Publication Date: August 8, 2009
Effective: August 8, 2009 through January 4, 2010

ORDER OF THE DEPARTMENT OF REVENUE ADOPTING AN EMERGENCY RULE

The Wisconsin Department of Revenue hereby adopts an emergency rule interpreting s. 71.255, Stats., relating to combined reporting for corporation franchise and income tax purposes.

Analysis by the Department of Revenue
Statute interpreted: s. 71.255, Stats.
Statutory authority: General rulemaking authority in s. 227.24, Stats.; specific rulemaking authority granted in s. 71.255, Stats., as follows:

- Section 71.255(6)(b)2. and (c)2., Stats., relating to net business loss carryforwards, credits, and credit carryforwards.
- Section 71.255(7)(a), Stats., relating to identifying the designated agent.
- Section 71.255(11), relating to the adoption of federal treasury regulations so that transactions among combined group members are treated consistently with transactions among federal consolidated group members.

Explanation of agency authority: An agency may promulgate a rule as an emergency rule without complying with the notice, hearing, and publication requirements of the statutes if preservation of the public peace, health, safety, or welfare necessitates putting the rule into effect prior to the time it would take effect if the agency complied with the procedures.

Related statute or rule: ss. 71.24(1), (1m), and (7), 71.29, 71.44(1),(1m), and (3), 71.77, 71.82, 71.83, and 71.84, Stats.

Plain language analysis: This emergency rule creates eight new rule sections. The purpose of each rule section is provided below:

Section Tax 2.60 Definitions Relating to Combined Reporting.

- Provides definitions relating to the other rule sections created by this rule order. Those other sections are ss. Tax 2.61, 2.62, 2.63, 2.64, 2.65, 2.66, and 2.67.

Section Tax 2.61 Combined Reporting.

- Explains who must use combined reporting.
- Provides rules for determining whether a corporation is a member of a "commonly controlled group."
- Explains when a corporation's income is not subject to combination because of the degree of the corporation's activity outside the U.S. ("water's edge" rules).
- Explains how to compute the combined group's combined unitary income, including the applicability of federal regulations that relate to consolidated groups. The following components of the computation are covered:
  - Intercompany transactions
  - Capital gains and losses
  - Charitable contributions
  - Dividends
  - Stock basis adjustments
  - Earnings and profits
  - Allocation of expenses and deductions
- Explains how to apportion the combined unitary income and rules that apply to various aspects of the apportionment computation.

- Provides rules for determining the taxable income of combined groups that are not subject to apportionment.
- Describes how to apply net business loss carryforwards, including rules relating to the sharing of net business losses.
- Describes how to apply credits, including rules relating to the sharing of research credits.

Section Tax 2.62 Unitary Business.

- Explains the concept of a "unitary business" and its relationship to the concept of a "combined group."
- Enumerates several characteristics that are indicators of a "unitary business."
- Lists some key U.S. Supreme Court cases which provide further guidance on the extent to which a business enterprise is considered a "unitary business" under the U.S. Constitution. This is significant because the statute provides that "unitary business" shall be construed to the broadest extent permitted by the U.S. Constitution.
- Provides several presumptions to aid taxpayers in determining whether a unitary business exists.
- Provides specific rules relating to the inclusion of passive holding companies and pass-through entities in the unitary business.

Section Tax 2.63 Controlled Group Election.

- Explains how to make the election and how to renew it after its 10-year duration.
- Provides rules relating to the department's authority to disregard the election in cases where it has the primary effect of tax avoidance rather than its intended purpose of simplifying the determination of who must be included in the combined report.

Section Tax 2.64 Alternative Apportionment for Combined Groups Including Specialized Industries.

- Specifies how and when a qualifying group may file a petition for alternative apportionment and what information must be submitted to the department.
- Provides that once the department approves the alternative method, that same method must be used for a 7-year period, subject to a limitation that the tax computation under the alternative method cannot be lower than what it would have been if each corporation apportioned its income separately.

Section Tax 2.65 Designated Agent of Combined Group.

- Explains how to identify which corporation is responsible to act on behalf of the combined group for matters relating to the combined return.
- Defines the scope and limitations of the agency relationship.

Section Tax 2.66 Combined Estimated Tax Payments.

- Explains when a combined group member may make its own estimated payments, rather than having the designated agent make the payments on its behalf.
- Provides rules for determining the combined group's required estimated tax payments.
- Provides rules for applying estimated payments and overpayments of prior year estimated payments.

Section Tax 2.67 Combined Returns.

- Enumerates the required components of a combined return and explains how to report separate entity items.
- Explains how to determine the taxable year of a combined return.
- Provides rules relating to interest, penalties, and statutes of limitations as they relate to combined returns.

Summary of, and comparison with, existing or proposed federal regulation:
The emergency rules presented in this rule order are very similar to the federal regulations relating to consolidated groups. The federal regulations listed below are specifically referenced or adopted in this rule order, but modified to apply to combined groups instead of federal consolidated groups.

- Treas. Reg. §1.1502-13, relating to intercompany transactions. This federal regulation was actually adopted by statute (s. 71.255(4)(g), Stats.), but is interpreted in this rule order (s. Tax 2.61(6)(b)).
- Treas. Regs. §1.1502-22 and 1.1502-23, relating to capital gains and losses and section 1231 gains and losses (s. Tax 2.61(6)(c)).
- Treas. Reg. §1.1502-24, relating to charitable contributions (s. Tax 2.61(6)(d)).
- Treas. Reg. §1.1502-32, relating to investment (stock basis) adjustments (s. Tax 2.61(6)(f))
- Treas. Reg. §1.1502-33, relating to earnings and profits (s. Tax 2.61(6)(g)).

The general purpose of the above federal regulations is to treat the members of a federal consolidated group as if they were divisions of a single corporation. Likewise, the purpose of adopting these rules for Wisconsin purposes is to treat the members of a combined group as if they were divisions of a single corporation.

Comparison with rules in adjacent states:
Illinois: Illinois has comprehensive regulations relating to its combined reporting statute. (including IL Regs. 100.2340, 100.2570, 100.5200, 100.5201, 100.5210, 100.5220, 100.5230, 100.5240, 100.5250, 100.5260, 100.5265, 100.5280, and 100.9700). The following aspects of the rules in this rule order were modeled after the Illinois regulations, with some modifications:

- Adoption of federal consolidated return regulations
- Combined estimated tax payments
- Rules relating to the duties of the designated agent

Iowa: Iowa does not have a statute which permits or allows combined reporting. Thus, it has no rules or regulations relating to combined reporting.

Michigan: Michigan adopted combined reporting in 2008, when it enacted its Michigan Business Tax. At the time this rule order was authored, Michigan has not yet promulgated rules or regulations relating to its combined reporting statute. However, Michigan has published an extensive amount of guidance in the form of Frequently Asked Questions.

Minnesota: Like Illinois, Minnesota has rules relating to its combined reporting statute (including Rules 8019.0100, 8019.0300, 8019.0405, and 8019.0500, Minn. Rules). The section of this rule order that provides guidance in determining a "unitary business" (s. Tax 2.62) is modeled after Minnesota's rule 8019.0100, with some modifications.

Summary of factual data and analytical methodologies:

The department developed these regulations based upon research of the combined reporting laws, rules, regulations, published guidance, and tax form instructions of other states. The Illinois and Minnesota regulations referenced above were frequently used as a resource, in addition to various law journal articles and tax publications.

The combined reporting regulations recently promulgated by Massachusetts (830 CMR 63.32B.2) were heavily relied upon. The Massachusetts combined reporting law (M.G.L. c. 63 §32B), like Wisconsin's, is first effective for taxable years beginning on or after January 1, 2009, and Wisconsin's law has many similarities with the Massachusetts law.

The department also studied the regulations under section 1502 of the Internal Revenue Code, relating to consolidated returns.

Analysis and supporting documents used to determine effect on small business:

Combined reporting primarily affects larger corporations, rather than small businesses. Combined reporting is required for regular "C" corporations, but is not required for the types of entities that are more characteristic of small businesses, such as:

- Sole proprietorships,
- Partnerships,
- Limited liability companies taxed as partnerships, and
- S corporations

Anticipated costs incurred by private sector: This emergency rule does not have a significant fiscal effect on the private sector independently from the statute it interprets.

Effect on small business: This emergency rule does not have a significant effect on small business.

Agency contact person: Please contact Wendy Miller at (608) 266-7177 or WENDY.MILLER@revenue.wi.gov, if you have any questions regarding this emergency rule.

Place where comments are to be submitted and deadline for submission: Comments may be submitted to the contact person shown below no later than one week after the public hearing on this emergency rule is conducted. Information as to the place, date, and time of the public hearing will be published in the Wisconsin Administrative Register.

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FINDING OF EMERGENCY
The Department of Revenue finds that an emergency exists and that the attached rule order is necessary for the immediate preservation of the public peace, health, safety or welfare. A statement of the facts constituting the emergency is:

The function of the Wisconsin Department of Revenue is to administer the Wisconsin tax laws. These laws, and tax policy for raising revenue, are determined by the State Legislature. The State Legislature recently enacted numerous items of tax legislation, affecting individuals and businesses alike. Some of these apply retroactively to January 1, 2009. Emergency rules are needed, not only to address the risk of revenue loss, but to add more clarity and certainty about the scope and application of the newly enacted statutes.

This rule is therefore promulgated as an emergency rule and shall take effect upon publication in the official state newspaper. Certified copies of this rule have been filed with the Secretary of State and Revisor of Statutes, as provided in s. 227.24, Stats.

SECTION 1. Tax 2.60, 2.61, 2.62, 2.63, 2.64, 2.65, 2.66, and 2.67 are created to read:

Tax 2.60 Definitions Relating to Combined Reporting. (1) PURPOSE. This section provides definitions applicable to ss. Tax 2.61, 2.62, 2.63, 2.64, 2.65, 2.66, and 2.67, which interpret the combined reporting provisions of s. 71.255, Stats.

(2) DEFINITIONS. (a) "Combined group" has the meaning given in s. 71.255(1)(a), Stats. The following subdivisions clarify this meaning:

1. If a group of corporations satisfies all three conditions described in s. Tax 2.61(2)(a), it is considered a combined group even if the group is not eligible to apportion its income because all corporations in the group do business solely in Wisconsin.

2. A combined group remains in existence for as long as two or more corporations meet all three conditions described in s. Tax 2.61(2)(a) with regard to the same unitary business. The mere addition of new members or departure of existing members does not create a new combined group.

3. Any commonly controlled group that has made a controlled group election is a combined group, and each member of such commonly controlled group is a combined group member.

(b) "Combined group member" means a corporation for which any part of the corporation's net income or loss is subject to combination and therefore required to be included in a combined report, or any member of a commonly controlled group that is subject a controlled group election.

(c) "Combined report" has the meaning given in s. 71.255(1)(b), Stats. A combined report is considered a return filed pursuant to ss. 71.24(1) or (1m) or 71.44(1) or (1m), Stats., as applicable, by each corporation included in the combined report. For this reason, the term "combined return" is used throughout the rules of this chapter to refer to a combined report.

(d) "Combined return" has the same meaning as "combined report" as explained in par. (c). In general, a combined return includes the computation of combined unitary income, the apportionment of the income to each combined group member, as applicable, any separate entity items, loss carryforwards, and credits of each combined group member, and the net tax and recycling surcharge liability of each combined group member. To be considered complete, a combined return must contain all the items required in s. Tax 2.67(2)(c).

(e) "Combined unitary income" means the combined group's net income or loss attributable to the unitary business which is subject to combination under s. 71.255, Stats., before apportionment and net business loss carryforwards. Combined unitary income excludes any amounts that are not subject to combination because of the water's edge rules.

(f) "Controlled group election" means an election to include every member of the commonly controlled group in the combined group as provided by s. 71.255(2m), Stats., and further described in s. Tax 2.63.

(g) "Corporation" includes corporations, publicly traded partnerships treated as corporations in section 7704 of the internal revenue code, limited liability corporations treated as corporations under the internal revenue code, joint stock companies, associations, common law trusts and all other entities treated as corporations under section 7701 of the internal revenue code, unless the context requires otherwise in this chapter or in ch. 71, Stats.

(h) "Designated agent" means the corporation in the combined group responsible for acting on behalf of the group for matters relating to the combined return, as further described in s. Tax 2.65.

(i) "Income" and "net income" include net losses, unless the context requires otherwise.

(j) "Intercompany transaction" means a transaction between two members of the same combined group.

(k) "Internal revenue code" has the meaning given in ss. 71.22(4) and (4m) and 71.42(2), Stats., as applicable.

(L) "Nonincludable corporation" means a corporation that is not required to use combined reporting even if it satisfies all three conditions described in s. Tax 2.61(2)(a). A nonincludable corporation cannot be a combined group member even if the nonincludable corporation is a member of a commonly controlled group which has made the controlled group election.

(m) "Separate entity item" means a combined group member's item of net income or loss or apportionment factor amount which is not subject to combination but instead must be accounted for on a separate entity basis. Separate entity items include those listed in s. Tax 2.61(5)(b) to (g), assuming such items are taxable. Separate entity items do not include a corporation's net income or loss or apportionment factors which were incurred while the corporation was not a member of the combined group.

(n) "State" means a state of the United States, the District of Columbia, the commonwealth of Puerto Rico, or any territory or possession of the United States.

(o) “Unitary business income” means the net income or loss derived from the unitary business, whether or not such income or loss is subject to combination. “Unitary business” is explained further in s. Tax 2.62.

(p) “Unitary combination” means the computation of a combined group’s combined unitary income and of each member’s share thereof.

(q) “Water’s edge rules” means the rules provided under s. Tax 2.61(4) under which some or all of a corporation’s items attributable to a unitary business are not subject to combination because of the degree of the corporation’s activity outside the United States.

Note: Section Tax 2.60 interprets s. 71.255, Stats.

Tax 2.61 Combined Reporting. (1) SCOPE. Section 71.255, Stats., generally requires corporations that are commonly controlled and engaged in a unitary business to compute their net income on a combined basis. This section explains when combined reporting is required and how to compute a corporation’s net income and tax liability under combined reporting. Subsections (2) to (4) describe who must use combined reporting and what income is subject to combination. Subsections (5) to (9) explain how to compute the taxable income of a combined group member, including net business loss carryforwards. Subsection (10) provides rules relating to credits and credit carryforwards.

(2) CORPORATIONS REQUIRED TO USE COMBINED REPORTING. (a*) General.* A corporation is required to use combined reporting if it satisfies each of the following three conditions:

1. The corporation is a member of a “commonly controlled group” as defined in s. 71.255(1)(c), Stats. See sub. (3) for rules that apply to identifying a commonly controlled group of corporations.

2. The corporation is engaged in a “unitary business,” as defined in s. 71.255(1)(n), Stats., with one or more other corporations in its commonly controlled group, or the commonly controlled group makes a controlled group election. See s. Tax 2.62 for rules to determine whether corporations are engaged in a unitary business. See s. Tax 2.63 for rules pertaining to the controlled group election.

3. The corporation has unitary business income that is subject to combination under the water’s edge rules described in sub. (4).

(b) *Effect of controlled group election.* If a controlled group election applies as indicated in par. (a)2., all corporations in the commonly controlled group are deemed to be engaged in the same unitary business, and all of their net income or loss and apportionment factors are deemed to be derived from that unitary business. In general, this means that if the controlled group election applies, all members of the commonly controlled group are included in a combined report. However, despite this election, a corporation may be required to exclude some or all of its net income, loss, and apportionment factors from the unitary combination if so required under the water’s edge rules described in sub. (4).

(c) *Corporations treated as pass-through entities.* Corporations that are included in the definition of “pass-through entity” in s. 71.255(1)(m), Stats., including tax-option corporations, real estate investment trusts, regulated investment companies, real estate mortgage investment conduits, and financial asset securitization investment trusts, are generally nonincludable corporations. However, to the extent the net income or loss of such pass-through entities is included in the net income of, or distributed to, a combined group member, such net income or loss, along with the corresponding apportionment factors as provided in sub. (7)(e), is subject to combination to the extent derived from the unitary business and otherwise subject to combination under the water’s edge rules described in sub. (4).

(d) *Tax exempt organizations.* A corporation that is exempt from income and franchise taxes under ss. 71.26(1) or 71.45(1), Stats., is a nonincludable corporation except to the extent it has unrelated business taxable income as defined in section 512 of the internal revenue code. The net unrelated business taxable income, and any apportionment factors related thereto, is subject to combination to the extent such net income or loss is derived from the unitary business and is otherwise subject to combination under the water’s edge rules described in sub. (4).

(e) *Disregarded entities.* An entity that is disregarded as a separate entity for federal income tax purposes under section 7701 of the internal revenue code is considered a branch or division of its owner for Wisconsin income and franchise tax

purposes. A corporation must include the net income or loss and apportionment factors of any disregarded entity of which it is an owner in the combined report to the extent they would be included if the corporation itself earned the income. The water's edge rules described in sub. (4) do not apply to disregarded entities except insofar as the rules apply to the owner of the disregarded entity.

(f) *Other provisions that may apply.* Nothing in ss. Tax 2.60 to 2.67, inclusive, is intended or should be construed as a waiver of the department's authority under s. 71.255(2)(f), Stats., or any other authority granted to the department by law. Section 71.255(2)(f), Stats., provides the following:

1. The department may require that a combined report include the items of any person or entity who is not otherwise a combined group member but who is a member of the unitary business, in order to reflect proper apportionment of income of the entire unitary business.

2. If the reported income or loss of a combined group member engaged in a unitary business with a person or entity who is not otherwise a combined group member represents an avoidance or evasion of tax by either party, the department may require all or any part of the income or loss and apportionment factors of either party to be included in or excluded from a combined report, or may require the use of a different apportionment factor or factors.

(3) COMMONLY CONTROLLED GROUP. In general, s. 71.255(1)(c), Stats., provides that a commonly controlled group exists in cases where there is common ownership or control of stock representing more than 50 percent of the voting power of the corporations in the group. The corporations in a commonly controlled group shall be determined as provided in s. 71.255(1)(c), Stats., which is further explained in the following paragraphs:

(a) *Stock attribution rules.* For purposes of s. 71.255(1)(c)1. and 2., Stats., a shareholder is considered to have indirect ownership of stock or indirectly own stock if the shareholder has constructive ownership of such stock by operation of section 318 of the internal revenue code, except as provided in subds. 1. and 2.

Example: Corporation A owns stock representing 40% of the voting power of Corporation B and has a 50% interest in Partnership C. Partnership C owns stock representing 30% of the voting power of Corporation B. By operation of section 318 of the internal revenue code, Corporation A constructively owns stock representing 55% (= 40% + (50% x 30%)) of the voting power of Corporation B.

1. In applying section 318(a)(2) of the internal revenue code, if a partnership, estate, trust, or corporation owns, directly or indirectly, more than 50 percent of an entity, it shall be considered to own all of the stock or other ownership or control interests owned by such entity.

Example: Corporation D owns stock representing 10% of the voting power of Corporation E and has a 75% interest in Partnership F. Partnership F owns stock representing 45% of the voting power of Corporation E. Under subd. 1., Corporation D is considered to constructively own stock representing 55% (= 10% + 45%) of the voting power of Corporation E. This is because Corporation D owns more than 50% of Partnership F and is therefore considered to own all of the Corporation E stock owned by Partnership F.

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

(b) *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.

(c) *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.

(d) *Voting power.* 1. A shareholder has ownership or control of stock representing more than 50 percent of the voting power of a corporation only if the shareholder has ownership or control of more than 50 percent of the total combined voting power of all classes of stock of the corporation entitled to vote.

2. A group of 2 or more corporations need not be commonly owned to be commonly controlled. As provided in s. 71.255(1)(c)3., Stats., a group of corporations may be a commonly controlled group if stock representing more than 50 percent of the voting power in each corporation are interests that cannot be separately transferred. If a group of 2 or more corporations would be considered stapled entities under section 269B of the internal revenue code and the regulations thereunder, without regard to whether such corporations are foreign or domestic, the corporations shall be considered part of a commonly controlled group.

3. The mere ownership of stock entitled to vote does not by itself mean that the shareholder owning such stock has the voting power of such 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 50 percent or less of the total combined voting power will exercise voting power normally possessed by a majority of stockholders, the department may presume that the nominal ownership of the voting power is not determinative of which shareholders actually hold such voting power and may disregard the nominal ownership. This presumption may be rebutted by the taxpayer.

4. If a shareholder owns shares of stock of a corporation which has another class of stock outstanding, the voting power of such 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 such other class of stock do not exercise their voting rights independently or fail to exercise such 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 department may presume that the principal purpose of the arrangement was avoid the inclusion of such corporation in the commonly controlled group and may disregard the voting power of the class of stock that was not exercised. This presumption may be rebutted by the taxpayer.

(4) WATER'S EDGE. This subsection describes how a corporation that is otherwise a combined group member must determine and report items that are not subject to combination due to the extent of the corporation's activities outside the United States, as provided in s. 71.255(2), Stats. In general, the corporation must consider whether it is a foreign corporation or domestic corporation, whether it qualifies as an "80/20 corporation," and whether its income is from foreign sources or U.S. sources. The following rules apply:

(a) *Qualifying as a "foreign corporation."* For purposes of the water's edge rules in pars. (d) and (e), a "foreign corporation" means any corporation that is not incorporated, organized, or created in the United States or under the laws of the United States or any state. For purposes of determining whether a corporation is a foreign corporation or a domestic corporation, the following rules apply:

1. If, for federal purposes, a corporation is treated as created or organized under the laws of both the U.S. and a foreign jurisdiction, it is a domestic corporation.

2. A foreign corporation that domesticates and is treated by a state as organized under the laws of that state is a domestic corporation.

3. If an entity is organized in a foreign country and is recognized in that country as a corporation, but the entity's owner elects to treat that entity as a branch for U.S. taxation purposes or the entity is a disregarded entity, the entity shall be treated as a branch of its owner.

(b) *Qualifying as an "80/20 corporation."* 1. For purposes of the water's edge rules in pars. (d) and (e), a corporation is an "80/20 corporation" if 80 percent or more of its worldwide gross income during the testing period is "active foreign business income" as defined in section 861(c)(1)(B) of the internal revenue code.

2. The testing period for purposes of subd. 1. is the tested corporation's taxable year that would be included in the combined group's taxable year, as determined by s. 71.255(8), Stats. If the tested corporation was not otherwise eligible to be a combined group member for any part of such taxable year (for example, the corporation did not satisfy the conditions in sub. (2)(a)1. or 2.), the testing period is the portion of such taxable year in which the corporation was otherwise eligible to be a member.

3. An 80/20 corporation may be either a foreign corporation or a domestic corporation.

4. For purposes of this paragraph, a corporation's active foreign business income includes gross income attributed from subsidiary corporations as provided in section 861(c)(1)(B) of the internal revenue code, but only to the extent the gross income of the subsidiary corporations is derived from the combined group's unitary business.

5. A disregarded entity's active foreign business income and worldwide gross income must be combined with those of its owner for purposes of applying the test in subd. 1.

(c) *Foreign source income.* 1. For purposes of the water's edge rules in pars. (d) and (e), income is foreign source income if it is from sources without the United States as provided in sections 861 through 865 of the internal revenue code, subject to subd. 3. "United States" has the same meaning as in sections 861 through 865 of the internal revenue code.

2. All income that is not foreign source income is U.S. source income.

3. For purposes of this subsection, income that is effectively connected with the conduct of a trade or business within the United States, as provided in section 864(c)(4) of the internal revenue code, is considered U.S. source income even if derived from sources without the United States.

(d) *Water's edge rules for domestic corporations.* 1. A domestic corporation that is not an 80/20 corporation shall include in the unitary combination its net income or loss, and apportionment factors related thereto, from the unitary business regardless of whether it is foreign source income or U.S. source income.

2. A domestic corporation that is an 80/20 corporation is a consolidated foreign operating corporation. A consolidated foreign operating corporation shall include in the unitary combination its net income or loss, and the apportionment factors related thereto, from the unitary business only to the extent it is both U.S. source income and is income described in s. 71.255(2)(d), Stats. Such corporation shall not include in the unitary combination any foreign source income, income not described in s. 71.255(2)(d), Stats., expenses or deductions related to the excluded income as provided in sub. (6)(h), or apportionment factors related to the excluded income. However, the excluded income may still be taxable as described in par. (h). The income described in s. 71.255(2)(d), Stats., is explained further in par. (f).

(e) *Water's edge rules for foreign corporations.* 1. A foreign corporation that is not an 80/20 corporation shall include in the unitary combination its net income or loss, and the apportionment factors related thereto, from the unitary business only to the extent it is U.S. source income. Such corporation shall not include in the unitary combination any foreign source income, expenses or deductions related to the excluded income as provided in sub. (6)(h), or apportionment factors related to the excluded income. However, this foreign source income may still be taxable as described in par. (h).

2. Except as provided in subd. 3., a foreign corporation that is an 80/20 corporation shall not include any income, expenses, or apportionment factors in the unitary combination, but may still have taxable income as described in par. (h).

3. A foreign corporation that is an 80/20 corporation but elects to be included in a federal consolidated return for the taxable year shall be treated as if it is a domestic corporation. The rules of par. (d)2. apply to such corporation.

(f) *Includable income of consolidated foreign operating corporations.* The net income that a consolidated foreign operating corporation must include in a unitary combination, as described in par. (d)2., includes the following to the extent such income is U.S. source income and from the unitary business:

1. Interest income or income generated from intangible property, whether or not such income is derived from persons or entities related to the consolidated foreign operating corporation. Income generated from intangible property includes, but is not limited to, income related to the direct or indirect acquisition, use, maintenance, management, ownership, sale, exchange, or any other disposition of intangible property; income from factoring transactions or discounting transactions; royalty, patent, technical, and copyright fees; and licensing fees. For purposes of this subdivision, "intangible property" has the meaning given in s. 71.22(3h), Stats.

2. Income derived from interest expenses or intangible expenses that were paid, accrued, or incurred by combined group members to or for the benefit of the consolidated foreign operating corporation; to the extent those amounts were

not already included under subd. 1. For purposes of this subdivision, "interest expenses" has the meaning given in s. 71.22(3m), Stats., and "intangible expenses" has the meaning given in s. 71.22(3g), Stats.

3. Dividend income received from a real estate investment trust that is not a qualified real estate investment trust as defined in s. 71.22(9ad), Stats.

4. Gains or losses derived from the sale or lease of real or personal property located in the United States.

5. Expenses or deductions related to the income, gains, and losses described in subds. 1. to 4., determined in the manner provided in sub. (6)(h).

(g) *Applicability of federal treaties.* If a corporation's income is not taxable for federal income tax purposes under the provisions of a federal treaty, such income is not taxable for Wisconsin purposes and is not required to be included in combined unitary income. A corporation shall not include in the unitary combination any expenses or apportionment factors attributable to income that is exempt by federal treaty.

(h) *Taxation of income not subject to combination under water's edge.* Any income, expenses, and apportionment factors that are excluded from the unitary combination under pars. (d) and (e) must be taken into account by the separate corporation that earned the income. The following rules apply to determining and reporting Wisconsin net income or loss not subject to combination under the water's edge rules:

1. The net income or loss is presumed to be from a unitary business and therefore apportionable.

2. Except as provided in subd. 3., if a corporation has no net income or loss or apportionment factors that are subject to combination, the corporation is not a combined group member and the provisions of s. 71.255(5)(a), Stats., which state that each member of a combined group is doing business in this state if any member of the combined group is doing business in this state relating to the unitary business, do not apply. Such corporation has nexus in this state if it is doing business in this state as defined in s. 71.22(1r), Stats., and further explained in s. Tax 2.82. A corporation may have nexus in this state if any agent of the corporation, including a member of the combined group, acts on the corporation's behalf in this state in a manner that would create nexus under s. 71.22(1r), Stats., s. Tax 2.82, or otherwise.

3. A member of a commonly controlled group that is subject to the controlled group election is a combined group member regardless of whether it has items subject to combination under the water's edge rules. Therefore, such member has nexus in this state if any member of the combined group is doing business in this state.

4. A corporation that is a combined group member has nexus in Wisconsin by operation of s. 71.255(5)(a), Stats. Therefore, an apportioned share of its net income or loss that is not subject to combination under the water's edge rules may be taxed by Wisconsin.

5. The provisions of ss. 71.26(2)(a)7. and 71.45(2)(a)16., Stats., requiring an addition modification for interest expenses, rent expenses, intangible expenses, and management fees paid, accrued, or incurred to a related entity, apply to any amounts not subject to combination which were paid, accrued, or incurred by the corporation to any related entity, even if the related entity was a combined group member.

6. The numerator and denominator of the apportionment ratio shall include only that corporation's apportionment factors attributable to unitary business income that is not subject to combination. Intercompany transactions shall not be eliminated from the apportionment factors unless the department determines those transactions have no economic substance as determined under the provisions of ss. 71.30(2m) or 71.80(1m), Stats., as applicable, or if those transactions have no business purpose other than tax avoidance. In computing the amount of throwback sales includable in the numerator, the provisions of sub. (7)(c) do not apply unless the corporation is a combined group member.

7. Income separately apportioned as described in this paragraph may be reported on a designated line of the combined return, supported by a department-prescribed schedule. This separately apportioned income is considered a separate entity item. See s. Tax 2.67(2)(d) for filing requirements relating to separate entity items.

Examples: 1) A, B, and C are corporations in a commonly controlled group and engaged in a unitary business. All of the income of the corporations is derived from the unitary business. A and B are incorporated in Delaware. C is incorporated in France. The income of A and B is derived exclusively from U.S. sources. Ninety percent of C's worldwide gross income is active foreign business income. The remaining 10% of C's worldwide gross income is U.S. source income, some of which has situs in Wisconsin. C has agents acting on its behalf in Wisconsin which create nexus. Since C is a foreign 80/20 corporation, none of its net income, expenses, or apportionment factors may be included in the unitary combination. Thus, C is not a combined group member.

However, C is subject to tax on an apportioned share of its worldwide net income, to the extent such income is not exempt by federal treaty. In determining the apportioned share, the numerator and denominator of C's apportionment factors are its numerator and denominator computed for C on a separate entity basis. Since C is not a combined group member, it cannot consider the activities of A or B when it computes its throwback sales for purposes of the numerator. C is required to report this income to Wisconsin as a separate entity item.

2) Combined Group DE consists of Member D and Member E. Both D and E are Delaware corporations. All of the income of D and E is derived from the unitary business. All of D's income is from sources within the U.S. However, 85% of E's worldwide gross income is active foreign business income, making E a domestic 80/20 corporation. E has total of $150,000 of income from the unitary business, net of expenses. Of this amount, $100,000 is derived from intangible property and $50,000 is derived from service fees. D and E must include in the unitary combination all of D's income, expenses, and apportionment factors and E's income, expenses, and apportionment factors only to the extent related to its income derived from intangible property. Since E is a domestic 80/20 corporation and service fees are not one of the types of income subject to combination for a domestic 80/20 corporation, E's service fee income, and expenses and apportionment factors relating to that income, must be excluded from the unitary combination.

However, E is subject to tax on an apportioned share of its service fee income. E has nexus in Wisconsin because it is a member of Group DE, which is doing business in Wisconsin. In determining the apportioned share, the numerator and denominator of E's apportionment factors are its numerator and denominator including only the factors relating to its service fee income and computed for E on a separate entity basis. However, since E is a combined group member, it may consider the activities of D when it computes its throwback sales for purposes of the numerator. E is required to report this income to Wisconsin as a separate entity item.

(5) TAXABLE INCOME OF A COMBINED GROUP MEMBER. The taxable income of a combined group member consists of the components listed in this subsection. For purposes of pars. (c) and (d), a "distinct business activity" means a business activity that is not unitary with the combined group's unitary business. For purposes of determining the expenses and deductions attributable to each component, the provisions of sub. (6)(h) apply. A combined group member's taxable income is the total of all of the following:

(a) Its apportioned share of the combined unitary income, as computed under subs. (6) and (7), or, in the case of a combined group where all members are doing businesses solely within Wisconsin, its unitary business income subject to combination as computed under subs. (6) and (8).

(b) An apportioned share of the unitary business income not subject to combination under the water's edge rules of sub. (4), or in the case of a combined group where all members are doing business solely within Wisconsin, its total unitary business income not subject to combination under the water's edge rules of sub. (4).

(c) An apportioned share of income from a distinct business activity conducted within and outside this state wholly by the member.

(d) Its income from a distinct business activity conducted entirely within this state wholly by the member.

(e) Its nonbusiness income or loss allocable to this state.

(f) Its income realized from the purchase and subsequent sale or redemption of lottery prizes, if the winning tickets were originally bought in this state.

(g) Any income, loss, or deduction allocated or apportioned in an earlier year which is taken into account as Wisconsin source income or loss during the taxable year, other than a net business loss carryforward. This includes non-sharable net capital loss carryovers as described in sub. (6)(c).

(h) Its net business loss carryforward, including any other combined group members' net business loss carryforwards which may offset the member's share of combined unitary income under the provisions of sub. (9).

(6) COMPUTATION OF COMBINED UNITARY INCOME. This subsection interprets s. 71.255(4), Stats., relating to a combined group's computation of business income subject to combination, which is called "combined unitary income" for purposes of this section. The steps to compute combined unitary income are as follows:

(a) *General.* 1. Compute the sum of each combined group member's net income determined under the internal revenue code before Wisconsin modifications, without regard to net capital gain or loss or deductions for charitable contributions. Compute this income as if the member were not consolidated for federal purposes.

2. Defer or recognize any intercompany income, expense, gain, or loss between combined group members as described in par. (b), except to the extent the income, expense, gain, or loss is excluded from the combined unitary income because it does not relate to the unitary business or is not subject to combination under the water's edge rules of sub. (4).

3. Add net capital gain includable in the combined unitary income, applying the loss limitation as described in par. (c) and using the federal basis of assets. Any differences between the federal and Wisconsin basis of assets, including but not limited to basis differences that arise from the application of par. (f), are accounted for as Wisconsin modifications under subd. 5. The Wisconsin basis of a corporation's depreciable property for the first year the corporation becomes taxable in Wisconsin equals its federal basis as of the beginning of the taxable year in which the corporation becomes taxable in Wisconsin, as required under s. 71.265, Stats.

4. Subtract the charitable contributions deduction includable in the combined unitary income, computed as described in par. (d).

5. Apply Wisconsin addition and subtraction modifications provided in ss. 71.26 and 71.45, Stats., as applicable. For interest expenses, rent expenses, intangible expenses, and management fees paid, accrued, or incurred between combined group members, including pass-through entities owned by such members to the extent of their distributive shares of income, the addition modifications for related entity expenses under ss. 71.26(2)(a)7. and 71.45(2)(a)16., Stats., are not required to the extent the recipient of the income includes the income in the combined unitary income.

6. Subtract any dividends that qualify for elimination under par. (e) to the extent the dividends did not qualify for a subtraction modification under subd. 5.

7. If a combined group member is an insurance company, subtract the portion of net income attributable to the insurance company's life insurance operations as determined using s. 71.45(2)(b), Stats.

8. Subtract the income, as modified by subds. 5. to 7., which is not includable in combined unitary income because it is not derived from the unitary business or is not subject to combination under the water's edge rules of sub. (4). The income subtracted under this subdivision must be net of any directly or indirectly related expenses as provided in par. (h). The amount subtracted under this subdivision shall not duplicate any amounts already subtracted.

(b) *Intercompany transactions*. Defer or recognize any intercompany income, expense, gain, or loss between combined group members that would be deferred or recognized between those members under United States treasury regulation 1.1502-13 as if the combined group were a federal consolidated group, except that the provisions for intercompany dividends are excluded and replaced with par. (e). This paragraph does not apply to intercompany transactions which occurred in taxable years beginning before January 1, 2009 or to intercompany transactions where the income, expense, gain, or loss would not otherwise be subject to combination. For modifications to United States treasury regulation 1.1502-13 that are necessary in the case of a combined group doing business solely in this state, see sub. (8). Any deferred intercompany income, expense, gain, or loss that is recognized under this paragraph shall be recognized by the same combined group member that deferred the income, expense, gain, or loss. The deferred income, expense, gain, or loss

shall be recognized when required under United States treasury regulation 1.1502-13 as if the combined group were a federal consolidated group, or when any of the following apply:

1. The buyer resells the object of the deferred intercompany transaction to an entity that is not a member of the combined group.

2. The object of the deferred intercompany transaction is used outside the combined group's unitary business as a result of the buyer's resale, conversion, or transfer of the asset.

3. The buyer and seller are no longer members of the same combined group, regardless of whether they are in the same unitary business.

Example: S and B are combined group members. S has land with a basis of $130,000 at the end Year 1. In Year 2, S sells the land to B for $100,000. B holds the land until Year 3, when it sells it to X, a person outside the combined group, for $110,000. Assume both sales are otherwise includable in the combined unitary income. Applying U.S. Treas. Reg. § 1.1502-13 to S and B in the manner described in this paragraph, S would not recognize any gain or loss on the sale of the land to B in Year 2. However, in Year 3, S would recognize a $30,000 loss and B would recognize a simultaneous $10,000 gain. Thus, in Year 2, the combined group cannot include S's $30,000 loss on sale of land in its combined unitary income, but in Year 3, the combined group can include a $20,000 loss on sale of land (the net amount of S's Year 2 loss and B's Year 3 gain) in its combined unitary income. However, the capital loss limitation may limit this loss, as described further in par. (c).

(c) *Capital gains and losses.* Compute the capital loss limitation so that it applies to the combined group as a whole, to the extent the capital gains and losses are derived from the unitary business and otherwise subject to combination. Rules to determine the capital loss limitation, the assignment of capital gains and losses to members, and the amounts available for carryover, are as follows:

1. For short-term capital gains or losses, long-term capital gains or losses, section 1231 gains or losses, and involuntary conversions, aggregate all combined group members' amounts within each class of gain or loss. Except as provided in subd. 8., include sharable net capital loss carryovers as defined in subd. 2. but not non-sharable net capital loss carryovers.

2. A combined group member's sharable net capital loss carryover is any available net capital loss carryover which would be a sharable loss carryforward under sub. (9)(a) if it were a net business loss carryforward. A non-sharable net capital loss carryover is any available net capital loss carryover which would be a non-sharable loss carryforward under sub. (9)(b) if it were a net business loss carryforward. Net capital loss carryovers that are otherwise non-sharable may be included in the aggregation under subd. 1. if they were carryovers of a subgroup as described in sub. (9)(e)1., but such losses may only be included in an amount not exceeding the net capital gain the subgroup would have if its amounts were not aggregated with those of the other combined group members.

3. Determine and apply the capital loss limitation under section 1211 of the internal revenue code for the combined group based on the aggregate amounts computed in subd. 1. The provisions of United States treasury regulations 1.1502-22 and 1.1502-23, and the regulations referenced therein, shall apply for this purpose, except that the separate return limitation year provisions are excluded and replaced with the provisions of this paragraph and except to the extent otherwise inconsistent with ss. 71.26 and 71.45, Stats., and the provisions of this section.

4. If the result is a net capital gain for the group, the net capital gain is apportioned to Wisconsin for the members in the same manner as all other combined unitary income as described in sub. (7), except that if the combined group is doing business solely in Wisconsin, the net capital gain is assigned to the members as described in sub. (8)(b). If the result is a net capital loss for the group, the net capital loss is assigned to the members that would have a net capital loss from the unitary business if their amounts were not aggregated with those of the other members of the combined group, in proportion to the amount of that net capital loss.

Examples: 1) Combined Group PQR consists of Member P, Member Q, and Member R. In Group PQR's unitary combination for 2010, P, Q, and R aggregate their short term capital gains and losses (including sharable capital loss carryovers), long-term capital gains and losses, section 1231 gains and losses, and involuntary conversions, and compute a total of $20,000 in net capital gain for Group PQR. P's Wisconsin apportionment percentage is 10%; Q's is 25%; and R's

is 50%. P's apportioned share of this net capital gain is $2,000 (= $20,000 x 10%), Q's apportioned share is $5,000 (= $20,000 x 25%) and R's apportioned share is $10,000 (= $20,000 x 50%).

2) Combined Group STU consists of Member S, Member T, and Member U. In the taxable year 2010, S, T, and U have the following capital gains and losses and section 1231 gains and losses attributable to the unitary business and subject to combination:

	Member S	Member T	Member U
Long term capital gain			$5,000
Short term capital loss	($12,000)	($6,000)	
Section 1231 gain/loss	($500)	$2,000	$1,500

When S, T, and U aggregate each class of capital gains and losses and section 1231 gains and losses, Group STU has a net capital loss of $10,000. However, if S, T, and U's capital gains and losses and section 1231 gains and losses were not aggregated with one another, S would have a net capital loss of $12,000 (its section 1231 loss would be treated as ordinary under section 1231(a)(2) of the internal revenue code), T would have a net capital loss of $4,000, and U would have a net capital gain of $6,500. Thus, the amount of Group STU's net capital loss that would be assigned to S is $7,500 (= ($12,000 / $16,000) x $10,000) and the amount that would be assigned to T is $2,500 (= ($4,000 / $16,000) x $10,000). None of the net capital loss would be assigned to U since it did not contribute to Group STU's net capital loss.

5. After applying subd. 4., each member computes its net capital gain or loss from separate entity items without considering capital loss carryover amounts. If the result is a net capital loss, the loss may not be deducted except as provided in subd. 6. If the result is a net capital gain, the member may subtract from that amount, subject to the capital loss limitation, any current year net capital loss from the unitary business as computed in subd. 4. and any available net capital loss carryovers, whether they are sharable or non-sharable. The current year net capital loss from the unitary business shall be considered used before the net capital loss carryovers. Any remaining carryover may be used as provided in subd. 6.

Example: Assume the same facts as Example 2 in subd. 4. Assume also that S has a $10,000 long term capital gain from separate entity items in 2010 and a net capital loss carryover of $3,000 which was incurred in 2008. Since the current year net capital loss from the unitary business is considered used before the net capital loss carryover, at the end of 2010 S would have a remaining 2008 net capital loss carryover of $500 (= $10,000 - $7,500 current year net capital loss from unitary business - $3,000 net capital loss carryover).

6. If a member has a share of net capital gain from the unitary business as computed in subd. 4., the member may use any available net capital loss, including current year net capital loss from separate entity items and net capital loss carryovers, to offset that net capital gain. If the group uses apportionment, the member uses the available net capital loss by claiming a deduction equal to the amount of the available net capital loss that does not exceed the group's net capital gain from the unitary business, multiplied by the member's apportionment percentage from the unitary combination. The current year net capital loss from separate entity items shall be considered used before the net capital loss carryovers.

Example: Assume the same facts as Example 1 in subd. 4. Assume that Q has a $5,000 long term capital gain from separate entity items and a net capital loss carryover of $6,000 which was incurred in 2008. Since the net capital loss carryover was incurred in a taxable year beginning before 2009, it is non-sharable and could not be used in computing the aggregate net capital gain or loss of the unitary business as described in subd. 1. However, Q may use the non-sharable loss carryover to offset its net capital gain from separate entity items. After doing this, Q has a $1,000 available net capital loss (= $5,000 - $6,000) to use against its share of the $20,000 net capital gain from the unitary business. To use the remaining carryover, Q may claim an additional capital loss deduction of $250 (= $1,000 available carryover x 25% apportionment percentage). After claiming this deduction, Q would have no remaining net capital loss carryover.

7. After each member applies subds. 4. to 6., as applicable, the member may carry back or carry forward any remaining net capital loss carryover as provided in section 1212 of the internal revenue code. The sharable carryovers available for use in the aggregation under subd. 1. are determined without regard to when any non-sharable carryovers were incurred and are applied in the order the underlying sharable loss was incurred. The carryovers available to offset the member's net capital gain under subds 5. and 6. are applied in the order the underlying loss was incurred. If the carryover available to offset the member's net capital gain under subds. 5. and 6. consists of both a sharable and non-sharable amount incurred

in the same taxable year, the carryover is applied from the sharable and non-sharable amounts on a pro rata basis according to the amount of each type of carryover available from that year.

Example: Member L is a member of Combined Group LM. Group LM uses a calendar year. At the beginning of 2012, L has the following available net capital loss carryovers:

Year Incurred	Sharable Carryover	Non-sharable Carryover
2008	--	$2,500
2009	$4,000	$0
2010	$0	$500
2011	$10,000	$2,000

Since the sharable net capital loss carryovers available for use in the aggregation under subd. 1. are determined without regard to when any non-sharable carryovers were incurred, The total sharable carryover that L may include in Group LM's computation of aggregate net capital gain or loss for the year 2012 is $14,000 (= $4,000 + $0 + $10,000). Assume $12,000 of this amount is absorbed in the aggregation. Since carryovers are applied in the order incurred, L's remaining sharable carryover of $2,000 is from its 2011 net capital loss. This carryover is available to L to offset against its net capital gain from separate entity items for 2012.

Assume L has a net capital gain from separate entity items of $4,000 and applies its available net capital loss carryover to offset this amount. Since carryovers are applied in the order incurred, $2,500 of the amount used is from its 2008 non-sharable carryover and $500 is from its 2010 non-sharable carryover. Since the remaining $1,000 carryover used is from 2011 where L has both a sharable and a non-sharable carryover, the amount of each carryover used is determined on a pro rata basis. Since L has $2,000 in sharable carryover from 2011 and $2,000 in non-sharable carryover from 2011, the remaining $1,000 carryover used is applied equally from the sharable and non-sharable carryovers. Thus, at the end of its 2012 taxable year, L has $1,500 in sharable carryovers and $1,500 in non-sharable carryovers available to carry forward or carry back.

8. If a member has sharable net capital loss carryovers, that member may choose not to use them in the aggregation under subd. 1. If more than one member includes sharable net capital loss carryovers in the aggregation under subd. 1., the amount of each member's carryover used shall be computed on a pro rata basis according to the amount of such carryover each member included in the aggregation.

Example: Combined Group QR consists of Member Q and Member R. Group QR is on a calendar year. For 2010, Q and R have the following amounts:

	Member Q	Member R
Sharable net capital loss carryover at beginning of year	($10,000)	($5,000)
Long term capital gain	$6,000	$2,000
Section 1231 gain/loss	($2,000)	$3,000

Assume the long term capital gains and section 1231 gains and losses are derived from Group QR's unitary business and are subject to combination. Before applying the carryovers, Group QR has an aggregate net capital gain of $9,000 (= $6,000 + $2,000 + ($3,000 - $2,000)). Both Q and R use their sharable net capital loss carryovers to offset this amount. The amount used from Q's sharable carryover is $6,000 (= $9,000 x ($10,000 / $15,000)) and the amount used from R's sharable carryover is $3,000 (= $9,000 x ($5,000 / $15,000)). After applying these carryovers, Q's remaining sharable carryover is $4,000 (= $10,000 - $6,000) and R's remaining sharable carryover is $2,000 (= $5,000 - $3,000).

(d) *Charitable contributions.* Compute the charitable contributions deduction limitation so that it applies to the combined group as a whole. Rules to determine the charitable contributions deduction limitation are as follows:

1. Compute the aggregate total deductions for charitable contributions for the taxable year, and any carryforwards thereof, for all combined group members to the extent those deductions relate to the unitary business and are attributable to items subject to combination.

2. Determine and apply the charitable contributions deduction under internal revenue code section 170, before any Wisconsin modifications under ss. 71.26 or 71.45, Stats., as if the combined group were a consolidated group for federal purposes. The provisions of United States treasury regulation 1.1502-24, and the regulations referenced therein, shall apply for this purpose, except to the extent otherwise inconsistent with ss. 71.26 and 71.45, Stats., and the provisions of this section.

Example: Combined Group GH consists of Member G and Member H. G incurred $5,000 in charitable contribution deductions relating to the unitary business in Year 1, while H incurred $15,000 of such deductions. Assume these deductions are attributable to income that is subject to combination. Assume the federal taxable income upon which the charitable contribution limitation (10% of adjusted taxable income) would be based is $50,000 for G and $30,000 for H. Applying U.S. Treas. Reg. § 1.1502-24 to Group GH in the manner described in this paragraph, Group GH would include a charitable contribution deduction of $8,000 (= lesser of ($5,000 + $15,000) or (($50,000 + $30,000) x 10%)) in its combined unitary income.

3. Any unused charitable contribution deduction after applying subd. 2. is assigned to the member that incurred the expense and is available to that member to offset its net income, if any, from separate entity items, subject to the limitation of section 170 of the internal revenue code. Any of a member's remaining unused charitable contribution may be carried over by that member and used in subsequent years, subject to the carryover period provided in section 170 of the internal revenue code. The unused carryover may either be shared in a subsequent combined report in the manner described in subd. 2. or may be used by that member specifically.

Example: Assume the same facts as in the example for subd. 2. After the computation of Group GH's combined unitary income for Year 1, the amount of unused charitable contribution deduction available to G would be $3,000 (= $12,000 unused deduction x ($5,000 / $20,000)) and the amount available to H would be $9,000 (= $12,000 x ($15,000 / $20,000)). Assume G has separate entity items in Year 1 and the adjusted federal taxable income from those items is $20,000. G may deduct $2,000 (= $20,000 x 10%) of its unused deduction against its income from separate entity items. Assume H does not have separate entity items in Year 1 and both G and H are in Group GH in Year 2. In Year 2, Group GH could include $10,000 of charitable contribution deduction carryover from Year 1 ($1,000 from G and $9,000 from H) in its combined unitary income, subject to the limitations of section 170 of the internal revenue code.

(e) *Dividends.* Eliminate dividends paid between members of the same combined group, but only if the dividends were paid from earnings and profits attributable to net income or loss that was includable in that group's combined unitary income in the current taxable year or a prior taxable year, and only to the extent the dividend does not exceed the payee's basis in the payer's stock. The following rules apply in determining the dividends that may be eliminated under this paragraph:

1. The elimination of dividends applies only to the extent that the dividends received deduction provided in ss. 71.26(3)(j) or 71.45(2)(a)8., Stats., does not apply.

2. For purposes of this paragraph, dividends are treated as paid out of current earnings and profits to the extent thereof. If the dividends paid exceed current earnings and profits, then the dividends are treated as paid out of earnings and profits accumulated in preceding years, beginning with the year closest to the current year (LIFO rule). With respect to an individual taxable year, dividends are treated as paid from all earnings and profits earned in that taxable year on a pro rata basis according to the proportion of net income that was included in the combined unitary income for that taxable year (pro rata rule). Earnings and profits are determined as provided in par. (g).

Note: See the examples under subds. 4. and 5. for application of the LIFO and pro rata rules.

3. A combined group member's earnings and profits attributable to the unitary business that were generated in its taxable years beginning before January 1, 2009, shall be deemed to be earnings and profits attributable to combined unitary income if the corresponding net income would have been included in the group's combined unitary income in those years had s. 71.255, Stats., been in effect and required combined reporting in those years.

4. To the extent that a dividend is paid out of earnings and profits that were generated while the payer was not, or in the case of subd. 3. would not have been, a member of the combined group, the dividend shall not be eliminated.

Example: Combined Group MN consists of Member M and Member N. The combined group was formed when Corporation M acquired 60% of Corporation N on June 1, 2009. Group MN uses a calendar year. During 2010, N paid a dividend to M of $500,000. N's current earnings and profits for 2010, before accounting for the distribution to M, are $100,000. N's earnings and profits attributable to its 2009 calendar year are $1,000,000, of which $50,000 (5% of the total) were earned while N was a member of Group MN. Assume N had no separate entity items while it was a member of Group MN. Also assume M did not deduct any foreign taxes attributable to the dividend and N has sufficient stock basis. Applying the LIFO and pro rata rules of subd. 2., the amount of dividend that qualifies for elimination from Group MN's combined unitary income in 2010 is $120,000 (= $100,000 + (5% x $400,000)). Under the pro rata rule, 95%, or $380,000, of dividends paid out of N's 2009 earnings and profits are considered to be paid from pre-acquisition earnings and profits.

5. To the extent that a dividend is paid out of earnings and profits that were generated in taxable years when the payer was, or in the case of subd. 3. would have been, a member of the combined group for all or a portion of the taxable year, any portion of the dividend attributable to separate entity items shall not be eliminated.

Example: Combined Group GH consists of Member G and Member H. G owns 55% of H. Group GH is on a calendar year and both G and H were members of the group for the entire taxable year. During 2010, H paid a dividend of $1,000,000 to G. H's current year earnings and profits are $2,500,000. Of these earnings and profits, $250,000 (10% of the total) is attributable to separate entity items of H. Assume G did not deduct any foreign taxes attributable to the dividend and H has sufficient stock basis. Applying the pro rata rule of subd. 2., the amount of dividend that qualifies for elimination from Group GH's combined unitary income is $900,000 (= $1,000,000 x 90%). Under the pro rata rule, 10%, or $100,000, of dividends paid out of H's current year earnings and profits are considered to be attributable to separate entity items.

6. The amount of dividends eliminated under this paragraph shall not exceed the payee's basis in stock of the payer as determined under par. (f).

7. The amount of dividends eliminated under this paragraph must be net of any taxes thereon paid to a foreign nation if those taxes were claimed as a deduction under ch. 71, Stats.

(f) *Stock basis adjustments.* A combined group member's basis in stock of a subsidiary that is a member of the same combined group shall be adjusted to reflect the subsidiary's distributions and items of income, gain, deduction and loss taken into account while the subsidiary was a member of the combined group. Except as provided below and except to the extent otherwise inconsistent with this section or ss. 71.26 or 71.45, Stats., the provisions of United States treasury regulation 1.1502-32, and the regulations referenced therein, shall apply in determining the amount of basis adjustment as if the Wisconsin combined group is a federal consolidated group:

1. A basis adjustment shall not be made for the subsidiary's distributions or items of income, gain, deduction, or loss taken into account for the subsidiary's taxable years beginning before January 1, 2009.

2. A basis adjustment shall not be made for the subsidiary's items of income, gain, deduction, or loss to the extent those items were not included in the group's combined unitary income. In the case of tax-exempt income, a basis adjustment shall not be made for such income to the extent the income is attributable to items that were not included in the combined unitary income.

3. An adjustment to reduce basis shall be made for the subsidiary's distributions to the extent those distributions are from earnings and profits attributable to items that were included in the group's combined unitary income, or from earnings and profits attributable to items deemed to be included in the group's combined unitary income for purposes of the dividend elimination under par. (e)3. For purposes of determining the amount of basis reduction under this subdivision, the LIFO and pro rata rules of par. (e)2. apply.

Example: Combined Group CD consists of Member C and Member D. C owns 65% of D. Group CD is on a calendar year. At the beginning of taxable year 2009, C's basis in the stock of D is $2,000,000. In the group's taxable year 2009, D has $100,000 of net income, all of which is included in Group CD's 2009 combined unitary income. During 2009, D pays a dividend of $300,000 to C. Assume the entire dividend from D to C qualifies for elimination under par.

(e)3. and is eliminated from Group CD's combined unitary income in 2009. C's basis in the stock of D as of the beginning of 2010 is $1,800,000 (= $2,000,000 + $100,000 – $300,000).

4. A basis adjustment shall not be attributed to a subsidiary from a lower-tier subsidiary's items of income, gain, deduction, or loss, except to the extent that the lower-tier subsidiary's items of income, gain, deduction, or loss originated in taxable years beginning on or after January 1, 2009 and were included in the combined unitary income of that same unitary business.

Example: Combined Group QRS consists of Member Q, Member R, and Member S. Q owns all the stock of R, and R owns of all the stock of S. Group QRS is on a calendar year. As of the beginning of 2009, Q had an unadjusted basis of $500,000 in R stock, which includes R's unadjusted basis of $200,000 in S stock under the rules of federal Treas. Reg. §1.1502-32. In the group's 2009 taxable year, R had a total of $80,000 of net income and S had a total of $150,000 of net income. Of S's net income, $20,000 was attributable to overseas operations, the income from which was not included in combined unitary income under the water's edge rules. Neither R nor S made any distributions in 2009. At the end of 2009, Q's basis in R stock is $710,000 (= $500,000 + $80,000 + $150,000 - $20,000). Q's basis in R stock cannot include any amounts attributed from S that are attributable to separate entity items.

(g) *Earnings and profits.* A combined group member's earnings and profits shall be adjusted to reflect the undistributed earnings and profits of any subsidiary that is a member of the same combined group, subject to the following rules and limitations:

1. Except as provided below and except to the extent otherwise inconsistent with this section or ss. 71.26 or 71.45, Stats., the provisions of United States treasury regulation 1.1502-33, and the regulations referenced therein, shall apply in determining earnings and profits as if the Wisconsin combined group is a federal consolidated group.

2. Undistributed earnings and profits attributed to a subsidiary of a combined group member from any lower-tier subsidiary may not be included in the combined group member's earnings and profits or its subsidiary's earnings and profits except to the extent the lower-tier subsidiary's earnings and profits are attributable to net income that was, or in the case of par. (e)3. would have been, included in the group's combined unitary income.

Example: Combined Group EFG consists of Member E, Member F, and Member G. E owns all the stock of F, and F owns of all the stock of G. Group EFG is on a calendar year. During the taxable year 2009, E has current year earnings and profits of $300,000 and F has current year earnings and profits of $500,000, both exclusive of any amounts attributed from subsidiaries. Assume these amounts are attributable entirely to items included in Group EFG's 2009 combined unitary income. G has current year earnings and profits of $400,000. However, $50,000 of this amount is attributable to overseas operations, the income from which was not included in combined unitary income under the water's edge rules. Assume none of the corporations made distributions in 2009. F's total current year earnings and profits are $850,000 (= $500,000 + ($400,000 - $50,000 attributed from G)), and E's current year earnings and profits are $1,150,000 (= $300,000 + $850,000 attributed from F).

(h) *Allocation of expenses and deductions.* Combined unitary income shall exclude any expenses or deductions that are directly or indirectly related to income that is not subject to combination. If any expense or amount otherwise deductible is indirectly related both to income subject to combination and income not subject to combination, a reasonable proportion of the expense or amount shall be allocated to each type of income, in light of all the facts and circumstances.

(7) APPORTIONMENT OF COMBINED UNITARY INCOME. A combined group is considered to be a single taxpayer for purposes of determining whether it is engaged in business both within and outside Wisconsin. For combined groups engaged in business both within and outside Wisconsin, the combined unitary income is apportioned to the combined group members as provided in s. 71.255(5), Stats. Under this section, each member's share of the combined unitary income is the product of the combined unitary income and the member's modified sales factor ratio. The following rules apply to this computation:

(a) *Numerator of modified sales factor.* 1. For combined group members required to use the sales factor as provided in s. 71.25(6) and (9), Stats., the numerator of the member's modified sales factor ratio is the numerator of its sales factor as determined under s. 71.25(9), Stats., and s. Tax 2.39 as if it were not a member of a combined group, except as provided in subd. 5. and pars. (c) to (e).

2. For combined group members that are insurers subject to tax under subchapter VII, Stats., the numerator of the member's modified sales factor is the numerator of its premiums factor as determined under s. 71.45(3)(a), Stats., as if it were not a member of a combined group, except as provided in subd. 5. and pars. (d) and (e).

3. For combined group members that are "financial organizations" as defined in s. 71.25(10), Stats., the numerator of the member's modified sales factor is the numerator of its receipts factor as determined under ss. Tax 2.49 or 2.495, as applicable, as if it were not a member of a combined group, except as provided in subd. 5. and pars. (c) to (e).

4. For combined group members that are required to apportion their income using more than one factor under s. 71.25(10), Stats., and ss. Tax 2.46, 2.47, 2.475, 2.48, 2.50, or 2.502, the numerator of the member's modified sales factor is determined as provided in par. (g).

5. The numerator of the modified sales factor shall not include sales, premiums, or receipts which are not included in the combined unitary income as computed in sub. (6).

(b) *Denominator of modified sales factor.* The denominator of a combined group member's modified sales factor ratio is the sum of the separate company denominators of each combined group member, so that each member of the combined group has the same modified sales factor denominator. Each combined group member's separate company denominator is determined as follows:

1. For combined group members required to use the sales factor as provided in s. 71.25(6) and (9), Stats., the member's separate company denominator for purposes of the modified sales factor is the denominator of its sales factor as determined under s. 71.25(9), Stats., and s. Tax 2.39 as if it were not a member of a combined group, except as provided in subd. 5. and pars. (d) and (e).

2. For combined group members that are insurers subject to tax under subchapter VII, Stats., the member's separate company denominator for purposes of the modified sales factor is the denominator of its premiums factor as determined under s. 71.45(3)(a), Stats., as if it were not a member of a combined group, except as provided in subd. 5. and pars. (d) and (e).

3. For combined group members that are "financial organizations" as defined in s. 71.25(10), Stats., the member's separate company denominator for purposes of the modified sales factor is the denominator of its receipts factor as determined under ss. Tax 2.49 or 2.495, as applicable, as if it were not a member of a combined group, except as provided in subd. 5. and pars. (d) and (e).

4. For combined group members that are required to apportion their income using more than one factor under s. 71.25(10), Stats., and ss. Tax 2.46, 2.47, 2.475, 2.48, 2.50, or 2.502, the member's separate company denominator for purposes of the modified sales factor is determined as provided in par. (g).

5. The separate company denominator for purposes of the modified sales factor shall not include sales, premiums, or receipts which are not included in the combined unitary income as computed under sub. (6).

(c) *Throwback sales.* If a combined group member's sale of tangible personal property is destined for a state in which any member of the combined group has nexus under the standards set forth in s. Tax 2.82, and that nexus relates to the unitary business, the sale shall not be included in the numerator of the member's modified sales factor.

(d) *Intercompany transactions.* 1. Any transaction between members of the same combined group shall be excluded from the numerator and denominator of the modified sales factor. However, if the seller subsequently recognizes income or loss from the intercompany transaction under the provisions of s. 71.255(4)(g), Stats., and sub. (6)(b), the seller's modified sales factor shall include any factors corresponding to that income or loss in the year it recognizes the income or loss.

2. If a combined group member sells an item or service to another combined group member and the purchaser subsequently resells it to a third party outside of the combined group, the situs of the sale between the combined group members and the sale from the purchasing member to the third party shall both be determined based on the situs of the sale from the purchasing member to the third party, and the purchasing member shall exclude from the numerator and

denominator of the modified sales factor the amount the selling member already included under subd. 1. attributable to the item or service that was resold.

Example: Combined Group YZ consists of Member Y and Member Z. Group YZ is on a calendar year. On December 30, 2009, Y sells a widget with a cost of $400 to Z, for $600. Y ships the widget to Z's warehouse in Wisconsin. On January 30, 2010, Z resells the widget to Q, an unrelated third party, for $700. Z ships the widget to Q's headquarters in Illinois. Assume both the sale by Y and the sale by Z are subject to combination, and assume that Z has nexus in Illinois. In 2009, Y did not recognize any gain on the sale to Z because the gain was deferred under the provisions of s. 71.255(4)(g), Stats., and sub. (6)(b). Since the gain on the sale was not recognized, Y cannot include the $600 sale in its apportionment factors for 2009. In 2010, the year the widget was resold by Z, Y must include its $200 of gain on the sale to Z (= $600 - $400) in combined unitary income. Y must also include the sale amount of $600 in the modified sales factor denominator for 2010. Z must include its $100 gain on the sale to Q (= $700 - $600) in combined unitary income for 2010. However, since $600 of Z's sales price has already been included in the combined group's modified sales factor, Z may only include $100 of the sale amount in the modified sales factor denominator. Neither Y nor Z include these amounts in their modified sales factor numerators since both sales have a situs in Illinois where Z has nexus. Under the provisions of par. (c), Z's nexus in Illinois applies to both itself and Y for purposes of applying the throwback rule.

3. If an item or service is sold between more than two combined group members before it is sold to a customer outside of the combined group, the situs of all such intercompany sales is the situs of the ultimate sale to the customer outside of the combined group, and each purchasing combined group member shall exclude from the numerator and denominator of the modified sales factor the amount its selling member already included under subd. 1.

(e) *Pass-through entities.* A combined group member's numerator and denominator for purposes of the modified sales factor generally includes the apportionment factors of pass-through entities owned directly or indirectly by the member, in proportion to the combined group member's distributive share of the pass-through entity's net income or loss included in the combined unitary income. However, a combined group member's modified sales factor shall not include apportionment factors of a real estate investment trust, regulated investment company, real estate mortgage investment conduit, or financial asset securitization investment trust. Additionally, subds. 1. and 2. apply in order to avoid duplication. For purposes of subds. 1. and 2., "sale" includes sales as defined in s. 71.25(9), Stats., premiums under s. 71.45(3)(a), Stats., or receipts under ss. Tax 2.49 or 2.495, as applicable, which would otherwise be included in a combined group member's modified sales factor.

1. If a sale is made by a combined group member to a pass-through entity which is more than 50 percent owned, directly or indirectly, by members of the combined group as provided in subd. 3., the selling member must subtract from its modified sales factor numerator and denominator, as applicable, an amount equal to the gross receipts of the sale multiplied by the sum of all combined group members' interests in the pass-through entity as of the date of the sale. This subdivision applies to the extent the gross receipts of the sale are otherwise includable in combined unitary income. For purposes of this subdivision, a combined group member's interest in the pass-through entity as of the date of the sale means the percentage of the pass-through entity's income or loss that is allocable to the member in the taxable year of the sale.

Examples: 1) Combined Group LM consists of Member L and Member M. L owns a 40% interest in Partnership P. M owns a 60% interest in Partnership P. On March 1, 2010, L sells a widget to Partnership P for $10,000, and this sale is includable in Group LM's combined unitary income. In its computation of apportionment factors for 2010, L must subtract an amount of $10,000 (= $10,000 x (40% + 60%)) from the modified sales factor denominator and, if applicable, from its numerator.

2) Assume the same facts as Example 1, except that Member L owns a 25% interest and M owns a 50% interest in Partnership P. In its computation of apportionment factors for 2010, L must subtract an amount of $7,500 (= $10,000 x (25% + 50%)) from the modified sales factor denominator and, if applicable, from its numerator.

2. If a sale is made by a pass-through entity to a combined group member and more than 50 percent of the pass-through entity is directly or indirectly owned by members of the combined group as provided in subd. 3., each member with an interest in such pass-through entity must subtract from its modified sales factor numerator and denominator, as applicable, any amount attributable to the sale. This subdivision applies to the extent the gross receipts of the sale are otherwise includable in combined unitary income.

Example: Combined Group ST consists of Member S and Member T. S owns a 20% interest in Partnership R. T owns an 80% interest in Partnership R. On October 1, 2010, Partnership R sells a widget to S for $20,000, and this sale is includable in Group ST's combined unitary income. In its computation of apportionment factors for 2011, S must subtract an amount of $4,000 (= $20,000 x 20%) from its sales factor denominator and, if applicable, from its numerator. Similarly, T must subtract an amount of $16,000 (= $20,000 x 80%) from its sales factor denominator and, if applicable, from its numerator.

3. For purposes of subds. 1. and 2., a pass-through entity is owned more than 50 percent by combined group members if the aggregate amount of the combined group members' interests in the pass-through entity, without regard to any agreement to allocate gains or losses on a basis other than their capital interests, is more than 50 percent, or the combined group members taken as a whole have more than 50 percent of the management rights of the pass-through entity, as evidenced by the terms of the agreement under which the pass-through entity was formed, voting rights, provisions of state or federal law, or otherwise.

(f) *Special rules for zeroes and negative numbers in factors.* This paragraph applies the special rules in ss. 71.25(6m) and 71.45(3e), Stats., to combined group members as follows:

1. If both the numerator and denominator of a member's modified sales factor are zero, none of the combined unitary income shall be apportioned to the member. The member's separate company denominator has no effect on this determination.

2. If the numerator of a member's modified sales factor is a negative number, none of the combined unitary income shall be apportioned to the member. The member's separate company denominator has no effect on this determination.

3. If the numerator of a member's modified sales factor is a positive number and the denominator is a negative number or zero, all of the combined unitary income shall be apportioned to the member. The member's separate company denominator has no effect on this determination. If this subdivision would result in apportioning all of the combined unitary income to more than one member, the combined unitary income shall be apportioned to the members having positive modified sales factor numerators in proportion to the amounts of such numerators.

Example: Combined Group XY consists of Member X and Member Y. In its taxable year 2009, Group XY has combined unitary income of $50,000. X and Y have the following apportionment factors:

	Member X	Member Y
Modified Sales Factor Numerator	$5,000	$15,000
Separate Company Denominator	($10,000)	$5,000

The modified sales factor denominator, or sum of the separate company denominators, is ($5,000). Under subd. 3., the amount of combined unitary income that would be apportioned to X is $12,500 (= $50,000 x ($5,000 / $20,000)). The combined unitary income that would be apportioned to Y is $37,500 (= $50,000 x ($15,000 / $20,000)).

(g) *Multiple factor formulas.* If a combined group member is required under s. 71.25(10), Stats., to use an apportionment formula prescribed in ss. Tax 2.46, 2.47, 2.475, 2.48, 2.50, or 2.502, the member's modified sales factor is computed as follows:

1. The numerator of the modified sales factor is the product of the member's apportionment percentage computed under ss. Tax 2.46, 2.47, 2.475, 2.48, 2.50, or 2.502, as applicable, as if the member were not a member of a combined group except as provided in subds. 3. to 5., and the member's separate company denominator determined in subd. 2.

2. Except as provided in subds. 3. to 5., the member's separate company denominator for purposes of the modified sales factor is the member's total company sales that would be includable in the sales factor computed under s. 71.25(9), Stats., as if the member were required to use the sales factor and were not a member of a combined group.

3. Neither the numerator nor denominator shall include amounts that are not included in or directly related to income included in the combined unitary income as computed under sub. (6).

4. Intercompany transactions shall be excluded or recognized in the numerator and denominator, as applicable, in the manner described in par. (d).

5. To the extent the computation in this paragraph involves the sales factor as provided in s. 71.25(9), Stats., the provisions of pars. (c) and (e) apply.

(h) *Alternative apportionment under s. Tax 2.395.* The provisions of s. Tax 2.395 may apply to combined group members. The determination of whether an alternative apportionment method may be used is made for each corporation within the combined group rather than for the combined group itself. If the alternative apportionment method employed under s. Tax 2.395 is a formula that includes multiple factors, that corporation must compute its modified sales factor in the manner described in par. (g).

(i) *Alternative apportionment for specialized industries.* Notwithstanding the provisions of s. Tax 2.395, a qualifying combined group may petition the department to use an alternative apportionment method, as provided in s. Tax 2.64.

(8) INCOME COMPUTATION FOR GROUPS DOING BUSINESS SOLELY IN WISCONSIN. For combined groups that are engaged in business solely in Wisconsin, and therefore not eligible to use apportionment, each member's net income includable in the unitary combination is generally determined on a separate entity basis and adjusted to reflect the member's status as a combined group member. The income computed in this manner is considered the member's share of the combined unitary income. The adjustments described in sub. (6) apply to members of a combined group doing business solely in Wisconsin, except that the modifications in pars. (a) to (d) apply to such a group:

(a) *Intercompany transactions.* Intercompany transactions that consist of interest or other expenses paid, accrued, or incurred by one member to another are disregarded so that they neither increase nor decrease a member's net income or loss. Gain or loss from all other intercompany transactions is deferred and recognized using the provisions of United States treasury regulation 1.1502-13 and sub. (6)(b) as if the combined group were a federal consolidated group. This paragraph does not apply to intercompany transactions which occurred in taxable years beginning before January 1, 2009 or to intercompany transactions where the income, expense, gain, or loss would not otherwise be subject to combination.

(b) *Capital gains and losses.* 1. The net capital gain or loss, after applying any sharable net capital loss carryover, is first determined for the combined group as a whole in the manner described in sub. (6)(c)1. to 3. If the result is a net capital gain for the group, the net capital gain is assigned to the members that would have a net capital gain from the unitary business if they were not members of the combined group, in proportion to the amount of that net capital gain. If the result is a net capital loss for the group, the net capital loss is assigned to the members that would have a net capital loss from the unitary business if they were not members of the combined group, in proportion to the amount of that net capital loss.

Note: See Example 2 under sub. (6)(c)4. for an example of this assignment method.

2. After applying subd. 1., each member computes its net capital gain or loss from separate entity items and applies the provisions of sub. (6)(b)5. to 7.,except that the provisions of sub. (6)(c)6. relating to apportionment do not apply.

(c) *Basis adjustments.* A combined group member's basis in stock of a subsidiary that is a member of the same combined group shall be adjusted in the manner prescribed in sub. (6)(f). Intercompany interest and other expenses shall be included in these adjustments, even if those transactions were disregarded in the computation of the member's income for the taxable year as provided in par. (a).

(d) *Earnings and profits.* A combined group member's earnings and profits shall be adjusted to reflect the undistributed earnings and profits of a subsidiary that is a member of the same combined group in the manner prescribed in sub. (6)(g). Intercompany interest and other expenses shall be included in these adjustments, even if those transactions were disregarded in the computation of the member's income for the taxable year as provided in par. (a).

(9) NET BUSINESS LOSSES. A combined group member may carry forward its net business loss as provided in ss. 71.26(4) and 71.45(4), Stats. A net business loss carryforward is an attribute of the separate corporation rather than of the

combined group. However, s. 71.255(6)(b), Stats., provides that a combined group member may share all or a portion of its net business loss carryforward with the other members of its combined group if certain conditions are met. This subsection explains which net business loss carryforwards are sharable, how to compute the sharable amount, and how to apply the shared losses. The following rules apply:

(a) *Sharable loss carryforwards.* A combined group member may share its net business loss carryforward with other combined group members to the extent that all of the following conditions are met:

1. The net business loss originated in a taxable year beginning on or after January 1, 2009 and is attributable to combined unitary income included in a combined report.

2. The member originally computed the net business loss in the combined report for the same combined group as the combined group that will use the shared loss carryforward, regardless of whether new corporations have joined or left the combined group in the intervening years.

3. The member is still a member of the combined group described in subd. 2. for the year the loss carryforward will be shared.

(b) *Non-sharable loss carryforwards.* A combined group member's net business loss carryforward that cannot be shared with other combined group members includes amounts attributable to:

1. Net business losses that originated in a taxable year beginning before January 1, 2009.

2. Net business losses attributable to separate entity items.

3. Net business losses attributable to a different unitary business.

(c) *Order of carryforwards.* A combined group member shall apply net business loss carryforwards in the order that the underlying net business loss was incurred. If the net business loss carryforward to be used consists of both a sharable amount and a non-sharable amount incurred in the same taxable year, the amount of sharable and non-sharable carryforward used shall be determined on a pro rata basis according to the amount of each type of carryforward available from that year.

Example: Combined Group EFG consists of Member E, Member F, and Member G. E has the following loss carryforwards:

Year Incurred	Sharable Carryforward	Non-sharable Carryforward
2008	--	($10,000)
2009	($6,000)	($2,000)

In 2010, E's share of combined unitary income plus its separate entity items equal $14,000. After using its carryforwards to offset this income, E has $4,000 of remaining net business loss carryforward (= ($10,000) + ($6,000) + ($2,000) + $14,000). Of this amount, a portion is a sharable carryforward that may be applied against F and G's shares of combined unitary income in the manner described in par. (d). Since loss carryforwards are applied in the order incurred, the $10,000 carryforward from 2008 is used in its entirety, and $4,000 of the 2009 carryforward is used. The portion of E's remaining carryforward from 2009 that is sharable is $3,000 (= ($4,000) x ($6,000 / $8,000)) and the portion that is non-sharable is $1,000 (= ($4,000) x ($2,000 / $8,000)).

(d) *Method of sharing.* The amount of net business loss carryforward eligible for sharing shall be computed and assigned as follows:

1. Each combined group member shall first apply its total available net business loss carryforward against its total Wisconsin income as computed under sub. (5)(a) to (g), including net income or loss attributable to separate entity items. A combined group member's net business loss carryforward shall be considered used against its net income from separate entity items before its share of combined unitary income.

2. Each member shall then separate any remaining net business loss carryforward into the sharable amount and the non-sharable amount, as applicable, using the ordering rules in par. (c). The sharable net business loss carryforward amounts for each combined group member shall then be aggregated, except that any combined group member that elects not to share its sharable amount as provided in par. (h) shall not include any amount in the aggregate sharable amount.

3. Except as provided in par. (g), relating to insurance companies, the aggregate sharable net business loss carryforward shall be assigned to each combined group member in proportion to its share of combined unitary income as computed in subs. (6) to (8), net of any losses from separate entity items or loss carryforwards already applied to such income. The sharable amount may only be assigned to a member to the extent the member's share of combined unitary income has not already been offset by losses taken into account under subd. 1. No amount shall be assigned to a combined group member whose share of combined unitary income, net of any losses already applied by the member under subd. 1., is zero or less.

4. Any remaining sharable amount remains an attribute of the corporation that originally incurred the loss. The aggregate sharable amount used under subd. 3. shall be considered used proportionately from the sharable net business loss carryforwards of the corporations which contributed to the aggregate sharable amount.

Example: Combined Group ABCD consists of Member A, Member B, Member C, and Member D. The corporations have the following net business loss carryforwards and net income amounts in 2010:

	Member A	Member B	Member C	Member D
Net business loss carryforward – 1/1/2010	($28,000)	($24,000)	($1,000)	$0
Share of combined unitary income	$3,000	$10,000	$20,000	$20,000
Net income from separate entity items	$1,000	($2,000)	$3,000	($15,000)
Remaining net business loss carryforward	($24,000)	($16,000)	$0	$0

Assume all of A and B's net business loss carryforwards are sharable. The aggregate sharable amount is $40,000 (= $24,000 + $16,000). This amount may be allocated to C and D based upon their respective shares of combined unitary income after applying any losses from separate entity items. C's such amount is $20,000 (its $1,000 carryforward is considered used against its $3,000 net income from separate entity items before its share of combined unitary income) and D's such amount is $5,000 (= $20,000 - $15,000). The aggregate sharable amount exceeds the sum of C and D's adjusted shares of the combined unitary income, which is $25,000 (= $20,000 + $5,000). Thus, the entire remainder of C and D's adjusted share of combined unitary income is offset by the aggregate sharable amount.

After the aggregate sharable amount is applied, the remaining aggregate sharable amount is $15,000 (= $40,000 - $25,000). Since the remaining sharable amount remains an attribute of the corporation that originally incurred the loss, at the end of 2010, A would have $9,000 (= $15,000 x ($24,000 / $40,000)) in remaining net business loss carryforward, and B would have $6,000 (= $15,000 x ($16,000 / $40,000)) in remaining net business loss carryforward.

(e) *Departing combined group members.* Except as provided in subds. 1. and 2., if a corporation leaves a combined group or is no longer eligible to be a combined group member, the corporation's remaining net business loss carryforward may not be shared with any other combined groups but shall be available only to that corporation. The following exceptions apply:

1. If a subgroup of two or more corporations leaves a combined group on the same date and immediately thereafter the corporations become a separate combined group or together become members of a new combined group, those corporations may share their remaining sharable net business loss carryforwards attributable to the former combined group with one another. For purposes of the computations in par. (d), the new combined group's combined unitary income shall be used in place of the former combined group's combined unitary income. This subdivision also applies to combined groups that merge to become a new combined group by operation of the controlled group election as described in s. Tax 2.63(2)(c).

2. If a corporation leaves a combined group or is no longer eligible to be a combined group member, but subsequently rejoins the combined group, the corporation may share its net business loss carryforward with that combined group to the extent the carryforward otherwise qualifies as a sharable loss carryforward under par. (a).

(f) *New combined group members.* If a new member joins the combined group or is formed within the combined group, such member may use the net business loss carryforwards shared by other combined group members in the same manner as described in this subsection, even if those losses originated before the new members were part of the group.

(g) *Special rules for insurance companies.* Under s. 71.45(4), Stats., the net business loss of an insurance company cannot include the dividends received deduction provided in s. 71.26(3)(j), Stats. Further, an insurance company may not use net business loss carryforwards in cases where its franchise or income tax liability is limited by 2 percent of its gross premiums as provided in s. 71.46(3), Stats. Therefore, the following rules apply:

1. For purposes of applying s. 71.45(4), Stats., if a dividend qualified for both the dividends received deduction under s. 71.26(3)(j), Stats., and the elimination of dividends under sub. (6)(e), the dividend is considered to be eliminated under sub. (6)(e) rather than deducted under s. 71.26(3)(j), Stats.

2. If an insurance company is a member of a combined group that is engaged in business both within and outside Wisconsin and has a net business loss, the dividends received deduction that must be added back to that loss includes the insurance company's apportioned share of the total dividends received deduction which was deducted from the combined unitary income under s. 71.26(3)(j), Stats., regardless of whether the insurance company was the combined group member which received the dividend.

3. If an insurance company is a combined group member and its tax liability measured by its total Wisconsin net income as provided in sub. (5), including any net business loss carryforwards shared by other combined group members, exceeds 2 percent of its gross premiums as defined in s. 76.62, Stats., plus 7.9 percent of the income described in sub. (5)(f), its tax liability shall be limited to 2 percent of such gross premiums plus 7.9 percent of the income described in sub. (5)(f). If the insurance company's tax liability is limited in this manner, none of its business loss carryforwards may be shared with any other combined group members, and if the group is otherwise sharing loss carryforwards, no loss carryforwards may be assigned to the insurance company.

(h) *Elections.* 1. Although a combined group member is entitled to the benefit of a net business loss carryforward, the member may elect not to use a portion or any of the available net business loss carryforward for a taxable year. Such an election does not reduce the amount of carryforward available for the following taxable year nor suspend the carryforward period provided in ss. 71.26(4) and 71.45(4), Stats.

2. A combined group member may also elect not to share a portion or any of its sharable net business loss carryforward with other combined group members. However, if the corporation shares any part of its sharable net business loss carryforward, the shared amount must be divided among all members in the manner prescribed in this subsection, except as otherwise provided in pars. (d), (e)1., and (g)3.

(i) *Applicability of internal revenue code.* 1. Notwithstanding the provisions of this subsection, the total amount of net business loss carryforward that may be used by a combined group member or shared with other combined group members for a taxable year is limited by section 382 of the internal revenue code as provided in s. 71.26(3)(n), Stats. Section 382 of the internal revenue code shall be applied without regard to the federal consolidated return regulations under section 1502 of the internal revenue code.

2. If a combined group member is acquired by another combined group member, section 381 of the internal revenue code controls whether the acquiring corporation may succeed to the target corporation's net business loss carryforwards. Wisconsin follows section 381 of the internal revenue code, but modifies it in s. 71.26(3)(n), Stats., so that it applies to Wisconsin net business loss carryforwards instead of federal net operating loss carryovers. If the acquirer succeeds to the target corporation's net business loss carryforwards, such carryforwards shall be treated as originally incurred by the acquiring corporation and shall maintain their character as sharable or non-sharable.

3. The separate return limitation year provisions of the federal regulations under section 1502 of the internal revenue code do not apply to net business loss carryforwards. The provisions of this subsection apply in place of such limitations.

(10) CREDITS. A credit is an attribute of the separate corporation rather than of the combined group, and credits are computed for each corporation separately. However, s. 71.255(6)(c), Stats., provides that a combined group member may share all or a portion of its research credits with the other members of the combined group. For purposes of this subsection, the term "research credit" means only the research expense credit under ss. 71.28(4) or 71.47(4), Stats., and the research facilities credit under ss. 71.28(5) or 71.47(5), Stats. This subsection explains how credits are computed and applied as well as the special rules that apply to research credits.

(a) *Nonrefundable credits other than research credits.* A combined group member's nonrefundable credits other than research credits, including carryforwards of such credits, may only be used by that combined group member to offset the tax liability attributable to its own taxable income as computed under sub. (5).

(b) *Refundable credits.* Any refundable credits computed by a combined group member shall be claimed on the combined return and refunded to the designated agent to the extent not used to offset the total tax liability reported on the combined return.

(c) *Sharing of research credits*. If a combined group member computes a research credit, or has a carryforward thereof, the member may, after using the available credit to offset its own tax liability, share a portion or all of the remaining credit with the other members. For purposes of determining the sharable amount, the provisions of sub. (9)(e) and (f) apply to available research credits in the same manner as they apply to net business loss carryforwards. Research credit carryforwards incurred in taxable years beginning before January 1, 2009 are sharable to the extent the corporation with the credits would have been a member of the combined group had s. 71.255, Stats., been in effect and required combined reporting in those years. The method of sharing these credits is as follows:

1. Each combined group member shall first apply its total available credits, including its research credits, against its gross tax liability, including its tax liability attributable to separate entity items. A combined group member's available credits shall be considered used against its tax liability from separate entity items before its tax liability from its share of combined unitary income.

2. Each member shall then separate any remaining available research credit into the sharable and non-sharable amount, as applicable. The amount of available research credit for the current taxable year is considered used before any research credit carryforwards. The ordering rules provided in sub. (9)(c), relating to net business loss carryforwards, also apply to research credit carryforwards. The sharable research credits for each combined group member shall then be aggregated, except that any combined group member that elects not to share its sharable amount shall not include any amount in the aggregate sharable amount.

3. The sharable amount shall be assigned to each combined group member in proportion to its tax liability from its share of combined unitary income. The sharable amount may only be assigned to a member to the extent the member's tax liability from combined unitary income has not already been offset by other credits and carryforwards applied by that member under subd. 1. No amount shall be assigned to a combined group whose tax liability from combined unitary income has been fully offset by other credits.

4. Any remaining sharable amount remains an attribute of the corporation that originally generated the credit. The aggregate sharable amount used under subd. 3. shall be considered used proportionately from the sharable research credits of the corporations which contributed to the aggregate sharable amount.

Example: Combined Group FGH consists of Member F, Member G, and Member H. F, G, and H have the following amounts in 2010:

	Member F	Member G	Member H
Current year research expense credit	($3,000)		
Current year economic development credit			($17,000)
Research expense credit carryforward	($20,000)	(16,000)	
Tax liability from combined unitary income	$8,000	$5,000	$20,000

Tax liability from separate entity items	_____	$1,000	$2,000
Net tax	$0	$0	$5,000
Remaining available research expense credit	($15,000)	($10,000)	

Assume all of the research expense credit carryforward is sharable. The aggregate sharable amount is $25,000 (= $15,000 + $10,000). This amount may be assigned to H to the extent of its tax liability from its share of the combined unitary income after applying its own credits. After H applies its own credits, the remaining tax liability from combined unitary income is $5,000 (= ($17,000) + $2,000 + $20,000; its $17,000 economic development credit is applied against tax liability from separate entity items before tax liability from combined unitary items). Since this amount is less than the aggregate sharable amount, the entire remainder of H's tax liability from combined unitary income ($5,000) is offset by the aggregate sharable amount.

After the aggregate sharable amount is applied, the remaining aggregate sharable amount is $20,000 (= $25,000 - $5,000). Since the remaining sharable amount remains an attribute of the corporation that originally generated the credit, at the end of 2010, F would have $12,000 (= $20,000 x ($15,000 / $25,000)) in remaining research credit carryforward, and G would have $8,000 (= $20,000 x ($10,000 / $25,000)) in remaining research credit carryforward.

5. The provisions of sub. (9)(h), as they relate to elections applicable to net business loss carryforwards, apply also to available research credits under this paragraph.

(d) *Exception for funded research.* If a combined group member incurs expenses that are otherwise qualified research expenses under section 41(d) of the internal revenue code but for the fact that the research is funded by another combined group member, such expenses shall be considered qualified research expenses of the combined group member performing the research, and the reimbursement from the combined group member funding the research shall not be considered a qualified research expense of the funding member. Regardless of where the funding member is located, the research must be performed in Wisconsin to qualify for the research credit for Wisconsin purposes.

(e) *Applicability of internal revenue code.* The provisions of sub. (9)(i), as they relate to net business loss carryforwards, also apply to carryforwards of credits under this subsection.

Note: Section Tax 2.61 interprets s. 71.255, Stats.

Cross Reference: See s. Tax 2.60 for definitions that relate to this section.

Tax 2.62 Unitary Business. (1) SCOPE. Section 71.255(2)(a), Stats., provides that a corporation engaged in a unitary business with one or more other corporations in the same commonly controlled group is generally required to determine its share of income from that unitary business using a combined report. Section 71.255(1)(n), Stats., defines "unitary business." The purpose of this section is to provide further interpretation of the meaning of "unitary business."

(2) GENERAL. A unitary business is a single, commonly controlled economic enterprise for which the components of the enterprise are sufficiently interdependent, integrated, and interrelated through their activities to such a degree that if the enterprise is doing business both within and outside a state, the state is permitted under the U. S. Constitution to tax a fairly apportioned share of the total net income of the enterprise.

(a) *Commonly controlled.* A unitary business may consist of a single entity or a group of 2 or more related entities, including entities treated as corporations, tax-option corporations, partnerships, limited liability companies, sole proprietorships, estates, and trusts. 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:

1. The entities are related under the provisions of section 267 of the internal revenue code which disallow losses on sales between related persons. By reference, this includes the rules in 707(b) of the internal revenue code, relating to partnerships.

2. The entities are related under section 1563 of the internal revenue code, which defines a "controlled group of corporations" for federal income tax purposes.

3. The entities are corporations in the same "commonly controlled group" for Wisconsin purposes. "Commonly controlled group" has the meaning given in s. 71.255(1)(c), Stats., as further interpreted by s. Tax 2.61(3).

(b) *Components of enterprise.* The components of a commonly controlled economic enterprise may consist either of divisions of a single entity or of multiple entities, or both. For purposes of this section, the term "participants" is used to describe these components of an economic enterprise.

(c) *Sufficiently interdependent, integrated, and interrelated.* 1. In general, the participants in a commonly controlled economic enterprise are considered a unitary business if their activities generate a synergy and mutual benefit that produces a sharing or exchange of value among them and a significant flow of value to the separate parts. Subsection (3) presents indicators that such sharing or exchange and flow of value is present.

2. The participants in a commonly controlled economic enterprise may also be considered a unitary business if there is unity of operation and use, as further explained in sub. (4).

3. The definition of "unitary business" shall be construed to the broadest extent permitted by the U.S. Constitution. Thus, case law provides additional guidance to determine whether a unitary business exists. Subsection (5) presents factors that have been considered by the U.S. Supreme Court to be determinative of a unitary business.

(d) *Fairly apportioned.* If a unitary business has nexus in Wisconsin and is doing business both within and outside Wisconsin, an apportioned share of the unitary business's net income is taxable by Wisconsin under the rules of this paragraph. If a unitary business is doing business only in Wisconsin, no apportionment applies and all of the unitary business's income is taxable by Wisconsin unless specifically exempt. The following rules apply to the apportionment of income of a unitary business:

1. For any participant in the unitary business that is not a member of a commonly controlled group of corporations as provided in s. Tax 2.61(3), the participant's income from the unitary business is generally apportioned in the manner provided by ss. Tax 2.39, 2.395, 2.45, 2.46, 2.47, 2.475, 2.48, 2.49, 2.495, 2.50, or 2.502, as applicable. However, the participant may be required to apportion its income under the combined reporting rules provided in s. Tax 2.61 if certain conditions apply, as further explained in s. Tax 2.61(2)(f).

2. For any participant in the unitary business that is a member of a commonly controlled group of corporations as provided in s. Tax 2.61(3), the participant's income from the unitary business must be apportioned under the combined reporting rules provided in s. Tax 2.61.

3. A corporation that is engaged in the unitary business may have both apportionable income and nonapportionable income, as provided in s. 71.25(5), Stats.

(e) *Members of unitary business that are not in combined group.* It is possible that one or more members of a unitary business may not be members of a combined group. Members of a unitary business that may not be members of a combined group include the following:

1. Individuals or entities that are considered "pass-through entities" for purposes of combined reporting under s. 71.255(1)(m), Stats. This includes partnerships, limited liability companies treated as partnerships, tax-option corporations, estates, trusts, real estate investment trusts, regulated investment companies, real estate mortgage investment conduits, and financial asset securitization investment trusts.

2. Corporations whose net income and apportionment factors are not subject to combination under the water's edge rules of s. Tax 2.61(4).

3. Corporations that are related under the rules of sections 267 or 1563 of the internal revenue code but are not in a "commonly controlled group" as provided under s. Tax 2.61(3).

(f) *Members of combined group that are not in unitary business.* A combined group may include corporations that are not engaged in a unitary business if the combined group's designated agent has properly made the controlled group election as provided in s. Tax 2.63.

(3) SHARING, EXCHANGE, AND FLOW OF VALUE. (a) *General.* Participants 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:

1. The participants in the enterprise contribute or are expected to contribute in a nontrivial way to each other's profitability.

2. Each participant in the enterprise is either dependent on, or is depended upon by, one or more other participants in the enterprise for achieving one or more nontrivial business objectives.

3. The economic enterprise offers one or more participants some economies of scale or economies of scope that benefit the enterprise.

4. The prices charged on transactions between participants in the enterprise are inconsistent with the arms-length principle. However, if the prices charged on such transactions are consistent with the arms-length principle, that fact does not negate in any way the existence of a unitary business (*Exxon Corp. v. Dept of Revenue of Wisconsin*, 447 U.S. 207, 100 S. Ct. 2109 (1980)).

(b) *Evidence of flow of value.* Some activities between participants that would evidence a flow of value between them include, but are not limited to, the following:

1. Assisting in acquisition of assets.

2. Assisting with filling personnel needs.

3. Lending funds, guaranteeing loans, or pledging assets.

4. Interplay in the area of corporate expansion, including but not limited to common future planning or development of the enterprise.

5. Providing technical assistance, general operational guidance, or overall operational strategic advice.

6. Supervising.

7. Sharing use of trade names, patents, or other intellectual property.

(4) UNITY OF OPERATION AND USE. This subsection explains when participants in a commonly controlled economic enterprise are considered a unitary business because they have unity of operation and use.

(a) *General.* If the participants in a commonly controlled economic enterprise have both unity of operation and unity of use, they shall be considered engaged in a unitary business.

(b) *Unity of operation.* Unity of operation means there is functional integration among the participants, and is evidenced generally by shared support functions. Activities that indicate unity of operation include, but are not limited to:

1. Centralized purchasing, marketing, advertising, accounting, or research and development.

2. Intercorporate sales or leases, including but not limited to equipment and real estate.

3. Intercorporate services, including but not limited to administrative, data management, computer support, employee benefits, human resources, insurance, tax compliance, legal, financial, and cash management services.

4. Intercorporate debts.

5. Intercorporate use of proprietary materials, including but not limited to trade names, trademarks, service marks, patents, copyrights, and trade secrets.

(c) *Unity of use.* Unity of use is evidenced generally by centralized management or use of centralized policies. Factors that indicate unity of use include, but are not limited to:

1. Centralized executive force.

2. Interlocking directorates or corporate officers.

3. Intercompany employee transfers.

4. Common employee and executive training programs.

5. Common hiring and personnel policies.

6. Common recruiting programs.

7. Common employee handbooks.

8. Common employee benefit programs.

(5) FACTORS CONSIDERED BY U.S. SUPREME COURT. Since the definition of "unitary business" shall be construed to the broadest extent permitted by the U.S. Constitution, case law provides further guidance to determine whether a unitary business exists. Subsections (3) and (4) are reflective of that case law. Factors that have been considered by the U.S. Supreme Court to be determinative of a unitary business include:

(a) Unity of use and management (*Butler Bros. v. McColgan*, 315 U.S. 501, 508, 62 S. Ct. 701, 704 (1942)).

(b) A concrete relationship between the out-of-state and the in-state activities that is established by the existence of the unitary business (*Container Corp. of America v. Franchise Tax Bd. of California*, 463 U.S. 159, 167, 103 S. Ct. 2983, 2941 (1983)).

(c) Functional integration, centralization of management, and economies of scale (*Mobil Oil Corp. v. Comm'r of Taxes of Vermont*, 445 U.S. 425, 438, 100 S. Ct. 1223, 1232 (1980)).

(d) Substantial mutual interdependence (*F.W. Woolworth Co. v. Taxation and Revenue Dept. of New Mexico*, 458 U.S. 354, 371, 102 S. Ct. 3128, 3139 (1982)).

(e) Some sharing or exchange of value not capable of precise identification or measurement – beyond the mere flow of funds arising out of a passive investment or a distinct business operation (*Container*, 463 U.S. at 166, 103 S. Ct. at 2940).

(6) PRESUMPTIONS. The presumptions in pars. (a) to (g) apply when determining whether participants in a commonly controlled economic enterprise are considered a unitary business. Any of these presumptions may be rebutted by the taxpayer or by the department. However, the noncontrolling factors in par. (h) may not be used to rebut these presumptions:

(a) *Horizontal integration.* An entity or commonly controlled group of entities is presumed to be engaged in a unitary business when all of its activities are in the same general line of business.

(b) *Vertical integration.* An entity or commonly controlled group of entities is presumed to be engaged in a unitary business when its various divisions, segments, branches, or affiliates are engaged in different steps in a vertically structured enterprise.

(c) *Centralized management.* An entity or commonly controlled group of entities that might otherwise be considered as engaged in more than one unitary business is presumed to be engaged in one unitary business when there is strong central management coupled with the existence of centralized departments or affiliates for such functions as financing, advertising, research and development, or purchasing.

(d) *Different business segments.* An entity operating different business segments within the organizational structure of the single business entity is presumed to be engaged in a single unitary business with respect to the business segments.

(e) *Newly acquired corporations.* 1. Except as provided in subd. 2., when a corporation acquires another corporation so that the acquired corporation is a member of a commonly controlled group for the first time, it shall be presumed that the acquiring and acquired corporations are not engaged in a unitary business for the purchaser's taxable year that includes the acquisition. If the purchaser is already a combined group member, the taxable year that includes the acquisition is such taxable year of the combined group.

2. The presumption against unity in subd. 1. shall not apply if, immediately preceding the acquisition, the acquiring and acquired corporations were engaged in a unitary business apart from being in the same commonly controlled group, or if the designated agent of the combined group has properly made the controlled group election as provided in s. Tax 2.63.

(f) *Newly formed corporations.* Where a corporation or more than one corporation forms, or has formed, a new corporation, it shall be presumed that the formed corporation is engaged in a unitary business with the forming corporation or corporations from the date of its formation.

(g) *Refusal to provide information.* The department'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.* The following factors shall not negate the presumptions in paragraphs (a) to (g):

1. The use of arms-length pricing for sales, exchanges, or transfers between entities (*Exxon Corp. v. Dept of Revenue of Wisconsin*, 447 U.S. 207, 100 S. Ct. 2109 (1980)).

2. The fact that a business uses a separate accounting system including, but not limited to, separate accounting by division, by entity, by geographical area, by business function, or by business segment.

(7) PASSIVE HOLDING COMPANIES. 1. 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.

2. A passive parent holding company that directly or indirectly controls one 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.

(8) PASS-THROUGH ENTITIES. For purposes of subds. 1. and 2., "pass-through entity" includes a partnership, limited liability company treated as a partnership, tax-option corporation, estate, or trust, but does not include corporations treated as real estate investment trusts, regulated investment companies, real estate mortgage investment conduits, or financial asset securitization investment trusts.

1. For purposes of determining the scope of the unitary business, any business conducted by a pass-through entity that is controlled directly or indirectly by a corporation shall be treated as conducted by the corporation to the extent of the corporation's distributive share of the pass-through entity's income, regardless of the percentage of the corporation's ownership interest.

2. Any business conducted directly or indirectly by one corporation is unitary with that portion of a business conducted by another corporation through its direct or indirect interest in a pass-through entity if the requirements of s. 71.255(1)(n), Stats., are otherwise met with respect to the corporations' interests in such pass-through entity and the corporations are members of the same commonly controlled group.

Note: Section Tax 2.62 interprets s. 71.255(1)(n), Stats.

Cross References: See s. Tax 2.60 for definitions that relate to this section. See s. Tax 2.61(2) for more information on determining whether corporations are required to use combined reporting. See s. Tax 2.63 for more information on the controlled group election.

Tax 2.63 Controlled Group Election. (1) SCOPE. Section 71.255(2m), Stats., allows a commonly controlled group of corporations to elect to include every member of the commonly controlled group in a single combined group for combined reporting purposes. This section provides rules relating to making the election, continuity of the election, and limitations of the election.

(2) MAKING THE ELECTION. Preapproval by the department is not required to make the election. The designated agent of the combined group shall make the election on behalf of the group as described in this subsection. Paragraph (c) provides rules relating to identifying the designated agent in cases where a commonly controlled group consists of corporations that previously filed as more than one combined group.

(a) *Time period for making election.* The designated agent shall make the election on an original, timely filed combined return which includes all members of the commonly controlled group. A return shall be considered timely if it is filed by the designated agent on or before the due date of the return, including applicable extensions. If the return is not filed under extension, the designated agent may make the election by filing an amended combined return on or before the end of the automatic 7-month extension period provided in ss. 71.24(7) or 71.44(3), Stats. No return filed after this date shall constitute a valid controlled group election for the taxable year to which the return applies, although an election may be filed for a subsequent taxable year subject to the limitation in sub. (3)(b).

(b) *Method of election and required documentation.* 1. For the first year the designated agent makes the election, the designated agent must check a designated line of the combined return to indicate that a controlled group election is in effect.

2. For the first year the designated agent makes the election, the designated agent must include a statement with the combined return which lists every corporation that is a member of the commonly controlled group, and indicates that each such corporation has agreed to be bound by the election and that the election shall apply to any member that subsequently enters the group.

(c) *Multiple former combined groups.* 1. If a commonly controlled group consists of corporations that previously filed as more than one combined group, the controlled group election creates a new combined group. For purposes of application of loss carryforwards and research credits under s. Tax. 2.61, each former combined group included in the new combined group is a subgroup as described in s. Tax 2.61(9)(e)1. and the corporations within each subgroup are eligible to share loss carryforwards and research credits from taxable years prior to the election with all the members of that subgroup, to the extent such sharing would otherwise be allowed under s. Tax 2.61(6)(c), (9) and (10).

2. A new combined group described in subd. 1. shall appoint the designated agent of one of the former combined groups to be the designated agent, and the provisions of s. Tax 2.65 apply to that designated agent. The corporation that files the first combined return under the election shall be deemed the appointed designated agent for the new combined group.

(3) CONTINUITY OF ELECTION. (a) *Ten-year period.* Except as provided in sub. (4), the controlled group election is binding for and applicable to all members of the commonly controlled group for the taxable year for which the election is made and for the next 9 taxable years. The election is also binding on any corporations that join the commonly controlled group during the period the election is in effect. Any corporation that departs the commonly controlled group is not bound by the election for the taxable years after its departure from the group, except that if the corporation rejoins the commonly controlled group it becomes bound by the election for the taxable years it is part of the group.

(b) *Renewal.* 1. After the 10-year period described in par. (a), the designated agent may renew the election for another 10 taxable years, without prior written approval from the department. The renewal shall be made on an original, timely filed

return for the first taxable year after completion of the 10-year period. The requirements for a renewal of an election are the same as for making the original election as described in sub. (2).

2. If the election is not timely renewed as provided in subd. 1., the election is considered to be revoked by the designated agent. In the case of a controlled group election that is not timely renewed, a new election shall not be permitted in any of the next 3 taxable years.

(4) LIMITATION OF ELECTION. A controlled group election may be disregarded by the department if the facts demonstrate that the election has the primary effect of tax avoidance rather than its intended purpose of simplifying the determination of items includable in a combined report. The following rules apply to this limitation:

(a) *Tax avoidance.* 1. A controlled group election may be considered to have the primary effect of tax avoidance if from the facts available to any corporation in the commonly controlled group at the time of the election, the election will not have meaningful continuing application. For example, and without limitation, the department would disregard the tax effect of a controlled group election made in anticipation of a sale of a business if by making the election the seller incurred a significantly lower tax liability on the transaction and after such sale all other corporations in the combined group would be included in the combined group even if the controlled group election were not in effect.

2. While subd. 1. presents one indicator from which the controlled group election may be considered to have the primary effect of tax avoidance, this paragraph in no way limits the scope of possible indicators.

(b*) Administration.* If the department finds it necessary to disregard the tax effect of the controlled group election for a member of the commonly controlled group, the following rules apply:

1. The department shall compute adjustment amounts, and issue notices of assessment or refund accordingly, to remove the net income or loss and apportionment factors of the member from the unitary combination and to compute that member's tax liability in the manner it would have been computed had the controlled group election not been in place. Such notices must be sent within the statute of limitations provided under s. 71.77, Stats., including any extensions.

2. Except as provided in subd. 3., the controlled group election remains in effect for the remainder of the 10-year period with respect to all members other than those for which the department disregarded the tax effect of the election under subd. 1. A member for which the department disregarded the tax effect of the election shall not participate in the controlled group election for the remainder of the 10-year period, but may participate in any controlled group election made after the expiration of the 10-year period.

3. If the department makes an adjustment as described in subd. 1, the department and the commonly controlled group may enter into an agreement to revoke the controlled group election in its entirety. The agreement may provide that the revocation applies for all subsequent taxable years or may provide that the revocation applies for all years open to adjustment in addition to subsequent years. The agreement must provide that each corporation in the commonly controlled group has agreed to be bound by the agreement. If the revocation applies for all years open to adjustment, the agreement may specify that the taxpayers whose returns are affected by the revocation must file amended returns with the department by an agreed upon date in order for the revocation to be effective.

4. If the controlled group election is revoked under subd. 3., a new election shall not be permitted in any of the next 3 taxable years, but may be allowed thereafter provided the election has the primary effect of simplifying the determination of items includable in a combined report rather than of tax avoidance.

Note: Section Tax 2.63 interprets s. 71.255(2m), Stats.

Cross References: See s. Tax 2.60 for definitions that relate to this section. See s. Tax 2.61(2)(b) for more information on the effect of the controlled group election. See s. Tax 2.65 for more information on the duties of the designated agent. See s. Tax 2.67 for more information on combined returns.

Tax 2.64 Alternative Apportionment for Combined Groups Including Specialized Industries. (1) SCOPE. Section 71.255(5)(a), Stats., provides that a combined group is generally required to use the modified sales factor method to apportion its combined unitary income. However, s. 71.255(5)(b), Stats., provides that a qualifying combined group may

petition the department to use an alternative apportionment method. This section provides rules relating to the eligibility requirements, continuity, and limitations of this privilege.

(2) ELIGIBILITY REQUIREMENTS. (a) *Qualifying combined group.* A qualifying combined group is a combined group for which 30 percent or more of the combined unitary income would, in the absence of combined reporting, be required to be apportioned using more than one factor under a method described in ss. Tax 2.46, 2.47, 2.475, 2.48, 2.50, or 2.502.

(b) *Requirements for petition.* The designated agent of the combined group requesting an alternative apportionment method must file a petition no less than 60 days before filing the first original, timely filed return using the alternative method. If this return is not filed under extension, the designated agent may file the petition no less than 60 days before the end of the automatic 7-month extension period provided in ss. 71.24(7) or 71.44(3), Stats., as applicable. The petition shall include the following:

1. The full name, address, and federal employer identification number of each member of the combined group.

2. The combined group's taxable year for which the alternative apportionment method as requested would begin to be effective.

3. A description of the alternative apportionment method requested.

4. A complete and precise statement of the reasons for the modification requested, including why the modified sales factor method would result in an unfair representation of the degree of unitary business activity in this state. This statement must provide clear and convincing evidence of its assertions.

5. A calculation of the combined group's tax liability for the first taxable year to which the petition applies and for the previous taxable year, using the apportionment method prescribed in s. 71.255(5)(a), Stats., for both years. For the previous taxable year's computation, compute this amount as if a combined report including those same corporations were required in the previous taxable year, even if it was before s. 71.255, Stats., was in effect.

6. A calculation of the combined group's tax liability for the first taxable year to which the petition applies and for the previous taxable year, similar to the calculation in subd. 5., but using the requested apportionment method instead of the modified sales factor method.

7. A calculation of each combined group member's tax liability for the first taxable year to which the petition applies and for the previous taxable year, similar to the calculations in subds. 5. and 6., computed as if each corporation were not a member of the combined group and using the method prescribed by ss. Tax 2.39, 2.395, 2.45, 2.46, 2.47, 2.475, 2.48, 2.49, 2.495, 2.50, or 2.502, as applicable to each corporation.

8. A statement as to whether any combined group member is being audited by the department at the time of the petition.

(c) *Limitation.* In no case may the department grant a taxpayer's petition for an alternative apportionment method if such alternative method would result in a lower tax liability than the sum of the tax liabilities of the combined group members computed as if they were not members of a combined group and using the apportionment method prescribed by ss. Tax 2.39, 2.395, 2.45, 2.46, 2.47, 2.475, 2.48, 2.49, 2.495, 2.50, or 2.502, as applicable to each corporation.

(d) *Approval or rejection.* The petition must be approved by the department in writing before a combined return is filed using the alternative apportionment method. The department's acceptance of a return using the alternative apportionment method does not constitute approval of the petition or method used. The department may, after receipt and review of the petition, require additional information necessary to determine whether the modified sales factor method does not fairly represent the degree of unitary business activity in this state. Filing of a petition does not affect the accrual of interest on underpayment of estimated taxes.

(e) *Attachments to return.* For each combined return on which the alternative apportionment method is used, the designated agent must include the following documentation with the return:

1. A copy of the department's written approval for the alternative apportionment method.

2. A calculation of the combined group's tax liability computed as if it used the modified sales factor method instead of the alternative apportionment method.

3. A calculation of each combined group member's tax liability for the taxable year included in the combined return computed as if each corporation were not a member of the combined group and using the apportionment method prescribed by ss. Tax 2.39, 2.395, 2.45, 2.46, 2.47, 2.475, 2.48, 2.49, 2.495, 2.50, or 2.502, as applicable to each corporation.

(3) CONTINUITY AND LIMITATIONS. (a) *Continuity.* 1. If the department approves the alternative apportionment method, the combined group engaged in that unitary business shall continue to use the alternative apportionment method for 6 taxable years following the first year for which the alternative method was approved, except as provided in par (b).

2. No later than 60 days before filing the first return for a period subsequent to the expiration of the 7-year period in subd. 1., the designated agent of the combined group must file a new petition with the department in order to continue using the alternative apportionment method. The new petition is subject to the same requirements as the original petition except that the designated agent must include the calculations described in sub. (2)(b)5. to 7. for each of the years to which previous election applied, instead of for the first taxable year to which the petition applies and the previous taxable year.

(b) *Limitations.* 1. If the sum of the tax liabilities of the combined group members for the taxable year computed as if they were not combined group members, as reported in the attachment described in sub. (2)(e)3., is greater than the combined group's tax liability using the alternative apportionment method, the combined group cannot use the alternative method for the taxable year. Instead, the combined group must use the modified sales factor method. For each of the remaining taxable years in the 7-year period described in par. (a)1., the combined group must use the alternative apportionment method to the extent the limitations of this paragraph do not apply.

2. If the combined group is no longer a qualifying combined group as described in sub. (2)(a), the combined group may no longer use the alternative apportionment method beginning with the year the combined group no longer qualifies. If it subsequently becomes a qualifying combined group in a later taxable year, the designated agent of the group may file a new petition for an alternative apportionment method.

Note: Mail petitions for alternative apportionment methods to: Administration Technical Services – Corporations Unit, Wisconsin Department of Revenue, P.O. Box 8933, Mail Stop 6-40 Madison, WI 53708-8933.

Note: This section interprets s. 71.255(5)(b), Stats.

Cross References: See s. Tax 2.60 for definitions that relate to this section. See s. Tax 2.65 for more information on the duties of the designated agent. See s. Tax 2.67 for more information on combined returns.

Tax 2.65 Designated Agent of Combined Group. (1) SCOPE. Section 71.255(7), Stats., requires every combined group to have a designated agent to act on behalf of the group. This section provides rules relating to identifying the designated agent and describes the scope and limitations of the agency relationship.

(2) IDENTIFYING DESIGNATED AGENT. (a) *Eligibility.* The combined group may select any member as the designated agent, subject to a limitation that the designated agent's taxable year must be the same as the combined group's taxable year.

(b) *Creation of agency.* A combined group shall appoint a designated agent. The corporation which files, or will file, the first combined return for the combined group is deemed to be appointed as the designated agent. If no combined return is

filed, the department will appoint the parent corporation of the combined group to be the designated agent, or if there is no such parent, the department may appoint any corporation in the combined group to be the designated agent.

(c) *Continuity of agency into future years.* Once a member of the combined group is appointed as the designated agent, it shall remain the designated agent of that group for all future years unless one of the following applies:

1. The designated agent leaves the combined group, in which case the corporation which files, or will file, the first combined return after the date the designated agent leaves is deemed to be appointed as the new designated agent.

2. The designated agent ceases to exist, in which case the designated agent must notify the department in writing that another member of the combined group (or successor corporation of any member of the combined group) will thereafter act as designated agent for that taxable year and any prior taxable years. The member appointed for that taxable year and any prior taxable years need not be the new designated agent for all future taxable years. The substitute designated agent will succeed to the rights and responsibilities of the former designated agent and may in turn appoint another designated agent for future taxable years. If the designated agent fails to notify the department in writing of the new designated agent, the department may select a surviving member of the combined group to act as the designated agent.

3. The designated agent is still a member of the combined group but submits a written request to the department for another combined group member to act as designated agent, and the department grants the request.

Note: Send requests to change the combined group's designated agent and notifications of successor designated agents to: Corporation Processing Unit, Wisconsin Department of Revenue, P.O. Box 8908, Madison, WI 53708-8908.

(d) *Continuity of agency for prior years.* The designated agent of a combined group for a prior taxable year must continue to act as the designated agent for that taxable year unless the designated agent ceases to exist, in which case par. (c)2. applies., or the designated agent submits a written request to the department for another combined group member to act as designated agent, and the department grants the request.

Note: Send requests to change the combined group's designated agent and notifications of successor designated agents to: Corporation Processing Unit, Wisconsin Department of Revenue, P.O. Box 8908, Madison, WI 53708-8908. However, if the request relates to prior taxable years that are under audit, the designated agent may submit the written request to the department's representative that has notified the designated agent of the audit.

(e) *Designated agent for purposes of resolving disputes over combined group membership.* If the department determines that one or more corporations are members of a combined group and no combined return was filed, the group of corporations the department asserts is a combined group may appoint a member of that group as the designated agent solely for purposes of contesting the department's determination. The appointment of a designated agent under this paragraph shall not be construed as a concession by either the corporations or the department regarding the existence of a combined group or the proper composition thereof.

(3) SCOPE AND LIMITATIONS OF AGENCY. (a) *Duties of designated agent.* The designated agent is generally required to act on behalf of the combined group in its own name in all matters relating to the combined return. This includes performing the following duties:

1. Filing the combined return, including the reporting of any separate entity items attributable to combined group members.

2. Filing any extension of time to file the combined return.

3. Filing any amended combined returns or claims for refunds or credits relating to the combined return, including any separate entity items attributable to combined group members.

4. Sending and receiving all correspondence with the department regarding the combined return, except that if correspondence relates to separate entity items or a payment made by another member of the combined group as provided in s. Tax 2.66(2), the department may send such correspondence to that other member or the designated agent, or both.

5. Remitting taxes applicable to the combined return, including estimated taxes, except as otherwise provided in s. Tax 2.66.

6. Participating on behalf of the group in any investigation or hearing by the department regarding the combined return, including producing all information requested and filing any appeal. Unless provided otherwise in writing, any appeal filed by the designated agent relating to the combined return shall be considered filed by all members of the combined group, including any corporations that were not included in the combined return but which the department asserts are members the combined group.

7. Executing waivers, closing agreements, powers of attorney, and other documents relating to the combined return. Unless the department and taxpayer agree otherwise in writing, any waiver, closing agreement, power of attorney, or other document executed by the designated agent relating to the combined return shall be considered executed by all members of the combined group, including any corporations that were not included in the combined return but which the department asserts are members of the combined group.

8. Receiving assessment notices regarding the combined return. Subject to par. (f), a notice received by the designated agent is considered received by all members of the combined group, including any corporations that were not included in the combined return but which the department asserts are members the combined group. If a notice relates to separate entity items that are attributable to a combined group member other than the designated agent, the designated agent may submit a written request to the department to reissue the notice or a portion of the amount thereof to the combined group member responsible for the separate entity items. The designated agent must submit the written request on or before the due date shown on the notice.

Note: Send written requests to reissue notices relating to separate entity items to: Wisconsin Department of Revenue, Mail Stop 5-257, P.O. Box 8906, Madison, WI 53708-8906.

9. Receiving any refunds relating to the combined return.

(b) *Exclusivity.* Except as provided in this paragraph, no person other than the designated agent shall have authority to act for or represent itself or the combined group regarding the duties listed in par. (a). A combined group member, or a corporation which the taxpayer asserts is a combined group member, may assume such duties under any of the conditions described in subds. 1. to 3.:

1. By election of the designated agent or the applicable combined group member, a combined group member may perform any of the duties listed in par. (a) to the extent such duties relate to separate entity items. This may include the filing of a separate return to report the member's separate entity items, subject to the requirements of par. (c).

2. A combined group member may make estimated payments on its own behalf to the extent allowed in s. Tax 2.66(2).

3. If a combined return was filed, the department may allow any corporation which it asserts should be added to or eliminated from the combined group to represent itself after receipt of a written request from such corporation. However, any such corporation shall still be bound by any action taken by the designated agent before the request of such corporation to represent itself has been accepted by the department.

Note: A corporation described in subd 3. that wishes to represent itself should submit the written request to the department's representative that has notified the corporation of the department's assertion.

(c) *Reporting of separate entity items.* If a combined group member chooses to file a separate Wisconsin return to report its separate entity items rather than having the designated agent include them in the combined return in the manner described in s. Tax 2.67(2)(d)3., the member must consider the totality of its share of items from the combined return plus its separate entity items for purposes of applying any limitations, so that its total net tax plus recycling surcharge does not differ from the amount that would have been due if the separate entity items had been included in the combined return. The combined group member must submit a copy of the combined return with its separate return.

(d) *Unauthorized acts.* The department is not bound by unauthorized acts made with respect to a combined return by a corporation that is not the designated agent. The department may choose to receive the benefits or assume the obligations of any such unauthorized acts, in which case the department is bound only if it takes affirmative steps to expressly manifest its intent to receive the benefits or assume the obligations of such acts.

(e) *Failure to act.* If the designated agent is unable or unwilling to fulfill its obligations with respect to the combined return, is unresponsive, or has not been identified to the department, the department may appoint a new designated agent, or it may deal directly with any member of the combined group in respect to its share of the combined return items in which case each member shall have full authority to act for itself.

(f) *Joint and several liability.* The members of a combined group shall be jointly and severally liable for the combined tax, penalty, and interest attributable to the combined unitary income, net of any loss carryforwards and credits applied thereto. This provision does not apply to any tax, interest, or penalty attributable to separate entity items. Although the department may send correspondence, notices, refunds, assessments, or other documents relating to any combined group member's separate entity items to the designated agent, and the designated agent may choose to pay any tax, interest, or penalty on behalf of a combined group member, the tax, interest, or penalty attributable to separate entity items is ultimately the responsibility of the combined group member or members to which the separate entity items are attributable.

(g) *Confidentiality provisions.* The designated agent is an agent under s. 71.78(4)(e), Stats. Therefore, the department may provide information relating to any member of the combined group to the designated agent, including but not limited to information relating to such member's separate entity items.

Note: This section interprets s. 71.255(7), Stats.

Cross References: See s. Tax 2.60 for definitions that relate to this section. See s. Tax 2.66 for more information on combined estimated tax requirements. See s. Tax 2.67 for more information on combined returns.

Tax 2.66 Combined Estimated Tax Payments. (1) *SCOPE. In general, s. 71.255(7)(b)5., Stats., provides that only the designated agent of a combined group may make estimated tax payments applicable to a combined return. This section provides exceptions to the general rule, explains the estimated tax requirements, and provides rules for applying estimated payments and overpayments.*

(2) SEPARATE ESTIMATED PAYMENTS. (a) *When separate estimated payments are allowed.* Although the designated agent is always authorized to make estimated payments on behalf of any and all of its combined group members, a combined group member other than the designated agent may make estimated payments on its own behalf if any of subds. 1. to 3. apply:

1. For the first taxable year for which a combined group files a combined return, any member of such group may make estimated payments on its own behalf.

2. For the first taxable year for which a corporation is a member of a combined group, that corporation may make estimated payments on its own behalf.

3. Any combined group member may make estimated payments on its own behalf to the extent those payments relate to separate entity items.

(b) *Reporting of separate estimated payments.* If a combined group member other than the designated agent makes separate estimated payments and applies those payments to the combined return, the designated agent must notify the department of such payments on a department-prescribed form or forms filed with the combined return. This notification authorizes the department to apply the separate estimated payments to the combined return.

Note: The form prescribed for notifying the department of separate estimated payments to be applied to the combined return is Form 4M, Combined Group Member-Level Data. Instructions for Form 4M may indicate that further details regarding such payments should be reported on supporting schedules or on another department-prescribed form.

(3) DETERMINATION OF REQUIRED ESTIMATED PAYMENTS. (a) *General.* If a combined return is filed, the amount of any addition to tax under s. 71.84(2), Stats., shall be computed as if the combined group were one corporation. "Tax shown on the return" and "tax for the taxable year" as defined in s. 71.29(1)(b), Stats., have the same meaning with respect to a combined return as to a separate return.

(b) *Computation of thresholds.* Since "tax shown on the return" has the same meaning with respect to a combined return as to a separate return, the amounts of the following thresholds are the same regardless of the number of combined group members included in the combined return:

1. Section 71.29(7), Stats., which provides that no interest on underpayment is required if the tax shown on the return for the taxable year is less than $500.

2. Section 71.29(9), Stats., which provides that for corporations that have Wisconsin net incomes of less than $250,000 and whose preceding taxable year was a 12-month taxable year, estimated payments may be based on the lesser of 90 percent of tax shown on the return for the current taxable year or the tax shown on the return for the preceding year.

(c) *Effect of separate entity items.* The amount of net income and tax shown on a combined return includes net income and tax attributable to separate entity items. If the combined return includes separate entity items of a corporation that would otherwise be a combined group member except that it has no items that are subject to combination under the water's edge rules of s. Tax 2.61(4), such corporation is considered a combined group member for purposes of determining required estimated payments.

Example: Combined Group AB consists of Member A and Member B. Group AB filed a combined return for calendar year 2010. The 2010 return includes $30,000 of net tax attributable to Member A's items and $20,000 attributable to Member B's items, including $5,000 attributable to B's separate entity items. The 2010 combined return also includes $10,000 of net tax from the separate entity items of Corporation C, which would be a combined group member except that none of its items are subject to combination under the water's edge rules. If Group AB is not eligible to base its estimated taxes on its 2009 net tax under the provisions of par. (b), Group AB's required estimated tax payments for purposes of its 2010 combined return are $60,000 (= 30,000 + $20,000 + $10,000).

(d) *Annualized income installment method.* For purposes of the annualized income installment method provided in s. 71.29(9)(c) and (10)(c), Stats., the previous year's apportionment percentage for a combined group equals the sum of the combined group members' modified sales factor numerators as determined under s. Tax 2.61(7)(a) for the combined group's preceding taxable year, divided by the combined group's modified sales factor denominator as determined under s. Tax 2.61(7)(b) for the combined group's preceding taxable year.

(e*) Change in membership.* Except as provided in par. (f), for purposes of determining estimated tax requirements, the tax shown on the combined return shall not be adjusted to reflect members that have joined or departed the group during the current taxable year or the preceding taxable year.

Example: Group JK files a combined return for the calendar year 2009. During 2010, Member J acquires L and L becomes a member of the combined group. If the group qualifies to determine its estimated tax obligations for 2010 based on its preceding year's tax liability, its preceding year's tax liability only includes the tax shown on Group JK's 2009 combined return; it does not include any tax liability from L's 2009 separate return.

(f) *First combined return year.* The following rules apply to the computation of required estimated payments for the first year that a combined group files a combined return:

1. If the total of the combined group's Wisconsin net income reported on the combined return is less than $250,000, the required estimated payments may be based on the sum of the members' tax shown on their Wisconsin returns for the preceding year as provided by s. 71.29(9)(a)2., Stats., but only if all combined group members filed a Wisconsin return which covered a full 12 months in such preceding taxable year. If a member was included in the combined return of another combined group in the preceding taxable year, its tax shown on the return for that year is the tax attributable to the sum of its share of combined unitary income and income from separate entity items reported on that return.

2. If one or more combined group members did not file a Wisconsin return which covered 12 months in the preceding taxable year, the combined group must base its required estimated payments on 90 percent of the tax shown on the combined return as provided under s. 71.29(9)(a)1. and (10)(b), Stats.

3. The previous year's apportionment percentage for purposes of the annualized income installment method equals the sum of the current combined group members' apportionment factor numerators from their returns for the preceding taxable year, divided by the sum of the apportionment factor denominators from their returns for the preceding taxable year. If a member was included in the combined return of another combined group in the preceding taxable year, its apportionment percentage for this purpose is its modified sales factor numerator for that taxable year as determined under s. Tax 2.61(7)(a), divided by its separate company denominator for that taxable year as determined under s. Tax 2.61(7)(b).

4. For purposes of subds. 1. and 3., if a combined group member has a taxable year different than the combined group's taxable year, the member's preceding taxable year is its taxable year most recently ended before the first day of the combined group's taxable year.

(4) RULES FOR APPLYING ESTIMATED PAYMENTS AND OVERPAYMENTS. (a) *Separate returns filed in year following combined return year.* If a combined group terminates and the former members properly file separate returns in the subsequent year, any combined estimated payments made for such year shall be credited against the separate tax liabilities of the former members of the combined group in the manner allocated by the designated agent. The designated agent must notify the department of the manner in which the payments are to be allocated. The designated agent may make this notification in correspondence to the department unless the department prescribes a specific form for this purpose, in which case the prescribed form must be used. In either case, the notification must be submitted to the department separately from any return.

(b) *Combined estimated payments but no combined return.* If combined estimated payments are made for a taxable year but no combined return is filed for that year or for the previous year, the estimated payment shall only be credited to the corporation that made the payment.

(c) *Overpayments.* 1. If a combined group member has a credit for an overpayment of taxes from a prior taxable year when it was not a combined group member, the member may, through its designated agent, authorize the department to apply some or all of the credit against the total tax liability reported on the combined return. To carry out this authorization, the designated agent must use a department-prescribed form or forms to notify the department of the amount to be applied and file such form or forms with the combined return. Alternatively, the member may file a claim for refund of the overpayment, in which case the overpayment will be refunded to that member.

Note: The form prescribed for notifying the department of a member's prior year overpayments to be applied to the combined return is Form 4M, Combined Group Member-Level Data. Instructions for Form 4M may indicate that further details regarding such overpayments should be reported on supporting schedules or on another department-prescribed form.

2. If a corporation leaves a combined group that has an overpayment of taxes carried over from a prior combined return year, the designated agent may allocate a portion of that overpayment to the former member. The designated agent must notify the department of the amount to be allocated to the former member. The designated agent may make this notification in correspondence to the department unless the department prescribes a specific form for this purpose, in which case the prescribed form must be used. In either case, the notification must be submitted to the department separately from any return.

(d) *Erroneous combined estimated payments.* If a designated agent makes estimated payments on the erroneous premise that a corporation is an eligible member of the combined group, and discovers the error prior to the time the combined group and the corporation file their respective returns, the designated agent may allocate some or all of the combined estimated payments to the corporation. The designated agent must notify the department of the amount to be allocated. The designated agent may make this notification in correspondence to the department unless the department prescribes a specific form for this purpose, in which case the prescribed form must be used. In either case, the notification must be submitted to the department separately from any return. The combined group and the corporation will each compute their

addition to tax under s. 71.84(2), Stats., as if the estimated payments allocated to such corporation had actually been paid by it rather than by the combined group.

(e) *Erroneous separate estimated payments.* If a corporation makes separate estimated payments on the erroneous premise that it is not a combined group member, the following rules apply:

1. If the corporation discovers the error prior to the time the designated agent files the combined return for the taxable year, and the corporation has not filed a separate return for the period that should have been included in such combined return, the corporation may apply the separate estimated payments to the combined return. The designated agent must report the separate estimated payments in the manner described in sub. (2)(b).

2. If the corporation discovers the error prior to the time the designated agent files the combined return for the taxable year, but the corporation has already filed a separate return for the period that should have been included in the combined return, the corporation must file an amended separate return showing no net income, overpayment, or underpayment, and stating that such corporation will join in the filing of a combined return and identifying the designated agent of the combined group. Unless the corporation specifies otherwise on the amended return, the department will not refund the erroneously paid amounts. Instead, when the designated agent files the combined return including that corporation, the corporation may apply the separate estimated payments to the combined return. The designated agent must report the separate estimated payments so applied in the manner described in sub. (2)(b).

3. If the corporation discovers the error after the designated agent has filed the combined return for the taxable year, but the corporation has not filed a separate return, the designated agent must file an amended combined return, and may apply the corporation's separate estimated payments to the amount due on the amended combined return. The designated agent must report the separate estimated payments so applied in the manner described in sub. (2)(b).

4. If the corporation discovers the error after the designated agent has filed the combined return for the taxable year and after the corporation has already filed a separate return for the period that should have been included in the combined return, the corporation must file an amended separate return and the combined group must file an amended combined return. The provisions of subd. 2. apply with respect to the amended separate return. The corporation may apply the separate estimated payments to the amended combined return. The designated agent must report the separate estimated payments so applied in the manner described in sub. (2)(b).

Note: If an allocation described in sub. (4)(a), (c)2., or (d) is necessary and the department has not prescribed a form to use to notify the department of the allocation, send correspondence notifying the department of the allocation to: Corporation Processing Unit, Wisconsin Department of Revenue, P.O. Box 8908, Madison, WI 53708-8908.

Note: Section Tax 2.66 interprets ss. 71.255(7), 71.29, and 71.84(2), Stats.

Cross References: See s. Tax 2.60 for definitions that relate to this section. See s. Tax 2.65 for more information on the duties of the designated agent. See s. Tax 2.67 for more information on combined returns.

Tax 2.67 Combined Returns. (1) SCOPE. This section provides rules relating to the filing of combined returns by corporations required to use combined reporting under s. 71.255, Stats. This section explains the filing requirements for combined returns, provides rules relating to defining the taxable year included in a combined return, and describes how interest, penalties, and statutes of limitations apply to combined returns.

(2) FILING REQUIREMENTS FOR COMBINED RETURNS. (a) *General.* The designated agent of a combined group must file a combined return on behalf of the group. For each combined group member included in the combined return, the combined return satisfies the member's requirement for filing returns under ss. 71.24(1) or (1m) or 71.44(1) or (1m), Stats., as applicable. The combined return must generally be filed by the 15th day of the 3rd month following the close of the taxable year. However, an automatic 7-month extension is provided by ss. 71.24(7) or 71.44(3), Stats., as applicable.

(b) *Electronic filing.* All combined returns shall be filed electronically. The secretary of revenue may waive the requirement to file a combined return electronically when the secretary determines that the requirement causes an undue hardship, if the person requests the waiver in writing and clearly indicates why the requirement causes an undue hardship.

In determining whether the electronic filing requirement causes an undue hardship, the secretary of revenue may consider the following factors:

1. Unusual circumstances that may prevent the person from filing electronically.

Example: The person does not have access to a computer that is connected to the internet.

2. Any other factor that the secretary determines is pertinent.

Note: Written requests should be e-mailed to DORWaiverRequest@revenue.wi.gov, faxed to (608) 264-7776, or addressed to Mandate Waiver Request, Wisconsin Department of Revenue, Mail Stop 5−77, P.O. Box 8949, Madison, WI 53708−8949.

Note: Forms not filed electronically may be delivered in person to the Department of Revenue at 2135 Rimrock Road, Madison, Wisconsin or mailed to the address specified on the form or in the instructions.

(c) *Components of combined return.* A combined return shall include the items listed below, and shall be considered incomplete if any of these items are excluded:

1. One Wisconsin Form 4, Income or Franchise Tax Return, for the combined group as a whole.

2. One Wisconsin Form 4R, Federal Taxable Income Reconciliation for Combined Groups, for the combined group as a whole. The purpose of Form 4R is to reconcile federal taxable income per the federal consolidated return and separate returns, as applicable, with the amount on Form 4, line 1. Form 4R shall be considered complete only if the designated agent submits a supporting schedule which identifies each corporation to which each reconciling amount is attributable, and a schedule which identifies each corporation in the commonly controlled group which is not included in either the federal consolidated return or the combined return.

3. One Wisconsin Form 4M, Combined Group Member-Level Data, for each member of the combined group. The purpose of Form 4M is to identify the members of the combined group, provide information regarding the member's items included in the combined return, and account for payments to be applied to the combined return.

4. If the combined group is using apportionment, one Wisconsin Form 4A, Apportionment Data for Combined Groups, and the apportionment factor computation for each member of the combined group as performed on Form 4A-1, Apportionment Data for Single Factor Formulas, or Form 4A-2, Apportionment Data for Multiple Factor Formulas, as applicable.

5. Any other required supporting forms and schedules listed in s. Tax. 2.03, as applicable. Unless stated otherwise in the instructions, supporting forms and schedules shall be prepared separately for each combined group member.

6. A copy of the complete federal return for each combined group member, including all supporting schedules and any amended returns, for the member's taxable year included in the combined return. For combined groups that also file in a federal consolidated return, any of the alternatives described in subd. pars. a. to c. will be considered to satisfy this requirement:

a. A copy of the federal consolidated return, including all supporting forms, schedules, and statements for each corporation included in the consolidated return, as submitted to the internal revenue service.

b. Pro forma federal returns prepared separately for each combined group member, including all supporting forms and schedules prepared separately for each combined group member.

c. A spreadsheet showing the line-by-line computation of taxable income of each combined group member included in the federal consolidated return, including consolidating adjustments, plus the supporting forms, schedules, and statements filed with the internal revenue service pertaining to each such member. The supporting statements must include balance sheets as of the beginning and end of the tax year, a reconciliation of income per books with income per return,

and a reconciliation of retained earnings, to the extent the member was required to submit these items to the internal revenue service.

7. For combined groups that also file in a federal consolidated return, a copy of federal Form 851, Affiliations Schedule.

(d) *Separate entity items.* 1. Subject to the provisions of s. Tax 2.65(3)(b), if any combined group member has separate entity items, the designated agent shall include those separate entity items in the combined return. If a corporation that would otherwise be a combined group member has no items that are subject to combination under the water's edge rules of s. Tax 2.61(4), the designated agent may include that corporation's separate entity items in the combined return, in which case the combined return must include the items specified in sub. (2)(b)3., 5., and 6. for that corporation as if it is a combined group member. Alternatively, the corporation may file a separate Wisconsin return to report those items.

2. The joint and several liability provisions of s. Tax 2.65(3)(f) do not apply to any tax, interest, or penalty attributable to separate entity items. Although the department may send correspondence, notices, refunds, assessments, or other documents relating to any combined group member's separate entity items to the designated agent, and the designated agent may choose to pay any tax, interest, or penalty on behalf of a combined group member, the tax, interest, or penalty attributable to separate entity items is ultimately the responsibility of the combined group member or members to which the separate entity items are attributable.

3. The separate entity net income or loss and apportionment factors included in the combined return shall be reported on Wisconsin Form 4N, Nonapportionable and Separately Apportioned Income. The designated agent must complete and submit Form 4N with the combined return for each applicable combined group member and carry forward the total Form 4N amounts to the appropriate line on Form 4. For purposes of the requirement of s. 71.255(2)(d), Stats., separate entity items reported on Form 4N shall be considered filed on a separate return. However, for purposes of determining the member's net income, tax, interest, underpayment interest, recycling surcharge, and the statute of limitations, the separate entity amounts shall be added to its amounts computed in the unitary combination.

4. If a corporation is a member of more than one combined group at the same time, the corporation must include its separate entity items, if any, in the combined return of only one such group.

(e) *Amended returns.* If a corporation erroneously fails to join in the filing of a combined return, the designated agent shall file an amended combined return adding such corporation and, if a separate return was filed by such corporation, such corporation shall file an amended separate return showing no net income, overpayment, or underpayment, and stating that such corporation has joined in the filing of a combined return and identifying the designated agent of the combined group in which the corporation has been included.

(3) TAXABLE YEAR OF COMBINED RETURN. The taxable year included in a combined return is the combined group's taxable year as determined in s. 71.255(8), Stats. For purposes of determining the taxable year and the items includable in the combined group's taxable year, the following rules apply:

(a) *Combined group's taxable year.* If 2 or more members of the combined group file in a federal consolidated return, the combined group's taxable year is the taxable year of that federal consolidated return. If no such federal consolidated return applies or there is more than one federal consolidated return, the combined group's taxable year is the taxable year of the designated agent. In any case, s. Tax 2.65(2)(a) requires that the designated agent's taxable year must be the same as the combined group's taxable year.

(b) *Methods for members with differing taxable year*s. If the taxable year of a combined group member differs from the taxable year of the combined group, the designated agent shall elect to include that member's net income or loss and apportionment factors in the combined return by using one of the following methods:

1. Preparing a separate income statement from the member's books and records for the months included in the combined group's taxable year and using that income statement to determine the amounts includable in the combined return.

2. Using the net income or loss for the member's taxable year that ends during the combined group's taxable year to determine the amounts includable in the combined return.

(c) *Election of method.* If the designated agent converts a combined group member's taxable year to the combined group's taxable year as described in par. (b)1. or 2., it must use the same method for each combined group member subject to the election. Once the designated agent files the first combined return including a member whose taxable year is properly converted, the designated agent may not file an amended return to change the election, except that if the original return was not filed under extension, the designated agent may file an amended return to change the election on or before the end of the automatic 7-month extension period provided in ss. 71.24(7) or 71.44(3), Stats., as applicable. The designated agent must use the same method in each subsequent taxable year unless it obtains written approval from the department to use the other method.

Note: Send written requests for approval to change the election to: Audit Bureau, Wisconsin Department of Revenue, P.O. Box 8906, Madison, WI 53708-8906.

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

(4) INTEREST, PENALTIES, AND STATUTES OF LIMITATIONS. (a) *Interest.* For purposes of computing interest on late payments by or on behalf of combined group members, the following rules apply:

1. Interest shall be assessed to the designated agent of a combined group based upon the combined tax liability or deficiency shown on the combined return for the combined group's taxable year. However, the joint and several liability provisions of s. Tax 2.65(3)(f) do not apply to any interest attributable to separate entity items. If a notice of an interest amount due is attributable to separate entity items of a combined group member other than the designated agent, the designated agent may pay the amount due or may submit a written request to the department to reissue the notice or a portion of the amount thereof to the combined group member responsible for the separate entity items. The designated agent must submit the written request on or before the due date shown on the notice.

Note: Send written requests to reissue notices relating to separate entity items to: Wisconsin Department of Revenue, Mail Stop 5-257, P.O. Box 8906, Madison, WI 53708-8906.

2. An extension filed by the designated agent is considered an extension filed by all members of the combined group. However, such extension does not apply to corporations which are excluded from the unitary combination.

3. Interest due to underpayment of estimated taxes is computed based on the estimated tax requirements and other provisions described in s. Tax 2.66.

4. If a corporation erroneously fails to join in the filing of the combined return, all payments, credits, and other amounts collected from such corporation which are properly attributable to the combined group's taxable year and attributable to a period of time that such corporation was a member of the combined group shall be treated as having been paid by the combined group.

(b) *Late filing fees.* If a combined group fails to timely file a combined return and the late filing fee under s. 71.83(3), Stats., applies, the amount of the late filing fee shall be the amount provided in s. 71.83(3), Stats., regardless of the number of combined group members.

(c) *Failure to file.* For purposes of the penalty provided in s. 71.83(1)(a)1., Stats., the following rules apply:

1. A corporation which erroneously fails to join in the filing of a combined return, but which timely files a separate Wisconsin return or joins in the timely filing of a combined return for another combined group, shall not be subject to any penalty for failure to file. In determining whether such separate or combined return is timely filed, the taxable year of the

erroneously filed return shall be used, rather than the taxable year of the combined group with which the corporation should have filed.

2. A corporation which erroneously fails to join in the filing of a combined return and which fails, without reasonable cause, to timely file a separate Wisconsin return or join in the timely filing of a combined return for another combined group, shall be subject to the penalty computed based on its share of tax required to be reported on the combined return for its proper combined group, including its tax attributable to separate entity items. Except as provided in sub. (2)(d)2., the members of the combined group shall be jointly and severally liable for the penalty because it is the duty of the designated agent to include such corporation in the combined return. The department may send a notice of assessment of such penalty to the designated agent instead of the corporation which was erroneously omitted from the combined return.

(d) *Statutes of limitations.* 1. The designated agent's filing of a combined return is considered to be a return filed by each combined group member whose items are included in the combined unitary income reported on that return.

2. If a combined return includes separate entity items of a corporation that would otherwise be a combined group member but for the water's edge rules of s. Tax 2.61(4), the designated agent's filing of the combined return is also considered to be a return filed by that corporation.

3. For purposes of the statute of limitations in s. 71.77(7)(a), Stats., allowing the department to make an assessment within 6 years after the filing of a return, the statute of limitations is determined for each combined group member separately based on its total net income reported on its return, which is its net income or loss from the unitary combination as included in the combined return, plus its net income or loss from separate entity items. The 6-year statute of limitations applies if a combined group member's total net income reported on its return is less than 75 percent of the net income properly assessable and the tax attributable to the additional income is in excess of $100. Although the designated agent's return, as included in the combined return, may not be open under the 6-year statute of limitations, the designated agent is still responsible for any combined group member's return that is open under the 6-year statute of limitations, subject to the provisions of s. Tax 2.65(3)(f).

Note: Section Tax 2.67 interprets ss. 71.24(1), (1m), and (7), 71.255(1)(b), (7)(b), (8), and (9), 71.44(1), (1m), and (3), 71.77, 71.82, and 71.83, Stats.

Cross References: See s. Tax 2.60 for definitions that relate to this section. See s. Tax 2.65 for more information on the duties of the designated agent. See s. Tax 2.66 for more information on combined estimated tax requirements.