Wisconsin Department of Revenue

Filing Wisconsin Returns Under Combined Reporting

This is a proposed guidance document. The document has been submitted to the Legislative Reference Bureau for publication in the Administrative Register for public comment as provided by sec. 227.112(1), Wis. Stats.

Updated January 10, 2023

In This Presentation...

See the table of contents for a summary of topics covered in this presentation and slide number references for each topic

For additional information relating to Wisconsin combined reporting, go to the Department's Combined Reporting web page at:

https://www.revenue.wi.gov/Pages/combrept/faqs.aspx

Who Must Be Included in a Combined Group?

Corporations that meet all of the following tests are included in the combined group:

Test 1: Are in a **commonly controlled group** of corporations,

Test 2: Are conducting a **unitary business** with one or more corporations in the group, AND

Test 3: Are not excluded by **water's edge rules**

Reference: Section Tax 2.61(2)(a), Wis. Admin. Code

Nonincludable Corporations

- S corporations
- Foreign insurers and insurers engaged exclusively in life insurance business
- Other tax exempt corporations that have no unrelated business taxable income
- Corporations that are REITs, RICs, REMICs, and FASITs*, all of which are treated as pass-through entities in sec. 71.255(1)(m), Wis. Stats.

*Real Estate Investment Trust (REIT), Regulated Investment Company (RIC), Real Estate Mortgage Investment Conduit (REMIC), and Financial Asset Securitization Investment Trust (FASIT).

References: Section Tax 2.61(2)(c)(d) and (e), Wis. Admin. Code

REITs, RICs, REMICs, and FASITs*

- REITs, RICs, REMICs, and FASITs are included in the definition of "pass-through entity" in sec. 71.255(1)(m), Wis. Stats., solely for the purpose of determining whether combined reporting applies

- Unlike S corporations or partnerships, these entities are **not** treated as an extension of their shareholders

  – For example, being a shareholder in a REIT that conducts business in Wisconsin does not automatically create nexus for the shareholder in Wisconsin

*Real Estate Investment Trust (REIT), Regulated Investment Company (RIC), Real Estate Mortgage Investment Conduit (REMIC), and Financial Asset Securitization Investment Trust (FASIT).

References: Sections Tax 2.61(2)(c) and (7)(e), and 2.62(8)(intro.), Wis. Admin. Code

Test 1: Commonly Controlled Group

- Sec. 71.255(1)(c). Wis. Stats., provides that a "commonly controlled group" can be any or a combination of four types of groups
- All four group types are based on ownership of stock representing more than 50% of voting power
  - A shareholder is considered to have more than 50% of voting power only if the shareholder has ownership or control of more than 50% of total combined voting power of all classes of stock entitled to vote

Reference: Section Tax 2.61(3)(d)), Wis. Admin. Code

Types of Commonly Controlled Groups

Type 1: Parent-subsidiary chain, based on direct or indirect ownership (sec. 71.255(1)(c)1., Wis. Stats.)

Type 2: Brother-sister corporations with a single common owner, based on direct or indirect ownership (sec. 71.255(1)(c)2., Wis. Stats.)

Type 3: Corporations where stock cannot be separately transferred ("stapled entities") (sec. 71.255(1)(c)3., Wis. Stats., and sec. Tax 2.61(3)(d)2., Wis. Admin. Code)

Type 4: Brother-sister corporations owned by, or for the benefit of, family members (sec. 71.255(1)(c)4., Wis. Stats.)

Indirect Ownership of Stock

- The stock attribution rules of section 318 of the Internal Revenue Code are used to determine if indirect ownership exists, with the following modifications:
  - If an entity owns more than 50% of another entity, it is considered to own all of the stock or interests owned by that entity for purposes of determining which entities are in the commonly controlled group
  - If a person has an option to acquire stock or interests, the stock or interests are not generally considered owned by the person

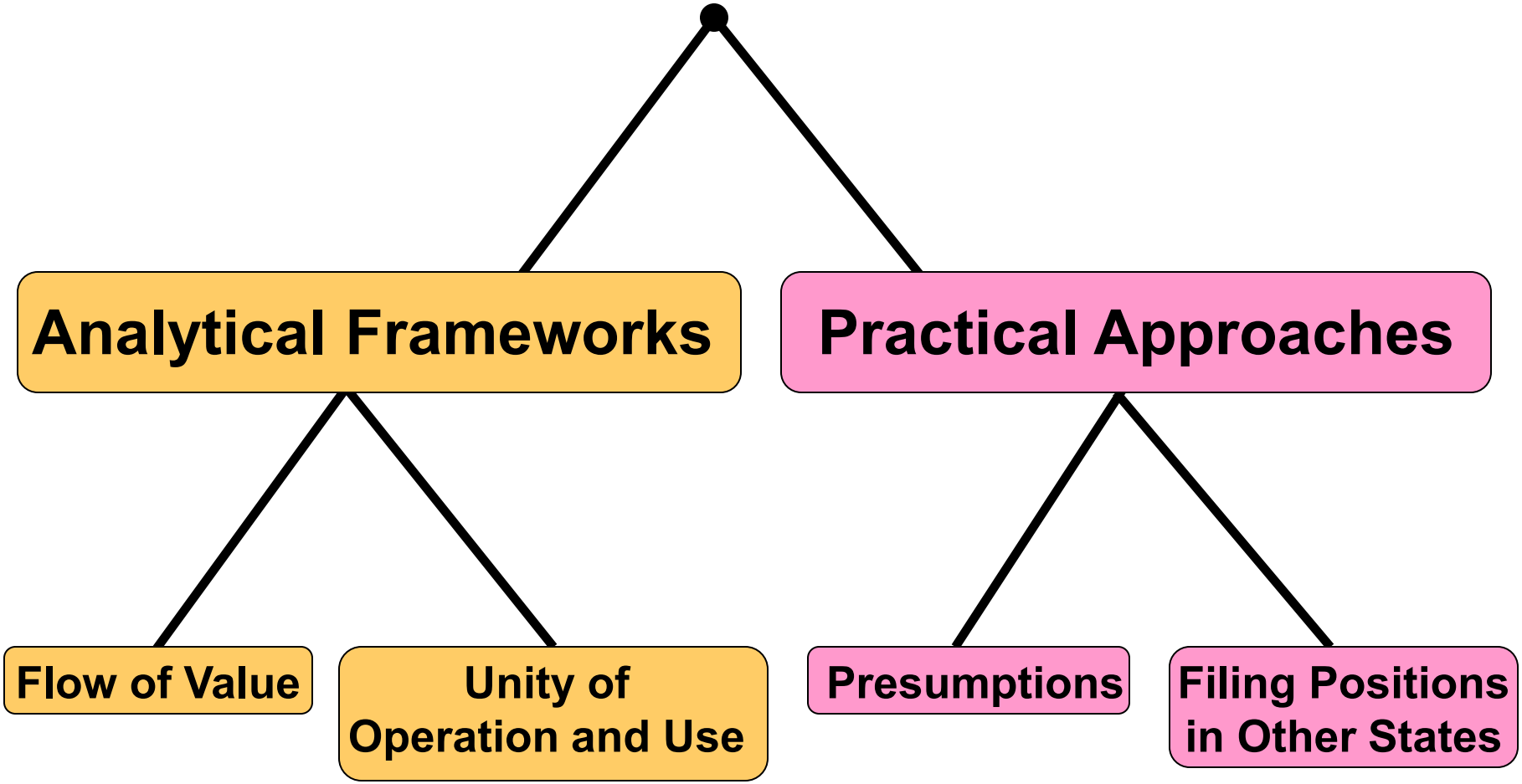
Reference: Section Tax 2.61(3)(a), Wis. Admin. Code

Test 2: Unitary Business

- The concept of a “unitary business” extends to non-corporate entities such as individuals
- Individuals, corporations, or other entities related under sections 267 or 1563 of the Internal Revenue Code can be a “unitary business”
- It is possible for corporations to be “related” for purposes of Test 2 without being in a “commonly controlled group” for purposes of Test 1

Reference: Section Tax 2.62(2)(a), Wis. Admin. Code

Methods of Identifying a Unitary Business



Analytical Frameworks for Identifying a Unitary Business

If the answer is “yes” to either of the questions below, the participants in the commonly owned enterprise are engaged in a unitary business:

- **Analytical Framework #1:** Is there sharing, exchange, or flow of value within the commonly owned enterprise?

- **Analytical Framework #2:** Is there unity of operation and use in the commonly owned enterprise?

Analytical Framework #1: Evidence of Sharing, Exchange, and Flow of Value

- The companies contribute or are expected to contribute in a nontrivial way to each other's profitability, or
- The companies are dependent on each other for achieving nontrivial business objectives, or
- The group offers one or more participants some economies of scale or economies of scope that benefit the group's enterprise, or
- Prices between the companies are not arms-length
  *(**Note:** If prices are arms-length, that does not negate in any way that a unitary business may exist)*

Reference: Section Tax 2.62(3)(a), Wis. Admin. Code

Examples of Specific Activities That Evidence Flow of Value

- Assisting in acquisition of assets
- Assisting with filling personnel needs
- Lending, guaranteeing loans, or pledging assets
- Common future planning or enterprise development
- Providing technical assistance, operational guidance, or overall strategic advice
- Supervising
- Sharing use of trade names, patents, or other intellectual property

Reference: Section Tax 2.62(3)(b), Wis. Admin. Code

Analytical Framework #2: Unity of Operation and Use

- Unity of operation means there is functional integration among the participants in the enterprise

- Unity of operation is evidenced by shared support functions, such as:
  - Centralized purchasing, marketing, advertising, accounting, or R&D
  - Intercorporate sales or leases
  - Intercorporate services
  - Intercorporate debts
  - Intercorporate use of proprietary materials

Reference: Section Tax 2.62(4)(b), Wis. Admin. Code

Unity of Operation and Use

- To be a “unitary business” under this analytical framework, the enterprise must also have unity of use

- Unity of use is evidenced by centralized management or use of centralized policies, such as:
  - Centralized or interlocking executive force
  - Intercompany employee transfers
  - Common employee and executive training programs
  - Common recruiting, hiring, and personnel policies
  - Common employee benefit programs

Reference: Section Tax 2.62(4)(c), Wis. Admin. Code

Practical Ways to Identify a Unitary Business

- **Practical approach #1:** Follow presumptions provided in Wisconsin Administrative Rules
- **Practical approach #2:** Follow the filing positions taken in other states, with some important exceptions

Practical Approach #1: Presumptions

A group of commonly owned persons or entities is presumed to be a unitary business when:

- The group's activities are all in the same general line of business
- The members of the group are engaged in different steps of a vertically structured enterprise
- There is strong central management coupled with the existence of centralized departments or affiliates for such functions as financing, advertising, R&D, or purchasing

References: Section Tax 2.62(6)(a) to (c), Wis. Admin. Code

More Presumptions

- A corporation that has different business segments is presumed to be engaged in the same unitary business throughout the corporation
- If a corporation forms a new corporation, the forming corporation and new corporation are presumed to be in a unitary business with one another from the formation date
- If a corporation acquires a new corporation, the acquired corporation is presumed to be NOT unitary for the taxable year that includes the acquisition
  - Except in cases where the corporations would have been engaged in a unitary business prior to the acquisition, had they been commonly owned at that time

References: Section Tax 2.62(6)(d) to (f), Wis. Admin. Code

Practical Approach #2:
Tax Filing Positions in Other States

- Generally, if a company files a combined return in another state as part of a unitary business, it should also file combined returns in Wisconsin

- Wisconsin Form 6, Part VI, line 14 requires taxpayers to disclose whether a company that is considered unitary for Wisconsin purposes is considered nonunitary in another state

Cautions and Exceptions for Practical Approach #2

- Section 71.255(1)(n), Wis. Stats., provides that "unitary business" shall be construed to the broadest extent permitted by the U.S. Constitution
- However, some states may have a more restrictive definition
- A state may allow a corporation to elect to file a combined return in another state even if the state doesn't consider it part of a unitary business
  - If this is the case, the filing position in that state should have no effect on the position taken for Wisconsin

Passive Holding Companies

Wisconsin Administrative Rules specifically provide that passive holding companies are deemed (not just presumed) to be part of a unitary business, as follows:

- A passive holding company that is part of a commonly owned enterprise and holds intangible assets that are used in the enterprise's unitary business is engaged in that unitary business

- A passive parent holding company that controls operating company subsidiaries engaged in a unitary business is also part of that unitary business

Reference: Section Tax 2.62(7), Wis. Admin. Code

Pass-Through Entities

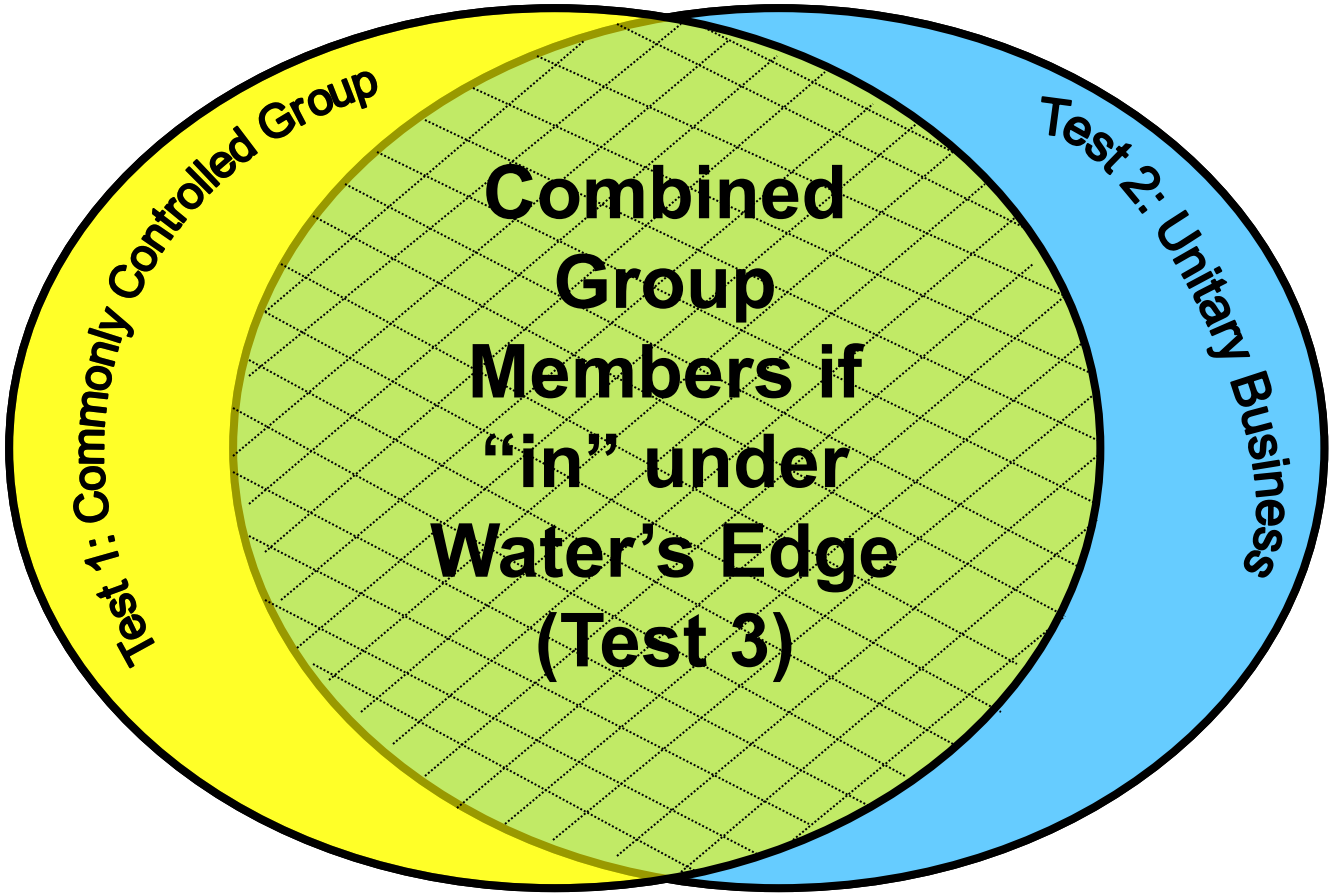
- In determining the scope of a unitary business, the business of a pass-through entity owned by a corporation is considered to be the business of the corporation to the extent of its distributive share

- A pass-through entity is treated as an extension of its owner

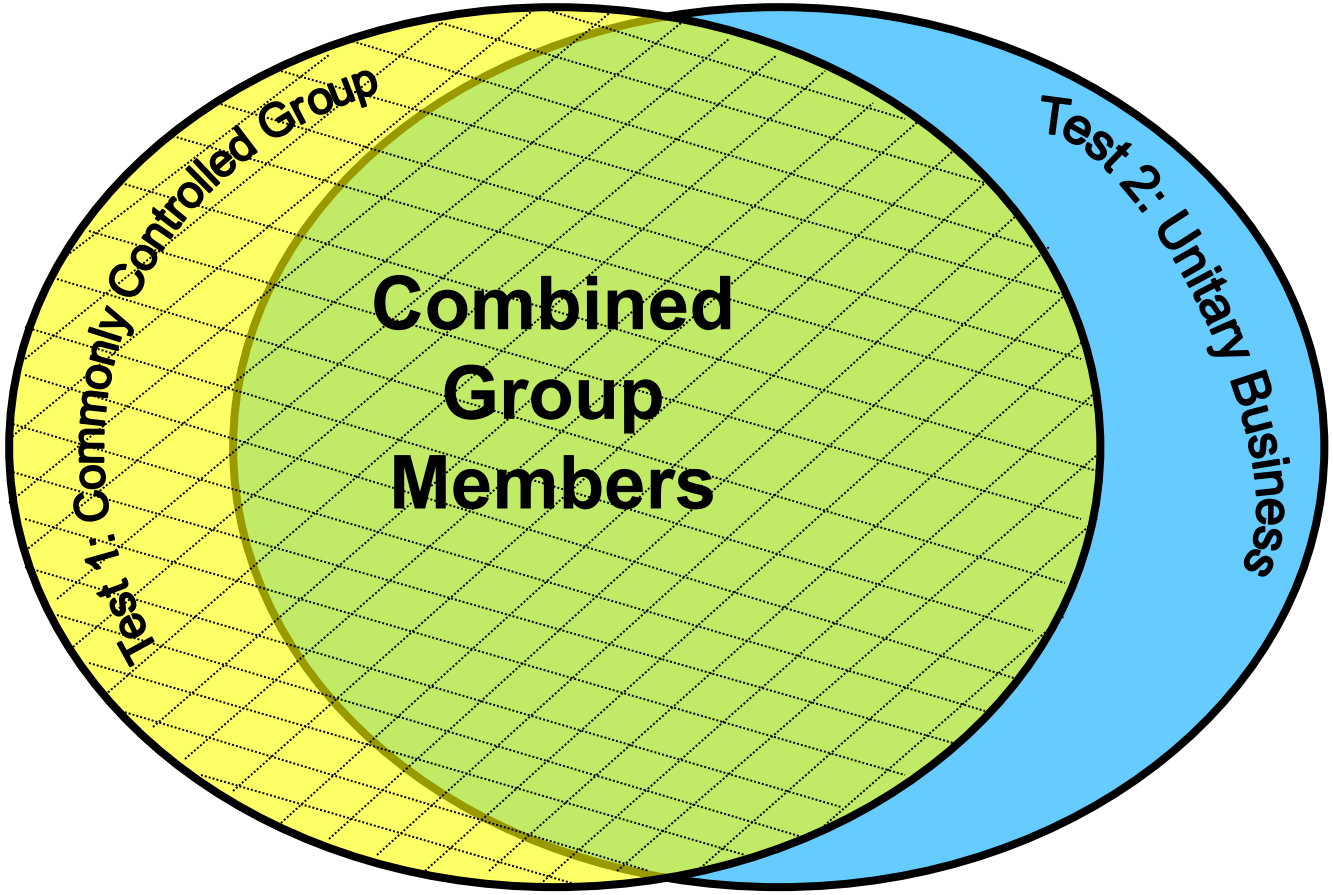
  – *Exception:* REITs, RICs, REMICs, and FASITs are not treated as an extension of their owners even though they are defined as “pass through entities” for purposes of determining if combined reporting applies

Reference: Section Tax 2.62(8), Wis. Admin. Code

Summary of Tests 1 and 2



Opt-out of Test 2:
Controlled Group Election



A commonly controlled group may make an election that the entire commonly controlled group is a combined group

Controlled Group Election

- Eliminates need to determine who is unitary
- Make the election by "checking the box" on Form 6, page 1, box D6 and submitting statement with the return that indicates each corporation has agreed to be bound by the election
- Election is binding for ten year period
- Applies to any corporations that subsequently enter the commonly controlled group during the ten year period

References: Sections Tax 2.63(2) and (3), Wis. Admin. Code

If the Controlled Group Election Applies:

- All income/loss of the entire commonly controlled group is deemed to be derived from a single unitary business
- All members of the controlled group are considered to be combined group members and therefore have nexus in Wisconsin
  - Also means that the activities of all members of the controlled group may be considered when determining if throwback sales apply
- The water's edge rules (Test 3) still apply and would exclude items from the combined amounts accordingly

References: Sections Tax 2.61(2)(b), (4)(h)2. and 3., and (4)(h), Wis. Admin. Code

Test 3: Water's Edge Rules

- Except where the controlled group election applies, a corporation that meets both Test 1 and Test 2 is not a combined group member unless it has something that is required to be "combined"

- The water's edge rules provide that corporations that are either foreign corporations or have a substantial amount of business conducted outside the U.S. are not required to (and cannot) include certain income/loss or apportionment factors in the combined amounts

Reference: Section Tax 2.61(4), Wis. Admin. Code

Factors That Control a Corporation's Status Under Water's Edge Rules

First Factor: Whether the corporation is foreign or domestic

Second Factor: Whether the corporation is an "80/20 corporation"

Third Factor: Sourcing of the corporation's income as either foreign source or U.S. source

Reference: Section Tax 2.61(4), Wis. Admin. Code

First Water's Edge Factor: Foreign vs. Domestic Corporation

- Generally based on where the corporation was incorporated or organized
- 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 it as a branch or disregarded entity for U.S. purposes, then it is treated as a branch of its owner rather than a separate foreign corporation
- A foreign corporation that is also an "80/20" corporation is considered domestic if it elects to be included in a federal consolidated return

References: Section Tax 2.61(4)(a) and (e)3., Wis. Admin. Code

Second Water's Edge Factor: "80/20" Status of Corporation

- A corporation is considered an "80/20 corporation" if 80% or more of its worldwide gross income during its taxable year is "active foreign business income" as defined in section 861(c)(1)(B) of the Internal Revenue Code
- A disregarded entity's active foreign business income and worldwide income must be combined with those of its owner

Reference: Section Tax 2.61(4)(b), Wis. Admin. Code

Who Is In The Group Under The Water's Edge Test So Far…

(Assumes Test 1 and Test 2 are already met)

Is it an "80/20" corporation?

Is it foreign or domestic?

	Not "80/20"	**"80/20"**
Domestic Corporation	In	Depends
Foreign Corporation	In	Out

Reference: Section Tax 2.61(4)(d) and (e), Wis. Admin. Code

Third Water's Edge Factor: Income Sourcing

- "Foreign source" vs. "U.S. source" is determined by sections 861 – 865 of the Internal Revenue Code
- All income that is "effectively connected" with conducting a trade or business within the U.S. is considered U.S. source
  - "Effectively connected income" can still be "active foreign business income" for purposes of the 80/20 test, to the extent not inconsistent with Internal Revenue Code

Reference: Section Tax 2.61(4)(c), Wis. Admin. Code

Effect of Sourcing Rules

	Not "80/20"	"80/20"
Domestic Corporation	**What's "in":** • U.S. source items • Foreign source items	**What's "in":** • Only items that are both: → U.S. source*, and → Specifically listed in s. 71.255(2)(d), Stats.
Foreign Corporation	**What's "in":** • U.S. source* items only	(All items excluded)

*U.S. source items include all effectively connected income

References: Section Tax 2.61(4)(d) and (e), Wis. Admin. Code

Includable Items for "Domestic 80/20's"

(Items specifically listed in s. 71.255(2)(d), Wis. Stats.)

- Interest income or income from intangible property, regardless of where payment is made
- Income derived from interest or intangible expenses of other combined group members, to the extent not already included per above
- Dividends from a non-qualified (i.e. "captive") REIT
- Gains or losses from the sale or lease of real or personal property located in U.S.
- Expenses or deductions and apportionment factors related to the above

Reference: Section Tax 2.61(4)(f), Wis. Admin. Code

Issues Related to Water's Edge Test

- For combined group members, items excluded from the combined items under the water's edge test must still be reported to Wisconsin if they have a Wisconsin situs
  - These items are called "separate entity items"
- If a corporation's income is not taxable for federal purposes under the provisions of a federal treaty, it is not taxable for Wisconsin purposes and is not includable in the combined items
  - Related expenses and apportionment factors must also be excluded

References: Section Tax 2.61(4)(g) and (h), Wis. Admin. Code

How Does a Combined Group Determine its Liability and File a Return?

- Taxable Years
- Designated Agent
- Combined Returns in General
- Walk-through of Forms and Computations

Taxable Year of Combined Group

- If one or more combined group members also file a federal consolidated return, the combined group's taxable year is the taxable year of the federal consolidated return

- If there is no federal consolidated return (or >1 federal consolidated return), the combined group's taxable year is the taxable year of the designated agent corporation

Reference: Section Tax 2.67(3)(a), Wis. Admin. Code

Taxable Year in Combined Return

- If a member has a different taxable year than the combined group, the group elects to include that member in the combined return in one of two ways:
  1. Preparing a separate income statement for the months included in the combined group's taxable year
  2. Using the amounts for the member's taxable year that ends during the combined group's taxable year
- The same method must be used for all members with differing taxable years, and the election is irrevocable unless the Department grants approval

References: Section Tax 2.67(3)(b) and (c), Wis. Admin. Code

Designated Agent

- The combined return is filed under the FEIN of the designated agent corporation
- The designated agent may be any member of the combined group, as long as the group and its designated agent are on the same taxable year
- The designated agent is responsible for all matters relating to the combined return, including making estimated payments

References: Sections Tax 2.65(2) and (3), Wis. Admin. Code

Designated Agent

- The designated agent is not required to identify itself as the designated agent before filing combined returns
- The corporation which files the first return for a combined group is deemed to be appointed as the designated agent
- The designated agent must be the same for each subsequent year, unless:
  - The designated agent leaves the group, or
  - The Department grants approval to change the designated agent

Reference: Section Tax 2.65(2), Wis. Admin. Code

Combined Returns in General

- "Combined report" = "Combined return"
- A combined return means one Wisconsin Form 6, with supporting forms and schedules described later
  - "100% Wisconsin" combined groups simply enter "100.0000%" as the apportionment percentage
  - Form 6 accommodates insurance companies
- Combined returns are required to be filed electronically

References: Sections Tax 2.60(2)(c) and (d), and 2.67(2)(b), Wis. Admin. Code

Combined Returns in General

- If a member enters or leaves a combined group during the year, the combined return includes that member's items for the part of the year that it was a member
- If a combined group member has "separate entity items," they generally must be included in the combined return; however, the tax effect of including them in the combined return is no different than including them on a separate return
- At taxpayer's option, a combined return may also include "separate entity items" of corporations that meet Tests 1 and 2 but aren't combined group members because of the water's edge rules

References: Sections Tax 2.67(2)(d) and (3)(d), Wis. Admin. Code

A Combined Return Must Include:

- A copy of federal Form 851, Affiliations Schedule, if the combined group also files in a federal consolidated return
- A copy of the complete federal return for each combined group member
- For combined groups that also file in federal consolidated returns, this may be done using any of the options on the next slide

Reference: Section Tax 2.67(2)(c), Wis. Admin. Code

Options for Providing Copy of Federal Return

- Complete copy of the federal consolidated return
- Pro forma separate federal returns for each combined group member, including all supporting forms and schedules for each member
- 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 any supporting forms, schedules, and statements that were submitted to the IRS pertaining to each member

Reference: Section Tax 2.67(2)(c)6., Wis. Admin. Code

Form 6, Part I, line 33: Adjustment for Intercompany Deferrals

- Income, expense, gain, or loss on transactions between combined group members is deferred in the same way as for federal consolidated group members under Treas. Reg. §1.1502-13

- The deferral applies even if the combined group is not a consolidated group for federal purposes

- Deferral is required to the extent the income, expense, gain, or loss would otherwise be in the combined unitary income

Reference: Section Tax 2.61(6)(b), Wis. Admin. Code

When Intercompany Deferrals Are Recognized

Events that trigger recognition of deferred intercompany transactions:

- The buyer resells the object of the transaction outside of the combined group
- The object of the transaction is used outside the unitary business
- The buyer and seller are no longer members of the same combined group

Reference: Section Tax 2.61(6)(b), Wis. Admin. Code

Computing the Adjustment on Form 6, Part I, Line 33

- Subtract the total amount deferred or recognized under Treas. Reg. §1.1502-13 within the federal consolidated group

- Add the total amount deferred or recognized under Treas. Reg. §1.1502-13 within the Wisconsin combined group
  - When computing gain/loss on sales of assets, use the federal basis, as differences between federal and Wisconsin basis are accounted for later in the Wisconsin additions and subtractions

Reference: Section Tax 2.61(6)(a)3., Wis. Admin Code

Form 6, Part I, line 30: Recomputed Net Capital Gain

- On Form 6, capital gains and losses, section 1231 gains and losses, and involuntary conversions are reversed out in Part I and recomputed on lines 30 and 32

- This is because the capital loss limitation applies at the combined group level similar to how it applies at the consolidated group level for federal purposes under Treas. Regs. §1.1502-22 and 1.1502-23

- However, capital loss carryovers can only be used at the combined group level if they are “sharable losses”

Reference: Section Tax 2.61(6)(c), Wis. Admin. Code

What Are "Sharable Losses?"

A sharable loss is a loss which satisfies both of the following:

- Is incurred by a combined group member in a taxable year beginning on or after January 1, 2009, and
- Is attributable to combined unitary income included in a combined return of the same combined group that uses the sharable loss

References: Sections Tax 2.61(6)(c)2., and (9)(a), Wis. Admin. Code

More on Sharable Losses

- If the member that originated the loss leaves the group, it may not share that loss with any other combined groups
  - However, if it is part of a subgroup that together joins another group, it can still share with that subgroup
- New combined group members may use shared losses even if they were not in the group when the loss originated

References: Sections Tax 2.61(6)(c)2., (9)(a), (e), and (f), Wis. Admin. Code

Computing the Amount on Form 6, Part I, line 30:

Complete a new federal Schedule D and the federal forms that flow into it as if the combined group is a single taxpayer, except:

- On Schedule D, line 6, include only the sharable amount of net capital loss carryovers (in 2009 this will generally be zero)
  - Non-sharable capital loss carryovers are accounted for later on Form 6CL

Computing the Amount on Form 6, Part I, line 30:

- Use the federal basis of assets in this computation, since differences between federal and Wisconsin basis are accounted for later in the Wisconsin additions and subtractions
  (Section Tax 2.61(6)(a)3., Wis. Admin. Code)
- Do not include gains or losses that are not includable in combined unitary income
  - Capital gains and losses attributable to separate entity items may have to be accounted for later on Form N

Form 6, Part I, line 32: Recomputed Charitable Contributions

- The charitable contributions deduction limitation applies at the combined group level similar to how it applies at the consolidated group level for federal purposes under Treas. Reg. §1.1502-24

- Unused charitable contribution deduction carryovers are automatically sharable, regardless of when incurred, as long as they have not expired

- The amount to enter on line 32 is the recomputed amount, since the federal amount has already been reversed out on line 31

Reference: Section Tax 2.61(6)(d), Wis. Admin. Code

Form 6, Part II, Line 2: Additions

- If any members have credits that must be added to Wisconsin income, those amounts flow through from the members' credit schedules

- If any members are insurance companies, the additions that apply specifically to insurance companies flow through from Part I of each applicable member's Form 6I

Additions from Schedule RT
(Addbacks of Related Entity Expenses)

- Addbacks for related entity expenses are not required for transactions between combined group members if the both the payer's expense and payee's corresponding income are included in the combined unitary income (causing a "wash")

- These "washed out" transactions need not be reported on Schedule RT either

Reference: Section Tax 2.61(6)(a)6., Wis. Admin. Code

When Addback Modifications Are Required in a Combined Return

- Required in cases where an expense subject to addback is included in combined unitary income but the corresponding income is or was not included in the group's combined unitary income, such as:
  - An expense paid to a related entity that is not a combined group member
  - An expense paid to a combined group member that excluded the corresponding income from the combined items under the water's edge rules

Reference: Section Tax 2.61(6)(a)6., Wis. Admin. Code

Expenses Subject to Addback

- Interest expenses

  Section 71.22(3m), Wis. Stats.

- Rent expenses

  Section 71.22(9an), Wis. Stats.

- Intangible expenses

  Section 71.22(3g), Wis. Stats.

- Management fees

  Section 71.22(6d), Wis. Stats.

Form 6, Part II, Line 4: Subtractions

- If any members are insurance companies, the nontaxable income from life insurance operations flows through to line 4n from Part II of each applicable member's Form 6I

Subtraction for Dividends

- Dividends subtracted on Form 6Y can be subtracted because they are eligible for either:

  A. The dividends received deduction under sec. 71.26(3)(j), Wis. Stats., or

  B. The elimination of dividends between combined group members under sec. 71.255(4)(f), Wis. Stats.

- If a dividend is eligible for a subtraction under **both** situations A. and B. above, the dividend is subtracted under the dividends received deduction provided in sec. 71.26(3)(j), Wis. Stats. (i.e. the regular dividends received deduction is the default)

Reference: Section Tax 2.61(6)(e)1., Wis. Admin. Code

Elimination of Dividends

- If the dividends received deduction does not apply, a dividend paid from one combined group member to another may be eliminated from combined unitary income under sec. 71.255(4)(f), Wis. Stats., to the extent that:
  - The dividend is paid out of earnings and profits attributable to net income or loss that was included in the group's combined unitary income in the current taxable year or a prior taxable year, and
  - The dividend does not exceed the payee's basis in the payer's stock

Reference: Section Tax 2.61(6)(e), Wis. Admin. Code

Transitional Rule for Earnings and Profits (E&P)

- A dividend paid out of pre-January 1, 2009 E&P may be eliminated to the extent that the net income that generated the E&P would have been included in the group's combined unitary income had the combined reporting law been in effect in those years

- Transitional rule applies only in situations where the regular dividends received deduction in sec. 71.26(3)(j), Wis. Stats., does not already apply

Reference: Section Tax 2.61(6)(e)3., Wis. Admin. Code

Computing Earnings and Profits

- Dividends are considered paid from current E&P first
- Exclude E&P attributable to:
  - Preacquisition income
  - Nonunitary income
  - Income not subject to combination under the water's edge rules

Reference: Section Tax 2.61(6)(e), Wis. Admin. Code

Computing Earnings and Profits

- If some E&P is not eligible for a particular year, the dividend is considered paid out of eligible and non-eligible E&P on a pro rata basis
- You may include E&P that "tiers up" from a lower-tier subsidiary under Treas. Reg. §1.1502-33, but only to the extent the lower-tier subsidiary's E&P is (or in the case of the transitional rule, would have been) attributable to items included in combined unitary income

References: Section Tax 2.61(6)(e)2. and (g), Wis. Admin. Code

Completing Form 6Y

- For each payer/payee combination, you may aggregate the total dividends paid during the combined group's taxable year

- For each payer/payee combination, indicate the reason for the subtraction by checking the appropriate box under "Payee's Ownership of Payer":
  - Check "> or = 70%" if the dividends received deduction under s. 71.26(3)(j), Stats., applies
  - Check "> 50% but < 70%" if the elimination of dividends under sec. 71.255(4)(f), Stats., applies

Form 6, Part II, Lines 2 and 4: Items That Can Be Either Additions or Subtractions

- Expense and gain/loss adjustments for depreciable and amortizable assets
- Gain/loss adjustments for sale of subsidiary stock

Gain/Loss Adjustments for Depreciable or Amortizable Assets

- Under sec. 71.265, Wis. Stats., the Wisconsin basis of depreciable or amortizable property for the first year a corporation becomes subject to tax in Wisconsin is its federal basis
  - This includes a corporation that first becomes subject to tax in Wisconsin in 2009 because it is a combined group member
- When such assets are sold, there may be no difference between federal and Wisconsin basis on the date of sale, in which case no adjustment would be necessary

References: Section Tax 2.61(6)(a)3., Wis. Admin. Code

Gain/Loss Adjustments for Sale of Subsidiary Stock

- A combined group member's stock basis in a subsidiary that is also a combined group member must be increased or decreased in a manner similar to that provided in Treas. Reg. §1.1502-32

- These adjustments are limited as described on the next slide

- The adjustments and limitations would generally cause gain or loss from the sale of a subsidiary to be different for Wisconsin purposes than for federal purposes

Reference: Section Tax 2.61(6)(f), Wis. Admin. Code

Subsidiary Stock Basis Adjustments: Income and Losses

- Basis in subsidiary stock is **increased** by the subsidiary's income and gains and **decreased** by its deductions and losses, but only to the extent the income, gains, deductions, or losses are <u>both</u>:
  - Taken into account for the subsidiary's taxable years beginning on or after January 1, 2009 and
  - Included in combined unitary income on a combined return for the same combined group
- The same limitations apply to basis adjustments that "tier up" from a lower-tier subsidiary

Reference: Section Tax 2.61(6)(f), Wis. Admin. Code

Subsidiary Stock Basis Adjustments: Distributions

- Basis in subsidiary stock is **decreased** by the subsidiary's distributions to the extent that the distributions were either:
  - Paid out of E&P attributable to items that were included in the group's combined unitary income, or
  - Eliminated from combined unitary income under the transitional rule regarding pre-January 1, 2009 E&P
- For purposes of determining stock basis adjustments for distributions, E&P is computed in the same manner as previously described for the dividend elimination

Reference: Section Tax 2.61(6)(f), Wis. Admin. Code

Line 6: Remove Separate Entity Items

- Form N, Part I computes a member's net income attributable to all separate entity items
- The total net income from all members' separate entity items must be subtracted from combined unitary income on Form 6, Part II, line 6

What Are Separate Entity Items?

Net income or loss attributable to:

- The combined group's unitary business but excluded from the combined items under the water's edge rules
- A separate unitary business
- Nonapportionable income
- The sale of or purchase and subsequent sale or redemption of lottery prizes

References: Sections Tax 2.60(2)(m), 2.61(5)(b) to (g), and 2.61(9)(b), Wis. Admin. Code

Cautions Regarding Amount Reported on Form 6, Part II, line 6

- The amount on Form 6, Part II, line 6 cannot include any amounts already subtracted from income on Form 6, Part II, line 4, and should include any amounts added to income on Form 6, Part II, line 2 which are attributable to separate entity items
- The amount on Form 6, Part II, line 6 must be net of all expenses or deductions directly or indirectly related to the separate entity items (may need to allocate indirect expenses)
  - This also applies to any amounts subtracted on Form 6, Part I that are attributable to corporations excluded from the combined group

References: Sections Tax 2.61(5) and (6)(h), Wis. Admin. Code

Form 6, Page 1, Line 2: Apportionment of Combined Unitary Income

- Does not apply to “100% Wisconsin” groups
- The group computes its total apportionment percentage on Form 6, Part III, line 1
- Each member must complete one of the following: Schedule A-01, A-02, A-03, A-04, A-05, A-06, A-07, A-08, A-09, A-10, or A-11

Numerators of Members' Apportionment Factors

- If one combined group member is doing business in Wisconsin relating to the unitary business, all combined group members are doing business in Wisconsin
  - All combined group members that have Wisconsin apportionment factors (numerators) are taxable
- Accordingly, when a combined group member computes its numerator on Schedules A-01, A-02, A-03, A-04, A-05, A-06, A-07, A-08, A-09, A-10, or A-11, it should not "throw back" sales destined for a state where <u>any</u> combined group member has nexus

References: Section Tax 2.61(7)(intro.) and (c), Wis. Admin. Code

Adjustments Required for Apportionment Factors

- In a combined return, the apportionment factors on Schedules A-01, A-02, A-03, A-04, A-05, A-06, A-07, A-08, A-09, A-10, or A-11 must exclude any amounts attributable to net income or loss that is not includable in combined unitary income
  - For example, sales for which the corresponding income or loss is excluded under the water's edge rules
- Apportionment factors related to separate entity items are accounted for later in Form N, Part II

References: Section Tax 2.61(7)(a)5. and (7)(b)5., Wis. Admin. Code

Intercompany Adjustments Required for Apportionment Factors

- Intercompany sales must be removed
- A combined group member's numerator and denominator cannot be increased by:
  - A sale from the combined group member to a pass-through entity that is more than 50% owned by combined group members
  - A sale to the combined group member from a pass-through entity that is more than 50% owned by combined group members

Reference: Section Tax 2.61(7)(d) and (e), Wis. Admin. Code

Other Intercompany Adjustments Required for Apportionment Factors

- If an intercompany sale is deferred and subsequently recognized in combined unitary income (per the computation on Form 6, Part I, line 33), the sale must be included in the apportionment factors in the year recognized

- If a combined group member sells an item to another member which in turn resells the item to a third party, the sale is treated as if sold directly by the member that made the initial sale

Reference: Section Tax 2.61(7)(d), Wis. Admin. Code

Form 6, Page 1, Line 4: Add Wisconsin Separate Entity Items

- Form N, Part II computes the Wisconsin portion of a member's items that were taken out of combined unitary income on Form 6, Part II, line 6
- If this amount includes capital gain or loss, the member should complete Form 6CL to determine the net capital gain to include on Form N, Part II
- If the member has separate entity items that are includable in another group's combined unitary income, those should be reported in that other combined return, not Form N

Nexus for Separate Entity Items

- By operation of sec. 71.255(5)(a), Wis. Stats., nexus is determined for the combined group as a whole

- Once a combined group has nexus, that nexus applies to all combined group members and applies equally to those members' combined items and separate entity items

- If a corporation would otherwise be a combined group member but is excluded under water's edge rules (i.e. all it has are separate entity items), its nexus is determined independently from the combined group's nexus

Reference: Section Tax 2.61(4)(h), Wis. Admin. Code

Apportionment for Separate Entity Items

- Separate entity items that are apportionable income are apportioned in Form N, Part II

- The apportionment percentage for separate entity items is computed as follows:
  - The numerator and denominator include only factors attributable to the separate entity items
  - Intercompany transactions are not excluded from the apportionment factors
  - If the corporation is a combined group member, it should not "throw back" sales destined for a state where <u>any</u> combined group member has nexus

Reference: Section Tax 2.61(4)(h)6., Wis. Admin. Code

Federal Limitations Applied to Separate Entity Items

- A combined group member applies federal limitations for capital losses and charitable contributions to its separate entity items independently from the limitations applied at the group level on Form 6, Part I
- Then, the member's share of any unused capital losses and charitable contributions from the computation of combined unitary income may be applied against separate entity items
- If a member has net capital gain from separate entity items, the member should complete Form 6CL before Form N to ensure that any unused capital loss from the current year's Form 6, Part I computation is used against separate entity items

References: Section Tax 2.61(6)(c) and (d), Wis. Admin. Code

Form 6, Page 1, Line 6: Net Capital Loss Adjustment

- A member may be eligible to claim a deduction for additional capital losses that could not be used in the computation of combined unitary income
  - Computation of capital gains and losses for combined unitary income were computed on Form 6, Part I, line 30
- To compute this deduction, the member completes Form 6CL

When the Net Capital Loss Adjustment Applies

The net capital loss adjustment applies when the following conditions exist:

- Net capital gain is included in combined unitary income, (i.e. there is an amount on Form 6, Part I, line 30), and
- The member has either or both of the following:
  - Non-sharable capital loss carryovers
  - Current year capital loss from separate entity items

Reference: Section Tax 2.61(6)(c)6., Wis. Admin. Code

Form 6, Page 1, Line 8: Loss Adjustment for Insurers

- As with pre-combined reporting law, an insurance company's net business loss must be computed without regard to the dividends received deduction under sec. 71.26(3)(j), Wis. Stats., and sec. 71.45(4), Wis. Stats.
  - If an insurance company has a net loss for the year, the dividends received deduction must be added back, to the extent it does not exceed the loss amount
- Insurance companies account for this limitation on Form 6I, Part III

Reference: Section Tax 2.61(9)(g), Wis. Admin. Code

Loss Adjustment for Insurers

- If a dividend that qualifies for the dividends received deduction is paid between combined group members and also qualifies for the elimination of dividends under sec. 71.255(4)(f), Wis. Stats., the dividend is considered to be eliminated under sec. 71.255(4)(f) for this purpose rather than deducted under the dividends received deduction
  - This is an exception to the general rule that the dividends received deduction takes precedence over the elimination of dividends in sec. 71.255(4)(f), Wis. Stats.

References: Sections Tax 2.61(9)(g)1. and 2., Wis. Admin. Code

Form 6, Page 1, Line 10: Business Loss Carryforward

- Each member uses Form 6BL to compute its available net business loss carryforward

Reference: Section Tax 2.61(9), Wis. Admin. Code

Form 6, Part III

- Each member's amounts on Form 6, Part III must add up to the total on each corresponding line of Form 6

- If the group chooses to include a nonmember corporation in the combined return for purposes of reporting that corporation's separate entity items, that corporation must be included in Form 6

- For combined groups that are "100% Wisconsin" corporations (i.e. their income is not apportioned), members have special instructions for computing their share of combined unitary income on Form 6, Part III

Form 6, Part III, Computations Unique to "100% Wisconsin" Groups

- A member's share of combined unitary income on Form 6, Part III, line 2 must be computed without regard to intercompany expenses paid, accrued, or incurred from one member to another
  - However, gain or loss from other intercompany sales is deferred and recognized under Treas. Reg. §1.1502-13 in the same manner as for combined groups that use apportionment
- If a member has a current year loss which was used to offset current year income of other members, the amount used must be reported on Form 6, Part III, line 3

Reference: Section Tax 2.61(8)(a), Wis. Admin. Code

Computation of Allowable Net Business Loss

- Prior to January 1, 2012, net business losses incurred before January 1, 2009 were non-sharable and each member's allowable net business loss on the 2009 combined return would be limited to that member's income

Reference: Section Tax 2.61(9), Wis. Admin. Code

Computation of Allowable Net Business Loss

- For taxable years beginning on or after January 1, 2012, up to 5% of net business losses incurred prior to January 1, 2009 and not used before January 1, 2012 may be shared among members of the same combined group
- This is known as the pre-2009 net business loss
- If the 5% shareable amount cannot be fully utilized during the taxable, the remaining amount may be added to the total pre-2009 shareable amount
- The pre-2009 net business losses have a 20 year carryfoward

How Net Business Losses Will Be Shared

- **Step 1:** Each member utilizes its own pre-2009 net business loss carryforward to the extent of its own income from separate entity items
  - Losses are considered used in the order incurred
- **Step 2:** Each member utilizes its own pre-2009 net business loss carryforward to offset its share of the Wisconsin combined groups net income
- **Step 3:** Each member uses its own post-2008 net business loss carryforward to offset its share of the Wisconsin combined groups Wisconsin income

Reference: Section Tax 2.61(9), Wis. Admin. Code

How Net Business Losses Will Be Shared

- **Step 4:** Each member uses its share of post-2008 net business loss carryforwards from other combined group members to offset its share of the Wisconsin combined groups Wisconsin income
- **Step 5:** Each member uses its share of the shareable pre-2009 net business loss carryover from other combined group members up to the allowable amount of 5% to offset its share of the Wisconsin combined groups Wisconsin income

Reference: Section Tax 2.61(9), Wis. Admin. Code

Other Notes on Sharing Net Business Losses

- A combined group member that has sharable loss carryforwards may choose not to include them in the aggregate sharable amount (i.e. not share them)
- Use Form 6BL to compute the Wisconsin net business loss carryforward for combined group members

Reference: Section Tax 2.61(9), Wis. Admin. Code

Tax Adjustment for Insurers

- The tax rate for insurance companies is generally the lesser of 7.9% of net income or 2% of gross premiums (sec. 71.46, Wis. Stats.)
- Insurance companies complete Form 6I, Part IV to compare their tax liabilities using the alternative computations
- Insurance companies that are combined group members use their Form 6, Part III amounts for the “7.9% of net income” computation

Tax Adjustment for Insurers

- If the “2% of gross premiums” computation applies, any net business losses that would have otherwise been used against the insurance company’s income are restored to the members that generated them

Reference: Section Tax 2.61(9)(g)3., Wis. Admin. Code

Form 6, Page 1, Line 13:
Nonrefundable Credits

- Nonrefundable credits are also reported on each applicable member's column of Form 6, Part V, and flow to Form 6, page 1, line 13
- Certain nonrefundable research credits may be shared among all group members
- The group computes its shared nonrefundable research credit amount on Form 6CS, which each member then uses in its computation of nonrefundable credits on Form 6, Part V

Sharable Credits

- The credits eligible for sharing are:
  - Nonrefundable research expense credits from Schedule R
  - Carryforwards of Development Zone research credits
  - Nonrefundable research credit carryforwards, except the super research and development credit

- The amount of these credits that may be shared includes the credit computed for the current taxable year plus any unused carryforwards

References: Section Tax 2.61(10)(b) and (c), Wis. Admin. Code

Sharable Credits

- Eligible nonrefundable research credit carryforwards are sharable to the extent the corporation with the credit was a member of that same combined group in the year the credit was generated

- Eligible research credit carryforwards generated before January 1, 2009 are sharable to the extent the corporation would have been a member of the combined group if combined reporting was in effect in the year the credit was generated

Reference: Section Tax 2.61(10)(c), Wis. Admin. Code

How to Share Nonrefundable Research Credits

- **Step 1:** Each member completes Form 6, Part V, lines 1 to 4 to utilize its total nonrefundable credits to the extent of its own tax liability
  - Credits are used in the order provided in sec. 71.30(3), Wis. Stats.
  - Each credit is used in the order it was generated
  - If a research credit amount used consists of both a sharable and non-sharable amount from the same year, the credit is considered used on a pro rata basis from each category

Reference: Section Tax 2.61(10)(c), Wis. Admin. Code

How to Share Nonrefundable Research Credits

- **Step 2:** Separate each member's available nonrefundable research credits into the sharable and non-sharable amount, if applicable

- **Step 3:** Enter each member's sharable amount on Form 6CS, and add those amounts to compute the aggregate sharable amount

  – As with losses, a member may choose not to share a sharable credit, in which case it would not include that amount in the aggregate sharable amount

- **Step 4:** Compute the combined group's tax liability eligible for shared credits on Form 6CS

Reference: Section Tax 2.61(10)(c), Wis. Admin. Code

How to Share Nonrefundable Research Credits

- **Step 5:** On Form 6CS, compute the percentage of the aggregate sharable amount to be applied to the combined return

- **Step 6:** Each member multiplies the percentage computed in Step 5 by the sharable amount computed in Step 1, and enters the result on Form 6, Part V, line 5, where it says *"...enter the amount shared with other combined group members as computed on Form 6CS. . . ."*

Reference: Section Tax 2.61(10)(c), Wis. Admin. Code

Modification of "Qualified Research" for Combined Group Members

- "Qualified research" does not generally include research that is funded by another party
  - Instead, the funding party may include 65% of the amount paid as "contract research" in its research expense credit
- However, if a combined group member does research that is funded by another member of the same combined group, the research is not considered to be funded by another party
  - The member actually doing the research could include the full amount of research expense in the credit, assuming it otherwise qualifies

Reference: Section Tax 2.61(10)(d), Wis. Admin. Code

Form 6, Page 1, Line 15:
Economic Development Surcharge

- Each member computes its economic development surcharge on Form 6, Part III, line 11
- The economic development surcharge is based on the member's gross tax and gross receipts reported on Form 6

Economic Development Surcharge

- Applies to each member of the combined group that has at least $4 million of gross receipts from all activities as reported on Form 6, Part VI, line 6

- The surcharge is 3% of gross tax as reported on the member's Form 6, Part III, line 9, with a minimum of $25 and maximum of $9,800

- Section 71.255(5)(a), Wis. Stats., provides that if any combined group member has nexus in Wisconsin for franchise or income tax purposes, all members of that combined group have nexus in Wisconsin for franchise or income tax purposes. This applies to the surcharge as well.

Form 6, Page 1, Line 19:
Estimated Payments

- In general, the combined group's designated agent must make estimated tax payments on behalf of the entire combined group (some exceptions apply)

Reference: Section Tax 2.66(2), Wis. Admin. Code

When a Member May Make its Own Estimated Payments

- For the first taxable year for which the combined group files a combined return
- For the first taxable year for which it is a member of the combined group
- For estimated taxes relating to any separate entity items

Reference: Section Tax 2.66(2), Wis. Admin. Code

Form 6, Page 1, Line 21:
Refundable Credits

- Each combined group member reports its refundable credits on Form 6, Part III, line 13
- After the credit is applied against the combined group's tax liability, any refundable amount is refunded to the designated agent

Reference: Section Tax 2.61(10)(b), Wis. Admin. Code

Form 6, Page 1, Line 26:
Underpayment Interest

- Required estimated payments and underpayment interest are computed by treating all companies in the combined return as a single taxpayer
- Required estimated payments may be based on:
  - 90% of tax shown on combined return for current year
  - 100% of tax shown on prior year's combined return(s), (eligible groups only; special rules apply to first combined return year)
  - Annualized income installment method

Reference: Section Tax 2.66(3), Wis. Admin. Code

Treating the Combined Group as a Single Taxpayer

- The threshold at which underpayment interest applies is $500 in combined tax liability
- A combined group may be eligible to base its estimated payments on its prior year's tax liability if the combined group's total Wisconsin net income (Form 6, Page 1, line 11) is less than $250,000
- If a member joins or leaves the group in the current taxable year or the preceding year, that change is not taken into account when determining required estimated payments based on the prior year's tax liability

References: Section Tax 2.66(3)(b) and (e), Wis. Admin. Code

Required Estimated Payments Based on Prior Year's Tax

- Generally, a combined group may base its required estimated tax payments on 100% of its prior year tax liability if all of the following are true:
  - The total net income on the combined return (Form 6, page 1, line 11) for the taxable year is less than $250,000
  - The combined group filed a combined return in the preceding year and that combined return covered a full 12 month period

Reference: Section Tax 2.66(3), Wis. Admin. Code

Special Rule for First Combined Return Year

- For its first combined return year, a combined group may base its estimated payments on the sum of the prior year tax liabilities shown on the separate returns of its members, but only if all of the following are true:
  - The total net income on the combined return (Form 6, page 1, line 11) for the taxable year is less than $250,000
  - Every combined group member filed a Wisconsin return in its preceding year and that return covered a full 12 month period

Reference: Section Tax 2.66(3)(f), Wis. Admin. Code

Applicable Laws and Rules

This document provides statements or interpretations of the following laws and regulations enacted as of January 10, 2023: sec. 71.255, Wis. Stats., and sec. Tax 2.61, Wis. Admin. Code.

Laws enacted and in effect after this date, new administrative rules, and court decisions may change the interpretations in this document. Guidance issued prior to this date, that is contrary to the information in this document is superseded by this document, according to sec. 73.16(2)(a), Wis. Stats.

FOR MORE INFORMATION

- **FOR MORE INFORMATION PLEASE CONTACT:**

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