Multistate Tax Commission

TO: PPWG – UNIFORMITY COMMITTEE LIAISON GROUP

FROM: ALAN H. FRIEDMAN, CONVENOR

SUBJECT: UNITARY BUSINESS DEFINITIONS

DATE: APRIL 2, 1999

I am writing to advise you of the outcome of my meeting with the MTC's Uniformity Committee on March 16th in New Orleans at which I described the current efforts of our PPWG-Uniformity Committee Liaison Group. I presented the reaction of some members that my earlier scheduling of teleconference meetings was too rigorous in terms of being able to concentrate, be constructive and communicate timely and effectively with one another. The Uniformity Committee concluded that so long as we were progressing, its timetable for considering our work product would be flexible. It has included our efforts as an agenda item for its next meeting in July in Traverse City, Michigan.

Given the input from the Uniformity Committee and those who have not been reluctant to call me merciless and maniacal, I have the following suggestions:

1. We should preserve the following teleconference meeting dates and times: Wednesday, April 14, May 5, May 26, June 9 and June 23 at 1:30 PM (Eastern). I recognize that this unilateral notice of times and dates may not fit into some of your schedules and I apologize for that. But, I could not see trying to find dates and times that met all of our schedules. I do hope that most of you can fit the Wednesday teleconferences into your workflow.

2. Our goal would be to finish by June 16th our work on alternative definitions under the Dependency/Contribution and alternative definitions for the Three Unities Test, with a look toward beginning the *Mobil* Factors Test. This should provide the Uniformity Committee with enough progress to continue relying on our efforts.

3. We should break into three working subgroups (see the attached list) after our April 14th teleconference with each of the three subgroups taking one slice of the Three Unities Test and *Mobil* Factors Test to develop through interim communications among subgroup members as may be needed. We will wait until after our work is done on the Three Unities Test to tackle the *Mobil* Factors Test; however, we should be sensitive to the fact that these two tests cross over one another at various places. A suggested calendar is as follows:

   Unity of Ownership/Functional Integration Subgroup teleconferences: April 28, May 12th and June 2nd at 11:30 PM (Eastern)

   Unity of Operations/Economies of Scale Subgroup teleconferences: April 28, May 12th and June 2nd at 1:30 PM (Eastern)

   Unity of Use/Centralized Management Subgroup teleconferences: April 28, May 12th and June 2nd at 4:30 PM (Eastern)

Please note the time intervals set between each subgroup teleconference. This permits all of you to attend all subgroup teleconferences should you wish by calling into 703-736-7307 at the appointed time. Only those assigned to a subgroup are expected to attend his/her subgroup; but all of us are to be treated as full members with equal voice as to any subgroup attended.

MTC staff will be responsible for setting up the teleconferences with Dialog Access and for issuing any notices required under the MTC Public Participation Policy. If either I or Paull Mines is present for the Subgroup discussion, we will take notes and record in bullet note fashion the proceedings and submit the bullet notes to the full PPWG-Uniformity Committee Liaison Group before its teleconferences. If, for some reason, neither Paull nor I are in attendance, I have noted with an "*" the party that should take notes and provide them to me for forwarding.

I have taken the input from our last teleconference on the Dependency/Contribution Test and the product is attached for your review. Please provide me with any written changes, additions and deletions you have for either of the two alternatives by **April 9th** so we can discuss them on the April 14th call. I am particularly interested in your developing more examples with more specificity than we now have.

I have also begun an initial beginning draft for the Three Unities Test that I hope (but can't promise) to get to you all by April 9th as well.

PROPOSED DEFINITION ONE OF
DEPENDENCY/CONTRIBUTION TEST
March 31, 1999

(DISJUNCTIVE)

I. Dependency/Contribution Test for Determining Unitary Business

A. Definitions.

For the purposes of this section, the following definitions shall apply and control:

1. "Business" means a single entity or two or more entities under common ownership or control with respect to which [this State's income/franchise tax] requires a determination of whether the entity or entities are conducting one or more unitary businesses within this State. [**Possible add on**: *In order to have "common ownership or control", it is not necessary for the common owner to have more than a ___% direct or indirect ownership in the entities or segments*.]

2. "Entity" means each type of organization that [this State's income/franchise law] recognizes as a reporting person, except such term does not include an individual or [insert other applicable exceptions].

3. "Segment" means a subdivision of an entity consisting of any grouping of business activities, functions or transactions.

B. Dependency/Contribution Test.

Alternative 1.

An entity or segment is part of a unitary business with entity or segment within the enterprise upon which it is dependent or to which it contributes, and with each entity or segment within the enterprise which is dependent upon or contributes to other entities or segments which are part of such unitary business. In order to satisfy this test, the entities and segments need not be interdependent or of mutual benefit to one another. This is illustrated by the following examples:

Example 1: Corporation A has an ownership interest in Corporations B, C, and D. Corporation A is dependent upon

or contributes to Corporation C. Corporation C is dependent upon or contributes to Corporation D. Corporation B does not contribute to and is not dependent upon Corporations A, C, or D. In this example, Corporations A, C, and D constitute a unitary business. This is the result even though Corporation A is not directly dependent upon and does not directly contribute to Corporation D.

Example 2: Corporation A has an ownership interest in Corporations B, C, and D. Corporation A consists of Segments A1, A2, and A3. The presumption that A1, A2, and A3 are part of a unitary business has not been successfully rebutted. Segment A1 is dependent upon or contributes to Corporation C. Corporation C is dependent upon or contributes to Corporation D. Corporation B does not contribute to and is not dependent upon Corporations A (or any of its segments), C, or D. In this example, Corporations A (including each of its segments), C, and D constitute a unitary business.

Example 3: Same as Example 2, except that the presumption that Segment A3 is part of a unitary business with the other segments of Corporation A has been successfully rebutted. Furthermore, Segment A3 does not contribute to and is not dependent upon Corporations C or D. In this example, Corporations A (including Segments A1 and A2), C, and D constitute a unitary business.

Alternative 2.

A unitary business includes each commonly owned or controlled entity or segment of the business whose operation is either dependent upon or contributes to the operation of at least one other entity or segment of the business. In order to satisfy this test, the operation of the entity or segment need not (i) contribute to or be dependent upon the operation of all other entities or segments; or (ii) be interdependent or of mutual benefit to one another. This is illustrated by the following examples:

[LIST EXAMPLES FOUND UNDER ALTERNATIVE 1 HERE]

C. Facts and Circumstances; Presumptions.

The determination of whether the operation of an entity or segment depends upon or contributes to the operation of another shall be determined by the facts and circumstances of each case. It shall be presumed, subject to rebuttal, that sufficient dependency or contribution exists between entities or segments thereof to form a unitary business enterprise when one or more of the following factors are present:

1. When the principal activities of the entities or segments are in the same general line of business. Illustrations of the same general line of business, but not limitations, are: manufacturing, wholesaling, retailing of tangible personal property, insurance, transportation or finance; or

2. When the entities or segments are engaged in different steps of a vertically structured business. Illustrations of such different steps, but not limitations, are: exploration, mining/drilling, production, refining, marketing, and/or transportation of natural resources; or

3. When there exists a strong centralized management among the entities or segments. Illustrations of such management, but not limitations, are: when activities such as purchasing, accounting, financing, tax compliance, legal services, human resources, health/retirement plans, product lines, capital investment, marketing and the like are determined by a central person or committee and not by each entity or segment; or

4. When the business segments are in the same entity.

[Note: There was support expressed to eliminate this subparagraph 4. as possibly duplicative of the other three subparagraphs, especially subparagraph 3.]

PROPOSED DEFINITION TWO OF
DEPENDENCY/CONTRIBUTION TEST
March 31, 1999

(CONJUNCTIVE)

I. Dependency/Contribution Test for Determining Unitary Business.

A. Definitions.

For the purposes of this section, the following definitions shall apply and control:

1. "Business" means a single entity or two or more entities under common ownership or control with respect to which [this State's income/franchise tax] requires a determination of whether the entity or entities are conducting one or more unitary businesses within this State. [**Possible add on**: *In order to have "common ownership or control", it is not necessary for the common owner to have more than a ___% direct or indirect ownership in the entities or segments*.]

2. "Entity" means each type of organization that [this State's income/franchise law] recognizes as a reporting person, except such term does not include an individual or [insert other applicable exceptions].

3. "Segment" means a subdivision of an entity consisting of any grouping of business activities, functions or transactions.

B. Dependency/Contribution Test.

Alternative 1.

An entity or segment is part of a unitary business with entity or segment within the enterprise upon which it is dependent or to which it contributes, and with each entity or segment within the enterprise which is dependent upon or contributes to other entities or segments which are part of such unitary business. In order to satisfy this test, the entities and segments need not be interdependent or of mutual benefit to one another. This is illustrated by the following examples:

Example 1: Corporation A has an ownership interest in Corporations B, C, and D. Corporation A is dependent upon

or contributes to Corporation C. Corporation C is dependent upon or contributes to Corporation A. Corporation B is dependent upon Corporation A, but does not contribute to either Corporations A, C, or D. Corporation D does not contribute to and is not dependent upon Corporations A, B, or C. In this example, Corporations A and C constitutes a unitary business.

Example 2: Corporation A has an ownership interest in Corporations B, C, and D. Corporation A consists of Segments A1, A2, and A3. The presumption that A1, A2, and A3 are part of a unitary business has not been successfully rebutted. Segment A1 is dependent upon and contributes to Corporation C. Corporation C is dependent upon and contributes to Corporation D, but is neither dependent upon nor contributory to Corporations A and B. Corporation B does not contribute to and is not dependent upon Corporations A (or any of its segments), C, or D. In this example, Corporations A (including each of its segments A1, A2 and A3), C, and D constitute a unitary business. This is the result even though Corporation A is not directly dependent upon and does not directly contribute to Corporation D.

Example 3: Same as *Example* 2, except that the presumption that Segment A3 is part of a unitary business with the other segments of Corporation A has been successfully rebutted. Furthermore, Segment A3 does not contribute to and is not dependent upon Corporations C or D. In this example, Corporations A (including only Segments A1 and A2), C, and D constitute a unitary business. This is the result even though Corporation A is not directly dependent upon and does not directly contribute to Corporation D.

Alternative 2.

A unitary business includes each commonly owned or controlled entity or segment of the business whose operation is either dependent upon or contributes to the operation of at least one other entity or segment of the business. In order to satisfy this test –

1. the entities and segments must be interdependent or of mutual benefit to one another; but,

2. the operation of the entity or segment need not contribute to or be dependent upon the operation of all other entities or segments.

This is illustrated by the following examples:

[LIST EXAMPLES FOUND UNDER ALTERNATIVE 1 HERE]

C. Facts and Circumstances; Presumptions.

The determination of whether the operation of an entity or segment depends upon or contributes to the operation of another shall be determined by the facts and circumstances of each case. It shall be presumed, subject to rebuttal, that sufficient dependency or contribution exists between entities or segments thereof to form a unitary business enterprise when one or more of the following factors are present:

1. When the principal activities of the entities or segments are in the same general line of business. Illustrations of the same general line of business, but not limitations, are: manufacturing, wholesaling, retailing of tangible personal property, insurance, transportation or finance; or

2. When the entities or segments are engaged in different steps of a vertically structured business. Illustrations of such different steps, but not limitations, are: exploration, mining/drilling, production, refining, marketing, and/or transportation of natural resources; or

3. When there exists a strong centralized management among the entities or segments. Illustrations of such management, but not limitations, are: when activities such as purchasing, accounting, financing, tax compliance, legal services, human resources, health/retirement plans, product lines, capital investment, marketing and the like are determined by a central person or committee and not by each entity or segment; or

4. When the business segments are in the same entity.

[Note: There was support expressed to eliminate this subparagraph 4. as possibly duplicative of the other three subparagraphs, especially subparagraph 3.]

MEMBERSHIP OF WORKING SUBGROUPS

Unity of Ownership/Functional Integration Subgroup

Brian Toman, CA Franchise Tax Board
Jerry Oxford, TX Comptroller of Public Accounts
John Parrish, KY Revenue Cabinet
Lennie Collins, NC Dept. of Revenue
Marshall Stranburg, FL Dept. of Revenue
Richard Truman, ME Revenue Services
Steven Krenkel, MN Dept. of Revenue
William Lunka*, MN Dept. of Revenue
John Warren, Loeb and Loeb
Leonard Hamilton, OR Dept. of Revenue

Unity of Operations/Economies of Scale Subgroup

Joe Thomas, CT Dept. of Revenue
Phil Plant, KPMG Peat Marwick
Robert Feinschreiber, Interstate Tax Report
Ted Spangler*, ID State Tax Commission
David Weeks, KS Dept. of Revenue
Karen Boucher, Arthur Andersen
Shona McHugh, MT Dept. of Revenue
Tom Bowen, AMP Incorporated
Richard Harris
Scott Heyman, Sidley & Austin

Unity of Use/Centralized Management Subgroup

Jennifer Hays, KY Revenue Cabinet
Gerard T. Andert, MO Dept. of Revenue
John Feldman, MO Dept. of Revenue
Mark Wainwright*, UT Attorney General Office
Roy Crawford, Brobeck, Phleger & Harrison
Terry Frederick, Sprint Corp.
Hattie Stancil, DC Office of Tax and Rev.
Tim Timmerman, Ford Motor Co.
Tom Yamachika, PricewaterhouseCoopers
John Sagaser, ME Revenue Services