

Combined Reporting Update: Controlled Group Election and Planning Opportunities

Combined reporting is now a fact of life for those Wisconsin corporations that are part of a commonly controlled group and meet the other requirements of Wisconsin's Combined Reporting law. Most Wisconsin corporations that will be subject to the new Combined Reporting law are likely familiar with some variant of combined reporting imposed by one or more of the 22 other states that have implemented combined reporting requirements. This e-alert looks at some of the planning opportunities presented by the careful use of a controlled group election.

Strategic Use of the Controlled Group Election

Wisconsin's Combined Reporting law requires a corporation to file on a combined basis if (1) the corporation is part of a commonly controlled group, (2) the corporations in the group are conducting a unitary business, and (3) the corporation meets the water's edge test. However, regardless of whether corporations are engaged in a unitary business, the Combined Reporting law permits a commonly controlled group of corporations to elect to be treated as a combined group. This option can provide tax planning opportunities. For example, a non-unitary corporate member may possess certain tax attributes that could be desirable (e.g., credits, losses) to other members covered by the controlled group election. Including such a non-unitary subsidiary in a controlled group may allow the remaining members of the group to benefit from those tax attributes.

Minimizing Throwback

While combined reporting and the new law on economic nexus are likely to minimize throwback liability for corporations operating in Wisconsin, there are a few situations that can throw income back to Wisconsin for tax purposes. In general, if a corporate subsidiary's only connection with a foreign state is that it makes sales that qualify for the safe harbor provided by Public Law 86-272, which sales, therefore, do not create nexus with the foreign state, the income from those sales may be thrown back to Wisconsin.

However, if that subsidiary is part of a controlled group and another member of

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the controlled group has nexus in that foreign state, then, under rules adopted by the Wisconsin Department of Revenue (WDR), the income from sales in that foreign state is not thrown back to Wisconsin. According to the WDR, this results because if one member of the group has nexus with another state, all other members of the group are deemed to have nexus for purposes of throwback. To take advantage of this situation, it may make sense to make a controlled group election to include a non-unitary subsidiary that is making sales that qualify under Public Law 86-272 as a strategy to reduce or eliminate throwback.

Initial Basis

Up until recently, the WDR has taken the position that the initial basis for the assets of a corporation that become subject to Wisconsin's corporate franchise/income tax is the federal tax basis of these assets. Since depreciation under the Internal Revenue Code is far more rapid, this means that these assets will have a much lower initial basis than if the corporation had been subject to Wisconsin's corporate income/franchise tax law for prior years. This position would certainly deter taxpayers from electing to include in their controlled group those affiliates not previously taxed in Wisconsin because their initial basis would be so low.

However, the WDR has now determined that the initial basis for corporations that become subject to Wisconsin tax should be the federal basis as defined for Wisconsin purposes. This removes initial basis as an obstacle to including certain subsidiaries in a controlled group election.

Review by the WDR

When making a controlled group election, one has to exercise caution because the WDR has the authority to void the election if it determines that the primary effect of the election is tax avoidance. Note that when the WDR makes this determination, it may not simply remove one or more "offending" corporations from the controlled group. Rather, the WDR's rules require that the entire election be voided and that no new election occur for at least three tax years.

If you have any questions about the implications of the combined reporting requirements and whether a controlled group election may be beneficial, feel free to contact any member of the [Reinhart State and Local Tax Team](#).



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