in an earlier year, required to be taken into  
27 account as state source income during the income year, other than a net operating loss; and

28 (f) If the taxable income computed pursuant to section 44-67-3 results in a loss for a  
29 taxpayer member of the combined group, that taxpayer member has a state net operating loss  
30 (NOL), subject to the net operating loss limitations, and carryforward provisions of section 44-  
31 11-11. Such NOL is applied as a deduction in a prior or subsequent year only if that taxpayer has  
32 state source positive net income, whether or not the taxpayer is or was a member of a combined  
33 reporting group in the prior or subsequent year.

34 (ii) Except where otherwise provided, no tax credit or post-apportionment deduction

1 earned by one member of the group, but not fully used by or allowed to that member, may be  
2 used in whole or in part by another member of the group or applied in whole or in part against the  
3 total income of the combined group; and a post-apportionment deduction carried over into a  
4 subsequent year as to the member that incurred it, and available as a deduction to that member in  
5 a subsequent year, will be considered in the computation of the income of that member in the  
6 subsequent year, regardless of the composition of that income as apportioned, allocated or wholly  
7 within the state.

8 (B) Determination of taxpayer's share of the business income of a combined group  
9 apportionable to this state.

10 The taxpayer's share of the business income apportionable to this state of each combined  
11 group of which it is a member shall be the product of:

12 (i) The business income of the combined group, determined under such subsection  
13 section 44-67-3(c); and

14 (ii) The taxpayer member's apportionment percentage, determined by the provisions of  
15 section 44-11-11 through section 44-11-14.6, including in the property, payroll, and sales factor  
16 numerators the taxpayer's property, payroll and sales, respectively associated with the combined  
17 group's unitary business in this state, and including in the denominator the property, payroll and  
18 sales of all members of the combined group, including the taxpayer, which property, payroll and  
19 sales are associated with the combined group's unitary business wherever located. The property,  
20 payroll and sales of a partnership shall be included in the determination of the partner's  
21 apportionment percentage in proportion to a ratio the numerator of which is the amount of the  
22 partner's distributive share of partnership's unitary income included in the income of the  
23 combined group in accordance with subparagraph 44-67-(3)(ii)(c) and the denominator of which  
24 is the amount of the partnership's total unitary income.

25 (C) Determination of the business income of the combined group.

26 The business income of combined group is determined as follows:

27 (i) From the total income of the combined group determined under subdivision 44-67-  
28 3(c)(ii), subtract any income, and add any expense or loss, other than the business income,  
29 expense or loss of the combined group;

30 (ii) Except as otherwise provided, the total income of the combined group is the sum of  
31 the income of each member of the combined group determined under federal income tax laws, as  
32 adjusted for state purposes, as if the member were not consolidated for federal purposes. The  
33 income of each member of the combined group shall be determined as follows:

34 (a) For any member incorporated in the United States, or included in a consolidated

1 federal corporate income tax return, the income to be included in the total income of the  
2 combined group shall be the taxable income for the corporation after making appropriate  
3 adjustments under the provisions of section 44-11-11.

4 (b)(1) For any member not included in subdivision 44-67-3(ii)(a), the income to be  
5 included in the total income of the combined group shall be determined as follows:

6 (A) A profit and loss statement shall be prepared for each foreign branch or corporation  
7 in the currency in which the books of account of the branch or corporation are regularly  
8 maintained.

9 (B) Adjustment shall be made to the profit and loss statement to conform it to the  
10 accounting principles generally accepted in the United States for the preparation of such  
11 statements except as modified by this chapter.

12 (C) Adjustments shall be made to the profit and loss statement to conform it to the tax  
13 accounting standards required by the state tax laws.

14 (D) Except as otherwise provided by regulation, the profit and loss statement of each  
15 member of the combined group, and the apportionment factors related thereto, whether United  
16 States or foreign, shall be translated into the currency in which the parent company maintains its  
17 books and records.

18 (E) Income apportioned to this state shall be expressed in United States dollars.

19 (2) In lieu of the procedures set forth in subparagraph 44-67-(ii)(b)(1), above, and subject  
20 to the determination of the director that reasonably approximates income as determined under the  
21 state tax laws, any member not included in subparagraph 44-67-(C)(ii)(a) may determine its  
22 income on the basis of the consolidated profit and loss statement which includes the member and  
23 which is prepared for filing with the securities and exchange commission by related corporations.  
24 If the member is not required to file with the securities and exchange commission, the director  
25 may allow the use of the consolidated profit and loss statement prepared for reporting to  
26 shareholders and subject to review by an independent auditor. If above statements do not  
27 reasonably approximate income as determined under the state tax laws the director may accept  
28 those statements with appropriate adjustments to approximate that income.

29 (c) If a unitary business includes income from a partnership, the income to be included in  
30 the total income of the combined group shall be the member of the combined group's direct and  
31 indirect distributive share of the partnership's unitary business income.

32 (d) All dividends paid by one to another of the members of the combined group shall, to  
33 the extent those dividends are paid out of the earnings and profits of the unitary business included  
34 in the combined report, in the current or an earlier year, be eliminated from the income of the

1 recipient. This provision shall not apply to dividends received from members of the unitary  
2 business which are not a part of the combined group.

3 (e) Except as otherwise provided by regulation, business income from an intercompany  
4 transaction between members of the same combined group shall be deferred in a manner similar  
5 to 26 CFR 1.1502-13. Upon the occurrence of any of the following events, deferred business  
6 income resulting from an intercompany transaction between members of a combined group shall  
7 be restored to the income of the seller, and shall be apportioned as business income earned  
8 immediately before the event:

9 (1) The object of a deferred intercompany transaction is:

10 (A) Re-sold by the buyer to an entity that is not a member of the combined group;

11 (B) Re-sold by the buyer to an entity that is a member of the combined group for use;  
12 outside the unitary business in which the buyer and seller are engaged; or

13 (C) Converted by the buyer to a use outside the unitary business in which the buyer and  
14 seller are engaged; or

15 (2) The buyer and seller are no longer members of the same combined group, regardless  
16 of whether the members remain unitary.

17 (f) A charitable expense incurred by a member of a combined group shall, to the extent  
18 allowable as a deduction pursuant to Internal Revenue Code Section 170, be subtracted first from  
19 the business income of the combined group (subject to the income limitations of that section  
20 applied to the entire business income of the group), and any remaining amount shall then be  
21 treated as a nonbusiness expense allocable to the member that incurred the expense (subject to the  
22 income limitations of that section applied to the nonbusiness income of that specific member).  
23 Any charitable deduction disallowed under the foregoing rule, but allowed as a carryover  
24 deduction in a subsequent year, shall be treated as originally incurred in the subsequent year by  
25 the same member, and the rules of this section shall apply in the subsequent year in determining  
26 the allowable deduction in that year.

27 (g) Gain or loss from the sale or exchange of capital assets, property described by Internal  
28 Revenue Code Section 1231(a)(3), and property subject to an involuntary conversion, shall be  
29 removed from the total separate net income of each member of a combined group and shall be  
30 apportioned and allocated as follows:

31 (1) For each class of gain or loss (short term capital, long term capital, Internal Revenue  
32 Code Section 1231, and involuntary conversions) all members' business gain and loss for the  
33 class shall be combined (without netting between such classes), and each class of net business  
34 gain or loss separately apportioned to each member using the member's apportionment

1 percentage determined under section 44-67-3(B) above.

2 (2) Each taxpayer member shall then net its apportioned business gain or loss for all  
3 classes, including any such apportioned business gain and loss from other combined groups,  
4 against the taxpayer member's nonbusiness gain and loss for all classes allocated to this state,  
5 using the rules of Internal Revenue Code Sections 1231 and 1222, without regard to any of the  
6 taxpayers member's gains or losses from the sale or exchange of capital assets, Section 1231  
7 property, and involuntary conversions which are nonbusiness items allocated to another state.

8 (3) Any resulting state source income (or loss, if the loss is not subject to the limitations  
9 of Internal Revenue Code Section 1211) of a taxpayer member produced by the application of the  
10 preceding subsections shall then apply to all other state source income or loss of that member.

11 (4) Any resulting state source loss of a member that is subject to the limitations of  
12 Section 1211 shall be carried forward by that member, and shall be treated as state source short-  
13 term capital loss incurred by that member for the year for which the carryover applies.

14 (h) Any expense of one member of the unitary group which is directly or indirectly  
15 attributable to the nonbusiness or exempt income of another member of the unitary group shall be  
16 allocated to that other member as corresponding nonbusiness or exempt expense, as appropriate.

17 **44-67-4. Designation of surety.** – As a filing convenience, and without changing the  
18 respective liability of the group members, members of a combined reporting group may annually  
19 elect to designate one taxpayer member of the combined group to file a single return in the form  
20 and manner prescribed by the department, in lieu of filing their own respective returns, provided  
21 that the taxpayer designated to file the single return consents to act as surety with respect to the  
22 tax liability of all other taxpayers properly include in the combined report, and agrees to act as  
23 agent on behalf of those taxpayers for the year of the election for tax matters relating to the  
24 combined report for that year. If for any reason the surety is unwilling or unable to perform its  
25 responsibilities, tax liability may be assessed against the taxpayer members.

26 **44-67-5. Water's-edge election; initiation and withdrawal.** – (A) Water's-edge  
27 election. Taxpayer members of a unitary group that meet the requirements of section 44-67-5(B)  
28 may elect to determine each of their apportioned shares of the net business income of loss of the  
29 combined group pursuant to a water's-edge election. Under such election, taxpayer members shall  
30 take into account all or a portion of the income and apportionment factors of only the following  
31 members otherwise included in the combined group pursuant to section 44-67-2, as described  
32 below:

33 (i) The entire income and apportionment factors of any member incorporated in the  
34 United States or formed under the laws of any state, the District of Columbia, or any territory or



1 possession of the United States;

2 (ii) The entire income and apportionment factors of any member, regardless of the place  
3 incorporated or formed, if the average of its property, payroll, and sales factors within the United  
4 States is twenty percent (20%) or more;

5 (iii) The entire income and apportionment factors of any member which is a domestic  
6 international sales corporation as described in Internal Revenue Code Sections 991 to 994,  
7 inclusive; a foreign sales corporation as described in Internal Revenue Code sections 921-927,  
8 inclusive; or any member which is an export trade corporation, as described in Internal Revenue  
9 Code Sections 970 to 971, inclusive;

10 (iv) Any member not described in Section 44-67-5(A)(i) to Section 44-67-5(A)(iii),  
11 inclusive shall include the portion of its income derived from or attributable to sources within the  
12 United States, as determined under the Internal Revenue Code without regard to federal treaties,  
13 and its apportionment factors related thereto:

14 (v) Any member that is a “controlled foreign corporation,” as defined in Internal Revenue  
15 Code Section 957, to the extent of the income of that member that is defined in Section 952 of  
16 Subpart F of the Internal Revenue Code (“Subpart F income”) not excluding lower-tier  
17 subsidiaries’ distributions of such income which were previously taxed, determined without  
18 regard to federal treaties, and the apportionment factors related to that income; any item of  
19 income received by a controlled foreign corporation shall be excluded if such income was subject  
20 to an effective rate of income tax imposed by a foreign country greater than ninety percent (90%)  
21 of the maximum rate of tax specified in Internal Revenue Code Section 11;

22 (vi) Any member that earns more than twenty percent (20%) of its income, directly or  
23 indirectly, from intangible property or service related activities that are deductible against the  
24 business income of other members of the combined group, to the extent of that income and the  
25 apportionment factors related thereto; and

26 (vii) The entire income and apportionment factors of any member that is doing business  
27 in a tax haven, where “doing business in a tax haven” is defined as being engaged in activity  
28 sufficient for the tax haven jurisdiction to impose a tax under United States constitutional  
29 standards. If the member’s business activity within a tax haven is entirely outside the scope of the  
30 laws, provisions and practices that cause the jurisdiction to meet the criteria established in Section  
31 (1)(I), the activity of the member shall be treated as not having been conducted in a tax haven.

32 (B) Initiation and withdrawal of election.

33 (i) A water’s-edge election is effective only if made on a timely-filed, original return for a  
34 tax year by every member of the unitary business subject to tax under the state income tax code.

1 The director shall develop rules and regulations governing the impact, if any, on the scope or  
2 application of a water's-edge election, including termination or deemed election, resulting from a  
3 change in the composition of the unitary group, the combined group, the taxpayer members, and  
4 any other similar change.

5 (ii) Such election shall constitute consent to the reasonable production of documents and  
6 taking of depositions in accordance with the state statute on discovery.

7 (iii) In the discretion of the director, a water's-edge election may be disregarded in part or  
8 in whole, and the income and apportionment factors of any member of the taxpayer's unitary  
9 group may be included in the combined report without regard to the provisions of this section, if  
10 any member of the unitary group fails to comply with any provision of this act or if a person  
11 otherwise not included in the water's-edge combined group was availed of with a substantial  
12 objective of avoiding state income tax.

13 (iv) A water's-edge election is binding for and applicable to the tax year it is made and all  
14 tax years thereafter for a period ten (10) years. It may be withdrawn or reinstated after  
15 withdrawal, prior to the expiration of the ten (10) year period, only upon written request for  
16 reasonable cause based on extraordinary hardship due to unforeseen changes in state tax statutes,  
17 law, or policy, and only with the written permission of the director. If the director grants a  
18 withdrawal of election, he or she shall impose reasonable conditions as necessary to prevent the  
19 evasion of tax or to clearly reflect income for the election period prior to or after the withdrawal.  
20 Upon the expiration of the ten (10) year period, a taxpayer may withdraw from the water's-edge  
21 election. Such withdrawal must be made in writing within one year of the expiration of the  
22 election, and is binding for a period of ten (10) years, subject to the same conditions as applied to  
23 the original election. If no withdrawal is properly made, the water's-edge election shall be in  
24 place for an additional ten (10) year period, subject to the same conditions as applied to the  
25 original election.

26 SECTION 2. This act shall take effect upon passage.

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EXPLANATION  
BY THE LEGISLATIVE COUNCIL  
OF  
A N A C T  
RELATING TO TAXATION – COMBINED REPORTING

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- 1           This act would address the factors required to be taken into account in determining the
- 2 taxpayers share of the net business income or loss apportionable to the State of Rhode Island.
- 3           This act would take effect upon passage.

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