Rule on Unitary Combined Reporting
~~Reg. § 1.5862(d) UNITARY COMBINED REPORTING~~

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~~Reg. § 1.5862(d)~~ UNITARY COMBINED REPORTING

~~Reg. § 1.5862(d) -~~Section 1. Effective Date

This Rule ~~These Regulations~~ shall be effective on____ ~~for tax years beginning on and after January 1, 2006.~~

~~Reg. § 1.5862(d) –~~ Section 2. Authorization and Purpose

(a) This rule is authorized by 32 V.S.A. § 3201(a)(1), Act 152 of 2003, and Act 148 of 2022, Section 6.

(b) The purpose of this rule is to establish standards for determining the Vermont income tax of unitary businesses and for filing the group return and related schedules required under 32 V.S.A. § 5862(d) ~~and related schedules~~.

~~Reg. § 1.5862(d) –~~ Section 3. Vermont Net Income

The Vermont corporate tax is imposed on that portion of a corporation's Vermont net income that is allocated or apportioned to Vermont under 32 V.S.A. § 5833 and the Allocation and Apportionment of Vermont Net Income by Corporations Rule.~~Reg. §1.5833.~~ The Vermont net income (income prior to state allocation or apportionment) of a taxable corporation that is a member of an affiliated group and that is engaged in a unitary business with one or more members of the affiliated group includes its allocable share of the combined net unitary ~~business~~ income of the group. A taxable corporation's Vermont net income also includes its non-~~business~~ apportionable income, its income from any non-unitary business, and its apportioned share of net business income from any other unitary business conducted with affiliates.

~~Reg. § 1.5862(d) –~~ Section 4. Composition of the Affiliated Group

(a) *Definition.* An affiliated group is a group of two or more corporations in which more than 50 percent of the voting stock of each member corporation is directly or indirectly owned by a common owner or owners, either corporate or noncorporate, or by one or more of the member corporations. An owner is any person as defined in 32 V.S.A. § 5811(20).

(b) *Excluded corporations.* An affiliated group shall exclude:

~~(1) overseas business organizations; and~~

~~(2)~~ (1) C~~c~~orporations taxable under section 6014 of title 8 of the Vermont Statutes Annotated; and captive insurance corporations domiciled outside Vermont whose activities do not exceed those permitted under chapter 141 of title 8; and

~~(3)~~ (2) S corporations;

~~(4)~~ (3) Corporations that are not taxable under the Internal Revenue Code.

Except as enumerated above, a corporation that is not subject to Vermont corporate income tax is not excluded from the affiliated group. For example, banks, insurance companies, telephone companies electing to pay gross receipts tax, and railroad companies, are part of the affiliated group notwithstanding that the income allocated to them is not subject to Vermont corporate income tax.

Ex. 1) Office Co. owns 100% of Insurance Co as a subsidiary. Insurance Co. pays the Vermont insurance premium tax on premiums collected in Vermont. The net income of Insurance Co. must be included in the combined report. The factors generated by Insurance Co. are not included in the apportionment numerator as per Section 8 of this rule.

Pass-through entities, including partnerships, limited liability companies taxed as partnerships under federal law, and S corporations are not themselves members of the affiliated group. However, a pro rata share of such entity's income and sales~~, payroll and property~~ is assigned to the unitary group member that holds an ownership interest in such pass-through entity.

Ex. 2) Same facts as Example 1, but Office Co. enters into an agreement to purchase a 30% interest in Partnership P. The partnership agreement provides that Office Co.'s income distribution from P is also 30%. P is used as Office Co. and Insurance Co.'s main supplier of paper.

P engages in unitary activities with the affiliated group. Office Co. is imputed to have engaged in the activities of P. The pro rata net income of P must be included in the combined report as well as the net income of Insurance Co. The pro rata share of apportionment factors of P should be included in Office Co.'s data according to the percentage of income distributed.

(c) *Fifty percent test.* The fifty percent ownership test is satisfied in the following circumstances:

(1) A parent corporation and one or more corporations or chains of corporations which are connected through voting stock ownership with the parent, whether such ownership is direct or indirect, but only if --

(A) the parent owns more than 50 percent of the outstanding voting stock of at least one corporation, and, if applicable,

(B) more than 50 percent of the outstanding voting stock of each of the corporations, other than the parent, is owned by the parent, one or more corporations owned by the parent as described in subparagraph (A) above, or one or more corporations that satisfy the conditions of this subparagraph.

(2) Any two or more corporations, if over 50 percent of the outstanding voting stock of each of the corporations is owned, or indirectly owned, by the same person.

(3) Any two or more corporations, over 50 percent of whose voting stock is cumulatively owned (without regard to the indirect ownership rules described below in paragraph (d)(1)) by, or for the benefit of, members of the same family. Members of the same family are limited to an individual, his or her spouse, parents, brothers or sisters, grandparents, children and grandchildren, and their respective spouses.

(d) Except as otherwise provided, voting stock is "owned" when title to the stock is directly held or if the voting stock is indirectly owned.

(1) An individual indirectly owns voting stock that is owned by any of the following:

(A) his or her spouse (other than a spouse who is legally separated from the individual);

(B) his or her children, grandchildren, and parents;

(C) an estate or trust, of which the individual is an executor, trustee, or grantor, to the extent that the estate or trust is for the benefit of that individual's spouse, children, grandchildren or parents.

(2) voting stock owned by a partnership, other than a limited partnership, is indirectly owned by a partner in proportion to the partner's capital interest in the partnership. For this purpose, a partnership other than a limited partnership is treated as owning proportionately the stock owned by any other partnership or limited partnership in which it has a tiered interest. Voting stock owned by a limited partnership is indirectly owned by the general partner who has authority to determine how the stock is voted.

(3) voting stock owned by a corporation, or a member of a controlled group of which the corporation is the parent corporation, is indirectly owned by any shareholder owning over 50 percent of the voting stock of the corporation.

(e) In determining ownership, effective control over election of the board of directors will be considered. For example, a group of shareholders acting in concert who collectively own over 50 percent of the voting stock of each of two or more corporations will be considered to be common owners of more than 50 percent of the voting stock of each of those corporations. “Voting stock” refers only to those shares of voting stock having the power to elect the corporation’s board of directors. If the power otherwise held in corporate stock to vote the membership of the board is transferred to another, other than a transfer of proxy only, the holder of that power will be considered to be the owner of that stock to the exclusion of the transferor of such power.

(f) In addition to the tests in paragraph(c), the commissioner may consider any other circumstance that tends to demonstrate that the 50 percent direct or indirect common ownership test was met or was not met.

(g) Membership in an affiliated group shall be treated as terminated in any year, or fraction thereof, in which the conditions of paragraph (c) are not met, except as follows:

> (1) when stock of a corporation is sold, exchanged, or otherwise disposed of, the membership of a corporation in an affiliated group shall not be terminated if the requirements of paragraph (c) are again met immediately after the sale, exchange, or disposition.
>
> (2) the Commissioner may treat the affiliated group as remaining in place if the conditions of paragraph (c) are again met within a period not to exceed two years.

~~Reg. § 1.5862(d) - 5 Overseas Business Organizations~~

~~(a) *Definition.* An overseas business organization is a business entity that ordinarily has 80% or more of its payroll and property located outside the United States. This definition of affiliated group adopts what is commonly referred to as a “water’s edge” group as opposed to a “worldwide combined” group. If a corporation meets the ownership test and is not excluded as an overseas business organization, an S corporation or a captive insurance company, as described in Reg. § 1.5862(d) - 4(b), it is part of the affiliated group.~~

~~(b) *Calculation.* The amount of property and payroll is determined in accordance with Reg. §1.5833 (allocation and apportionment). To qualify as an overseas business organization, the entity must meet the following tests:~~

> ~~(1) in two out of the three most recent tax years, including the current tax year, at least 80 percent of the average of the payroll and property was located outside of the fifty United States and the District of Columbia (referred to herein as “US”), calculated for each year as follows:~~

~~$\left[\frac{\text{outside US payroll}}{\text{total payroll}} + \frac{\text{outside US property}}{\text{total property}}\right] \div 2$~~

~~(2) at least 70 percent of the payroll and property in the current tax year is located outside the US, calculated as above.~~

~~If the organization has been in existence for less than three years, the average of two years of payroll and property will determine whether it qualifies as an overseas business organization. If the organization has been in business for less than two years, it is not an overseas business organization unless more than 80 percent of its payroll and property for the year was located outside the US.~~

~~Reg. § 1.5862(d) - 6~~ Section 5 Unitary Business

(a) *Definition.* Unitary business means one or more related business organizations ~~doing business both within and without the State~~ where there is a unity of ownership, operation and use when one organization does business within the State. It can also exist where there is interdependence in their functions. A determination under this rule ~~regulation~~ of whether an entity forms part of a unitary business with another is determined based on the facts and circumstances of each case. To the extent compatible with Vermont law, any legal or factual determination relevant to the existence or nonexistence of a unitary business will favor consistency with legal and factual determinations of other unitary states. A unitary business includes that part of the business that meets the definition in this Section 5(a) and is conducted by a taxpayer through the taxpayer's interest in a partnership, whether the interest in that partnership is held directly or indirectly through a series of partnerships or other pass-through entities.

(b) *Interdependence of functions test*. One or more related business organizations engaged in business activity both within and without the state are unitary if there exists interdependence in their functions. This test adopts the decisional law of the United States Supreme Court with respect to the constitutional prerequisites for requiring unitary combination. The Court has variously expressed the constitutional test, holding that a finding of unitary relationship requires "contribution or dependency" between businesses; "substantial mutual interdependency" or "flow of value"; functional integration, centralized management and economy of scale. *See, e.g., Edson California Stores*, *Container Corporation of America v. Franchise Tax Board, 463 U.S. 159 (1983)*, *Mobil Oil Corp. v. Commissioner of Taxes, 445 U.S. 425 (1980).* These concepts collectively express the Court's view of the constitutional parameters of required combination. Vermont's "interdependence of functions test" extends as far as, but no further than, the constitutional limits found by the Court.

(c) The following circumstances, together with those identified below in subdivision (d), indicate that an interdependence of functions exists:

(1) Same Line of Business. The principal activities of the entities are in the same general line of business. Examples of the same line of business are

manufacturing, wholesaling, and retailing of tangible personal property; insurance; transportation or finance.

(A) In determining whether two entities are in the same general line of business, consideration shall be given to the nature and character of the basic operations of each entity, including, but not limited to, sources of supply, goods or services produced or sold labor force and market.

(B) Two entities are in the same general line of business when their operations are sufficiently similar to reasonably conclude that the entities are likely to depend upon or contribute to one another.

(2) Vertically Structured Business. The principal activities of the entities are different steps of a vertically structured business. Illustrations of such different steps are exploration, mining and drilling, production, refining, marketing, and transportation of natural resources.

(3) Strong Centralized Management. Centralized management may be evidenced by executive level policy made by a central person, board or committee and not by each entity in areas such as, but not limited to, purchasing, accounting, finance, tax compliance, legal services, human resources, health and retirement plans, product lines, capital investment and marketing.

(4) Newly Acquired Corporations. When a corporation acquires another corporation, a presumption exists against a finding of a unitary relationship during the first reporting period. Any party may rebut such presumption by proving that the corporations were unitary. If such presumption is rebutted, then the corporations shall be considered unitary as of the date of acquisition, unless the evidence shows that unity was established as of another date.

(5) Newly-Formed Corporations. When a corporation forms another corporation, a presumption exists in favor of finding unity between the two corporations as of the date of formation. Any party may rebut such presumption by proving that the corporations are not unitary or became unitary at a later date.

(6) Non-Arm's-Length Prices. Goods or services or both are supplied at non-arm's length prices between or among entities. Existence of arm's-length pricing between entities, however, does not indicate lack of unity.

(7) Existence of Benefits from Joint, Shared or Common Activity. A discount, cost-saving or other benefit can be shown to result from joint purchases, leaseholds, or other forms of joint, shared or common activities between or among entities.

(8) Relationship of Joint, Shared or Common Activity to Income-Producing Operations. In determining whether or not the fact that there exists a

joint, shared, or common activity is indicative of a unitary relationship, consideration shall be given to the nature and character of the basic operations of each entity. Such consideration shall include, but not be limited to, the entity's sources of supply, its goods or services produced or sold, its labor force and market to determine whether the joint, shared or common activity is directly beneficial to, related to or reasonably necessary to the income-producing activities of the unitary business.

(9) Exercise of Control. The exercise of control by one entity over another entity.

(d) The "three unities test". This test adopts the state law test for unity followed in *Butler Brothers* v. McColgan, 315 U.S. 501 (1942).

(1) *Unity of ownership*. "Unity of ownership" exists with respect to corporations when the fifty percent ownership test is met. ~~Refer to Reg. § 5862(d) – 4 (c).~~ See Section 4.

(2) *Unity of operations and unity of use*. These unities exist if each entity that is to be included in the unitary business benefits or receives goods, services, support, guidance or direction arising from the actions of common staff resources or common executive resources, personnel, third-party providers, or operations under the direction of such common resources. The tests are overlapping and the indicators of each test also indicate the existence of interdependence of functions. The existence or non-existence of the following factors will assist in the determination of whether unity of operations and use exist with respect to an affiliated group. The existence or non-existence of any one factor, by itself, is normally not determinative of whether there is a unity of operations and use. Nor is this list a limitation on the factors that may be considered in determining this:

(1) Common purchasing;

(2) Common advertising;

(3) Common employees, including sales force;

(4) Common accounting;

(5) Common legal support;

(6) Common retirement plan;

(7) Common insurance coverage;

(8) Common marketing;

(9) Common cash management;

(10) Common research and development;

(11) Common offices;

(12) Common manufacturing facilities;

(13) Common warehousing facilities;

(14) Common transportation facilities;

(15) Common computer systems and support;

(16) Financing support;

(17) Common management, meaning that one or more officers or directors of the parent are also officers or directors of the subsidiary;

(18) Control of major policies, for example, the parent's board of directors requires that it approve any acquisition by either the parent or subsidiary of any interest in any other company, or the parent's board of directors requires that it approve any lending in excess of a minimum set amount to any one or more of either the parent or subsidiary's suppliers;

(19) Inter-entity transactions, for example, the subsidiary has licensed to parent the use of personal property developed by the subsidiary. The parent uses the property for its production;

(20) Common policy or training manuals, for example, the parent's employee handbook has been expanded to apply to all of a subsidiary's employees, or the subsidiary's employees are required to attend parent's employee training courses, or disciplinary procedures are the same for both the parent and subsidiary's employees, even if the appeal is only through their respective entities;

(21) Required budgetary approval, for example, the parent's board of directors requires that it approve the budget and expenditure plans of the subsidiary on an annual basis; and

(22) Required capital asset purchases approval, for example, the parent's board of directors requires that it approve any capital expenditures by the subsidiary in excess of a minimum set amount.

(e) Holding Companies. The test for a unitary business established by this rule applies in determining whether a holding company is included or excluded from a unitary

business. If a holding company is organizationally between two unitary entities, such holding company does not negate unity of ownership.

~~Reg. § 1.5862(d) –~~ <u>Section</u> 7 Combined Net Income of the Group

(a) *Definition.* In this <u>rule</u> ~~regulation~~, "group" refers to the collective members of an affiliated group that are engaged in a unitary business and <u>one or more members are</u> doing business in Vermont.

(b) *Determination of taxable income or loss of the group using a group return.* The use of a group return does not disregard the separate identities of the taxpayer members of the group. Each taxpayer member is responsible for tax based on its taxable income or loss apportioned to this state, which shall include, among other items of income, the taxpayer member's apportioned share of business income of the combined group, where business income of the combined group is determined by subtracting all but business income, expense and loss from the total income of the combined group, as provided below.

(c) *Components of income subject to tax in this state.* Each taxpayer member is responsible for tax based on its taxable income or loss apportioned or allocated to this state, which shall include:

(1) its share of any business income apportionable to this state of each of the combined groups of which it is a member;

(2) its share of any business income apportionable to this state of a distinct business activity conducted within and without the state wholly owned by the taxpayer member;

(3) its income from a business conducted wholly by the taxpayer member entirely within this state;

(4) its income sourced to this state from the sale or exchange of capital or assets, and from voluntary conversions;

(5) its nonbusiness income or loss allocable to this state; and

(6) its income or loss allocated or apportioned in an earlier taxable year, required to be taken into account as state source income during the taxable year, other than a net operating loss.

(d) *Determination of taxpayer's share of the business income of a combined group apportionable to this state.* The taxpayer's share of the business income apportionable to Vermont of each combined group of which it is a member shall be the product of:

(1) the business income of the combined group, determined under this <u>rule</u> ~~regulation~~, and

(2) the taxpayer member's apportionment percentage, ~~determined under Reg. § 1.5833~~, including in the numerator the taxpayer's ~~property, payroll and~~ sales associated with the combined group's unitary business in Vermont, and including in the denominator the ~~property, payroll and~~ sales of all members of the combined group, including the taxpayer, which ~~property, payroll and~~ sales are associated with the combined group's unitary business wherever located. The ~~property, payroll and~~ sales of a partnership shall be included in the determination of the partner's apportionment percentage in proportion to a ratio the numerator of which is the amount of the partner's distributive share of the partnership's unitary income included in the income of the combined group in accordance with (e)(3).

(e) *Determination of the business income of the combined group.* The business income of a combined group is determined as follows:

(1) From the total income of the combined group, subtract any income, and add any expense or loss, other than the business income, expense or loss of the combined group.

(2) Except as otherwise provided, the total income of the combined group is the sum of the incomes, separately determined, of each member of the combined group, eliminating items of income, expense, gain and loss from transactions between members of the combined group, applying the consolidated filing rules under the Internal Revenue Code and agency rules as if the combined group was a consolidated filing group. The income of each member of the combined group shall be determined as follows:

(A) For any member incorporated in the United States, or included in a consolidated federal corporate income tax return, the income to be included in the total income of the combined group shall be the taxable income for the corporation after making appropriate adjustments under 32 V.S.A. § 5811(18).

(B)(i) For any member not incorporated in the United States, or included in a consolidated federal corporate income tax return, the income to be included in the total income of the combined group shall be determined from a profit and loss statement prepared for each foreign branch or corporation in the currency in which its books of account are regularly maintained, adjustment to conform it to accounting principles generally accepted in the United States. The profit and loss statement of each member of the combined group , and the apportionment factors related thereto, whether United States or foreign, shall be translated into the currency in which the parent company maintains its books and records. Income apportioned to Vermont shall be expressed in United States dollars.

(ii) In lieu of the procedures set forth in (B)(i) above, and subject to the determination of the commissioner that it reasonably approximates income as determined under Title 32, any member not included in subsection (e)(2)(A) may determine its income on the basis of the consolidated profit and loss statement which includes the member and which is prepared for filing with the Security and Exchange Commission by related corporations. If the member is not required to file with the Security and Exchange Commission, the commissioner may allow the use of the consolidated profit and loss statement prepared for reporting to shareholders and subject to review by an independent auditor. If the above statements do not reasonably approximate income as determined under Title 32, the commissioner may accept those statements with appropriate adjustments to approximate that income.

(C) Any state tax credit shall not be combined and each state tax credit shall be limited to the member to which the credit is attributed.

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

(4) All dividends paid by one to another of the members of the combined group shall, to the extent those dividends are paid out of the earnings and profits of the unitary business included in the combined report, in the current or an earlier year, be eliminated from the income of the recipient. This provision shall not apply to dividends received from members of the unitary business which are not a part of the combined group.

(5) Income from an inter-company transaction between members of the same combined group shall be deferred in a manner similar to 26 CFR 1.1502-13. Upon the occurrence of any of the following events, deferred income resulting from an inter-company transaction between members of a combined group shall be restored to the income of the seller, and shall be apportioned as business income earned immediately before the event:

(A) the object of a deferred inter-company transaction is
(i) re-sold by the buyer to an entity that is not a member of the combined group,
(ii) re-sold by the buyer to an entity that is a member of the combined group for use outside the unitary business in which the buyer and seller are engaged, or
(iii) converted by the buyer to a use outside the unitary business in which the buyer and seller are engaged, or

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

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

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

(A) For each class of gain or loss (short term capital, long term capital, Internal Revenue Code Section 1231, and involuntary conversions) all members' business gain and loss for the class shall be combined (without netting between such classes), and each class of net business gain or loss separately apportioned to each member using the member's apportionment percentage determined under (d) above.

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

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

(D) Any resulting state source loss of a member that is subject to the limitations of Section 1211 shall be carried forward or carried back by

that member, and shall be treated as state source short-term capital loss incurred by that member for the year for which the carryover or carryback applies.

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

(f) *Dividends.* The combined net income of the affiliated group does not include dividends received from corporations that are included in the affiliated group that is operating as a unitary business. Dividends received from overseas business organizations are included in combined net income to the extent that the dividends are included as income of the recipient under the Internal Revenue Code. Income required to be reported by the parent by I.R.C. §§ 951-964 (Subpart F) is included in the Vermont net income of the group to the extent that Subpart F income is included as income of the recipient under the Internal Revenue Code.

(g) *Taxable year of the affiliated group.*

(1) The group's taxable year is determined as follows: (1) if two 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; (2) in all other cases, the taxable year is the taxable year of the principal Vermont corporation. See § 1.5862(d) -10(a) below for the definition of "principal Vermont corporation".

(2) *Members with different accounting periods*. If the taxable year of a member differs from the taxable year of the group, the principal Vermont corporation may elect to determine the portion of that member's income to be included in one of the following ways:

(A) a separate income statement prepared from the books and records for the months included in the group's taxable year; or

(B) including all of the income for the year that ends during the group's taxable year.

The same method must be used for each member with a different accounting period. Once an election is made under this section, it is the only method that may be used with respect to members of the group except upon prior approval by the commissioner.

~~Reg. § 1.5862(d)~~ Section 8 Apportionment

(a) *General rule*. The combined income of the group, ~~excluding the dividends from affiliated overseas business organizations~~ is apportioned in accordance with the

Allocation and Apportionment of Vermont Net Income by Corporations Rule. ~~Reg. § 1.5833~~. Factors of ~~corporations not doing business in Vermont and factors of~~ a corporation subject to a Vermont tax other than corporate income tax are not included in the Vermont numerator. ~~For example, sales shipped into Vermont by members of the group that are not taxable in Vermont are included in the denominator (everywhere sales), but not in the numerator (Vermont sales) of the sales factor. Sales from Vermont into a state in which the corporation is not taxable are included in the Vermont numerator pursuant to Reg. § 1.5833-1(d)(2) – the "throwback rule"- notwithstanding that another corporation that is a member of the group is doing business in that other state.~~

> ~~Example: Corporations X and Y are members of an affiliated group that conducts a unitary business. Corporation X is taxable in Vermont but not in New Hampshire. Corporation Y is taxable in New Hampshire but not in Vermont. A sale of tangible personal property shipped by Y from outside of Vermont to a customer in Vermont is not included in the Vermont sales factor (numerator). A sale of tangible personal property by X shipped from Vermont to a customer in New Hampshire is included in the Vermont sales factor under the throwback rule.~~

(b) *Apportionment of foreign dividends*. Dividends that are received from an affiliated overseas business organization and included in the combined net income of the group are apportioned using a modified apportionment factor. The intent of modification is the recognition of the property, payroll and sales of the business operations that generated the income. The modified factor is computed with respect to each overseas business organization by adding to the sales, payroll and property of the affiliated group a portion of the sales, payroll and property of the dividend-paying corporation. The modified factor is computed as follows:

> Step 1 - The dividend paid is divided by each payer's taxable income determined under the Internal Revenue Code;
>
> Step 2 - The sales, payroll and property of each payer are multiplied by the ratio determined in Step 1; and
>
> Step 3 – the portion of each payer's sales, payroll and property determined in Step 2 is added to the sales, payroll and property of the affiliated group.

The total dividends from all affiliated overseas business organizations are combined and apportioned using the modified factor. The modification is only used to apportion dividend income. Other income of the group from the unitary business is apportioned using the standard apportionment factors.

In cases in which the additional factor relief may be appropriate, the taxpayer may request such relief under the provisions of Reg. § 1.5862(d) -12. For example, where a foreign subsidiary is paying dividends that have been received from its subsidiaries, inclusion of the factors of the second level subsidiary may be necessary to fairly reflect generation of the included income.

~~Reg. § 1.5862(d) –~~ Section 9 Attributes of Separate Corporations

~~*(a) Net operating loss carryforwards and carrybacks.* If the taxable income computed pursuant to Reg. § 1.5862(d) –~~ Section ~~3 results in a loss for a taxable corporation that is a member of the group, that corporation has a Vermont net operating loss, subject to the net operating loss limitations of the Internal Revenue Code and the carryback and carryforward provisions of 32 V.S.A. § 5888(4)(B). Vermont law does not allow refunds from the operation of a net operating loss carryback. Such net operating loss is applied as a deduction in a subsequent year only if the loss was not absorbed as a net operating loss carryback on a federal return and that corporation has Vermont source positive net income. However, if some or all of the members elect to file a consolidated return, the net operating losses of these members that are part of a federal consolidated group may be used to offset the income of the affiliates entitled to file consolidated.~~

~~(b)~~ *Credits.* Any credit allowed by Vermont shall apply against the corporate income tax liability of the individual member of the group, as calculated in Reg. § 1.5862(d) - 12 below.

Reg. § 1.5862(d) - 10 Principal Vermont Corporation

(a) Definition. "Principal Vermont corporation" means a corporation that is the parent corporation unless the parent corporation is not subject to tax ~~in Vermont~~ in Vermont, ~~or is not part of the unitary business~~ or there is no parent, in which case it means the corporation that:

(1) is included within the group;

(2) is subject to Vermont's taxing jurisdiction; and

(3) has the greatest Vermont business activity during the first year that a combined return is required to be filed, as measured by the total of the Vermont factors, payroll, sales and property, for that year.

(b) *Change in principal Vermont corporation.* The principal Vermont corporation shall change only when the corporation is no longer subject to Vermont's jurisdiction to tax at which time the combined group shall designate another corporation that qualifies as its principal Vermont entity and notify the commissioner of the designation.

(c) *Responsibilities of principal Vermont corporation.*

(1) *Access to records.* In addition to the information required to be included in the group return, upon request of the commissioner, the principal Vermont corporation shall provide access to (1) the tax and financial records of members of the group that are part of the unitary group ~~but do not have Vermont nexus~~, and (2) non-financial records of the group.

(2) *Filing.* The principal Vermont corporation shall file a group return on behalf of the group together with all returns and schedules required by the commissioner using its federal identification number and its name.

(3) *Payment.* The principal Vermont corporation shall timely remit to the department the Vermont corporate tax imposed on the combined Vermont net income of the group and designate such payment on such forms as in such manner as prescribed by the Commissioner.

(d) *Notices.* Notices mailed to the principal Vermont corporation shall be deemed to have been mailed to each of the taxable corporations in the affiliated group.

Reg. § 1.5862(d) - 11 The Group Return

(a) The "group return" as referenced in this rule refers to the return that shows the liability of all corporations, wherever incorporated or domiciled, that are members of a unitary business. The group return shall be a combined return. ~~a schedule that shows the individual liability as calculated under this rule of each affiliated group member.~~ The return must include the income and apportionment factors, determined under Section 3, and other information required by the Department for all members of the combined group wherever located or doing business. The combined return must be filed under the name and federal employer identification number of the parent corporation if the parent is a member of the combined group. If there is no parent corporation, or if the parent is not a group member, the members of the combined group shall choose a member to file the return. The filing member must remain the same in subsequent years unless the filing member is no longer the parent corporation or is no longer a member of the combined group. The return must be signed by a responsible officer of the filing member on behalf of the combined group members. Members of the combined group are jointly and severally liable for the tax liability of the combined group included in the combined return

(b) The group return shall include the following information:

(1) the principal Vermont corporation;

(2) all members of the affiliated group;

~~(3) all members of the affiliated group with Vermont nexus~~;

~~(4)~~ (3) any change in the status or composition of the group since the previous taxable period;

(5) whether, in any other state requiring or allowing a combined report, any member of the Vermont affiliated group was: (i) included in a combined

report filed in the same tax year or (ii) excluded from a combined report that included other members of the Vermont group;

(6) whether any member of the affiliated group filed a separate Vermont return or was included in another group return in Vermont in a prior year;

(7) with respect to members that have separate attributes (see Reg. § 1.5862(d) - 9), the allocation of the combined income to such member;

(c) The group return shall report all income required to be included in the Vermont net income of such corporations pursuant to Reg. § 1.5862(d)-3.

~~Reg. §1.5862(d) –~~ Section 12 Tax Liability

The Vermont corporate tax is applied to the separate income of each taxable member of the group.

~~Reg. § 1.5862(d) –~~ Section 13 Alternative rule

(a) If combination under these rules leads to distortion of income or avoidance of tax, the commissioner may allow or require the use of other rules to the extent necessary to prevent such distortion or avoidance.

(b) A group that wishes to modify the application of these rules shall petition the commissioner for approval prior to employing any other method of reporting. The petition must be submitted separately by the principal Vermont corporation and not attached to a tax return and must include:

(1) The full names, addresses, federal and Vermont identifying numbers, if any, of all interested parties;

(2) a full and precise statement of the necessity for the modification;

(3) a detailed description of the business activity which necessitates the modification;

(4) evidence supporting the petition including any court decisions on the matter; any contracts, deeds, agreements, instruments or other documents which evidence the necessity of the modification; reference to statutes relating to the subject of the petition; a description of the modification requested; and a statement as to whether a similar or identical modification has been requested in any prior petition.

(c) Any petition received by the commissioner shall be submitted to the director of taxpayer services for review. The director shall review the available facts and evidence and determine if the requested modification results in a more accurate measure of the

Vermont income of the unitary group than the provisions of the rule ~~regulation~~. The director shall forward a recommendation regarding the request for modification to the petitioner and the commissioner.

(d) The petitioner may appeal the director's recommendation to the commissioner and request a hearing in the manner provided in 32 V.S.A. § 5883 within 60 days of the mailing of the recommendation.

(e) The fact that separate accounting produces a different tax liability does not prove the need for or the acceptability of modified of the rule ~~regulation~~.

(f) The use of modified combined reporting without prior written approval or determination of the commissioner or court decision approving the same shall constitute a failure to file as required by 32 V.S.A. § 5862.

~~Reg. § 1.5862(d) - 14 Exclusion From Consolidated Return~~

~~A corporation that is required to be included in a group return may be included in a consolidated return elected under 32 V.S.A. § 5832 provided that the consolidated members have the same fiscal year.~~