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Connecticut proposes combined reporting legislation

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Proposed Connecticut legislation would require a "combined group" to file a combined unitary tax return on a water's-edge basis, unless an election to compute the tax on a worldwide basis is made, applicable to income years beginning on and after January 1, 2011. The legislation lays out which corporate groups have to file unitary returns, how unitary groups should apportion net income, net operating losses, and their capital base. The bill also addresses the treatment of certain tax credits, credit limits, and minimum taxes, and the estimated tax payment requirements for groups filing unitary returns, among other items. [H.B. 6628, referred to Joint Committee on Finance, Revenue and Bonding, 3/22/11]

Some key provisions of the bill are highlighted below:

Definitions, determination of combined group income

Under the proposed legislation, "combined group" would mean all persons that have common ownership of not less than 50% and that are engaged in a unitary business where at least one person is subject to the state's corporate income tax. "Unitary business" would mean a single business entity or group of business entities under common ownership, which enterprise is sufficiently interdependent, integrated, or interrelated through its activities so as to provide mutual benefit and produce a significant sharing or exchange of value among such entities, or a significant flow of value among the separate parts. Any business conducted by a pass-through entity would be treated as being conducted by its members, whether directly held or indirectly held through a series of pass-through entities, to the extent of the member's distributive share of the pass-through entity's income, regardless of the percentage of the member's ownership interest or its distributive or any other share of pass-through entity income.

The combined group's net income would be the aggregate net income or loss of every taxable member and nontaxable member of the group derived from a unitary business. The legislation contains detailed provisions for determining the combined group's net income, including rules pertaining to U.S- group members, foreign members, income from pass-through entities, dividend elimination, the deferral of business income from intercompany transactions, charitable expenses, gain or loss from the sale or exchange of capital assets and property subject to an involuntary conversion, expenses attributable to constitutionally-exempt income, utilization of net operating losses, and the calculation of minimum taxes.

Apportionment

Detailed provisions are included in the legislation for determining the apportionment percentage of taxable members of the combined group. Notably, in computing the receipts factor, each taxable member would be required to add to its numerator its share of receipts of nontaxable members assignable to the state. Receipts assignable to Connecticut of each nontaxable member of the group would be aggregated and determined based upon the apportionment formula applicable to such member as if it were taxable. Each taxable group member would have to include in its receipts factor numerator a portion of the aggregate receipts assignable to the state of the nontaxable members based on a ratio, the numerator of which is the taxable member's receipts assignable to the state, and the denominator of which is the aggregate receipts assignable to the state of all taxable members of the group. The combined group would have to determine its property and payroll factor denominators for applicable members using the factors from all members, regardless of whether the member would utilize such factors.

Water's-edge group and worldwide election

Under the water's-edge approach, a nontaxable member's income, base and attributes that affect each member's apportionment factors would be included only if the nontaxable member is incorporated in the U.S. or its possessions or earns more than 20 percent of its income (directly or indirectly) from intangible property or service-related activities, the costs of which are deductible for federal income tax purposes against the income of other members of the group, to the extent of the related income and apportionment factors.

The world-wide election must be made by the group's designated taxable member on an original timely-filed return and is binding for the income year in which the election is made and for the ten immediately succeeding income years.

Deduction for increase in deferred taxes

Under the bill, a deduction would be allowed for publically-traded companies that have an increase in the net deferred tax liability or a decrease in the net deferred tax asset as a result of the imposition of the new unitary reporting requirements. The deduction must be taken ratably over a seven-year period starting with the unitary group's first tax year that begins in 2014.

Other provisions

The legislation would require the designated taxable member of the group to file the combined unitary tax return on behalf of the taxable members of the group. If a member of a combined group has a different income year than the group income year, such member would be required to report amounts from its return for its income year that ends during the group income year, but no such reporting would be required until such member's first income year beginning on or after January 1, 2011. A combined group must send its notice of selection of the designated taxable member of the combined group by the due date (or extended due date) of the combined unitary tax return for the initial income year that such a return is required. The designated taxable member would be responsible for paying estimated tax installments. Special due dates would apply to these installments for the 2011 group income year.

PwC observes

"Connecticut failed to adopt combined reporting legislation in recent years and a revised proposal has been raised again this year. The state has recently moved to single-party Democratic control, but a unitary provision was not in the governor's budget proposal so passage is uncertain," observes Stephen LaRosa, SALT Director with PwC in Hartford. "Prospects for adoption of combined reporting are further tempered by the fact that such a drastic, structural change to the state's corporate business tax provisions may be ill-timed given its potential negative impact on businesses and employment retention in the state."

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