WEST VIRGINIA
SECRETARY OF STATE
NATALIE E. TENNANT
ADMINISTRATIVE LAW DIVISION

Form #2

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OFFICE WEST VIRGINIA SECRETARY OF STATE

NOTICE OF A COMMENT PERIOD ON A PROPOSED RULE

AGENCY: State Tax Department TITLE NUMBER: 110

RULE TYPE: Legislative CITE AUTHORITY W. Va. Code §§11-10-5 and 11-24-1

AMENDMENT TO AN EXISTING RULE: YES X NO _____

IF YES, SERIES NUMBER OF RULE BEING AMENDED: 24

TITLE OF RULE BEING AMENDED: Corporate Net Income Tax

IF NO, SERIES NUMBER OF RULE BEING PROPOSED: _____

TITLE OF RULE BEING PROPOSED: _____

IN LIEU OF A PUBLIC HEARING, A COMMENT PERIOD HAS BEEN ESTABLISHED DURING WHICH ANY INTERESTED PERSON MAY SEND COMMENTS CONCERNING THESE PROPOSED RULES. THIS COMMENT PERIOD WILL END ON July 27, 2009 AT 5:00 pm. ONLY WRITTEN COMMENTS WILL BE ACCEPTED AND ARE TO BE MAILED TO THE FOLLOWING ADDRESS:

Legal Division
State Tax Department
P.O. Box 1005
Charleston, WV 25324-1005

THE ISSUES TO BE HEARD SHALL BE LIMITED TO THIS PROPOSED RULE.

Virgil T. Helton
Cabinet Secretary of the Department of Revenue

ATTACH A **BRIEF** SUMMARY OF YOUR PROPOSAL

SUMMARY OF TITLE 110, SERIES 24 LEGISLATIVE RULE

Legislation was passed on March 20, 2007 (SB 749) and March 8, 2008 (SB 680), which requires combined reporting in West Virginia. The combined report provisions were incorporated into the corporate net income tax statute, Chapter 11, Article 24 of the West Virginia Code.

Combined reporting is a tax reporting method where all of the members of a unitary group are required to determine their net income based on the activities of the unitary group as a whole. Unitary group members that have nexus with West Virginia apportion the total group income to West Virginia through an apportionment formula.

Combined reporting treats each filer as part of one business – part of the unitary group. If the income reported to West Virginia is the income of all of the unitary businesses apportioned to West Virginia, then the related corporations are: less able to shift income out of West Virginia and less able to shift expenses into West Virginia. And so are less able to manipulate and decrease taxable income.

Regulatory guidance relating to this reporting method addresses such issues as:

How to reconcile reporting periods for corporations belonging to the same combined group which have different tax reporting years, For example one corporation may be a calendar year file, but another may file on a tax year beginning October 1.

How to treat intercompany transactions so that they are not subject to manipulation to decrease net taxable income.

How to compute apportionment factors based on the combined group. West Virginia uses an apportionment formula based on:

A property factor,
A payroll factor and
A double weighted sales factor.

How to determine a combined group for a particular tax year when there have been corporate mergers, acquisitions, split ups and divestitures during the reporting period.

This proposed legislative rule repeals the Corporate Net Income Tax Rule and replaces it with a version that combines the requirements of corporate net income tax with the combined reporting requirements outlined in SB 749 and SB 680.

110 CSR 24
CORPORATION NET INCOME TAX
STATEMENT OF CIRCUMSTANCES

Legislation was passed on March 20, 2007 (SB 749) and March 8, 2008 (SB 680), which requires combined reporting in West Virginia. The combined report provisions were incorporated into the corporate net income tax statute, Chapter 11, Article 24 of the West Virginia Code.

This proposed legislative rule repeals the Corporate Net Income Tax Rule and replaces it with a version that combines the requirements of corporate net income tax, contained in West Virginia Code §§11-24-1, *et seq.*, with the combined reporting requirements outlined in SB 749 and SB 680.

TITLE 110
LEGISLATIVE RULES
DEPARTMENT OF TAX AND REVENUE

SERIES 24
CORPORATION NET INCOME TAX

§110-24-1. General.

1.1. Scope. -- These legislative regulations are intended to explain and clarify the West Virginia Corporation Net Income Tax as set forth in W. Va. Code §§11-24-1, *et seq.* This rule repeals and replaces all prior Corporation Net Income Tax regulations.

1.2. Authority. -- W. Va. Code §§29A-3-1, et seq., 11-10-5.

1.3. Filing date. -- xxx.

1.4 Effective date. -- xxx.

1.5 General.—Repeal and replace.

§110-24-2. Introductory Statement.

The West Virginia Corporation Net Income Tax became effective July 1, 1967, and is a conformity tax in that it utilizes federal taxable income as a starting point to determine West Virginia taxable income and in that it adopts federal definitions wherever possible.

§110-24-3. Definitions.

3.1. Meaning of terms - general rule. -- Any term used in W. Va. Code §§11-24-1, *et seq.*, and in these regulations have the same meaning as when used in a comparable context in the laws of the United States of America, as those laws relate to federal income taxation, unless a different meaning is clearly required by the context or by specific definition in article twenty-four, or in these regulations.

3.1.1. Any reference in W Va. Code §§11-24-1, *et seq.*, and in these regulations, to the laws of the United States means the provisions of the Internal Revenue Code, as amended, and such other provisions of the laws of the United States of America as those laws relate to the determination of income for federal income tax purposes. Refer to W. Va. Code §11-24-3 for the most recent updating of terms used in W Va. Code §§11-24-1, *et seq.*

§110-24-4. Effect Of Rate Changes During Taxable Year.

4.1. If any rate of tax imposed in W. Va. Code §§11-24-1, *et seq.* changes to become effective before the thirty-first day of December of a calendar year, and if the taxable year included the effective date for the change of rate, then:

4.1.a. Tentative tax due is computed by applying the rate for the period before the effective date of the change of rate, and the rate for the period on and after such date, to the taxable income of the corporation for the entire taxable year; and

4.1.b. The tax for such taxable year shall be the sum of that proportion of each tentative tax which the number of months in each period bears to the number of months in the entire taxable year.

4.1.c. The above procedure may only be used when the date of the rate change is other than the first day of the taxable year.

4.2. For purposes of this Section:

4.2.a. If the rate changes for taxable years "beginning after" or "ending after" a certain date, the following day shall be considered the effective date of the change; and

4.2.b. If a rate changes for taxable years "beginning on or after" a certain date, that date shall be considered the effective date for the change of rate.

4.2.c However, if West Virginia Code §11-10-5p applies with relation to the effective date for a corporate net income tax rate change, then the rate change shall first apply to a particular taxpayer for taxable years beginning on or after the effective date of the act of the Legislature containing such rate change amendment.

4.3. Example. -- The West Virginia Legislature enacts a rate change for the corporation net income tax beginning after June 30. West Virginia Code §11-10-5p does not apply. The corporation net income tax liability for a calendar year taxpayer is calculated by applying the former rate for the months January through June, and the new rate for July and succeeding months. A fiscal year taxpayer would use the former rate for those periods of its tax year occurring before June 30.

4.4 . Example. -- The West Virginia Legislature enacts a rate change for the corporation net income tax beginning after June 30 of year 1. West Virginia Code §11-10-5p applies. The corporation net income tax liability for a calendar year taxpayer is calculated by applying the former rate for the tax year of January 1, year 1 through December 31, year 1, and the new rate for the tax year beginning January 1, year 2 and succeeding years. A fiscal year taxpayer would use the former rate for those periods of its tax year occurring before June 30 and through the end of its fiscal year, and the new rate for the next succeeding fiscal year beginning on or after the effective date of the act of the Legislature containing such rate change amendment

§110-24-5. Corporations Exempt From Tax.

5.1. Corporations exempt from the corporate net income tax in accordance with the provisions or West Virginia Code §§11-24-1, *et seq.*, including, but not limited to, West

Virginia Code §11-24-5, or exempt from the corporate net income tax under any other provision of the West Virginia Code or under any provision of superseding federal code or federal law are exempt from the corporate net income tax. However regulated investment companies and real estate investment trusts subject to the provisions of West Virginia Code §11-24-4b shall be subject to tax as specified therein.

5.1.a. Corporations which by reason of their purposes or activities are exempt from federal income tax are exempt from the corporate net income tax. However regulated investment companies and real estate investment trusts subject to the provisions of West Virginia Code §11-24-4b shall be subject to tax as specified therein.

5.1a.1. This exemption shall not apply to the unrelated business income, as defined in the Internal Revenue Code, of any such corporation if such income is subject to federal income tax.

5.1a.1.2. Example. -- A corporation exempt from federal income taxation under IRC 501(c)(3) receives $1,000,000 in cash donations and is bequeathed an unrelated business during the year. The tax exempt corporation operates the business for the remainder of its tax year. The income from operating this business is deemed unrelated business taxable income by the Internal Revenue Service. Such income would also be taxed under the West Virginia Corporation Net Income Tax. However, the donations would be exempt.

5.1a.2. Insurance companies which pay this State a tax upon premiums, and insurance companies that pay the surcharge imposed by West Virginia Code subdivisions 23-2C-3(f)(1) or (3) are exempt from the corporate net income tax.

5.1a.2.1. This exemption is available if an insurance company actually paid an insurance premium tax imposed by West Virginia law or the surcharge imposed by West Virginia Code, subdivisions 23-2C-3(f)(1) or (3) for any year in which an exemption is claimed or would have paid the premium tax but for the utilization by the taxpayer of any tax credits allowed or allowable against the premium tax.

5.1a.3. Corporations otherwise exempted from the corporation net income tax by superseding state of federal law are exempt from the corporate net income tax, e.g. racing associations, W. Va. Code §19-23-12; hospital service corporations, W. Va. Code §33-24-4; farmer's mutual fire insurance companies, W. Va. Code §33-22-16; licensed fraternal benefit societies, W. Va. Code §33-23-29.

§110-24-6 Reserved for future use.

§110-24-7. Allocation And Apportionment.

7.1. Net rents and royalties from tangible personal property are allocable to this State in accordance with West Virginia Code §11-24-7.

7.2 . The extent of utilization of tangible personal property in a state is determined by multiplying the rents and royalties by a fraction, the numerator of which is the number of days of physical location of the property in the state during the rental or royalty period in the taxable year and the denominator of which is the number of days of physical location of the property everywhere during all rental or royalty periods in the taxable year. If the physical location of the property during the rental or royalty period is unknown or unascertainable by the taxpayer, tangible personal property is utilized in the state in which the property was located at the time the rental or royalty payer obtained possession.

7.2.a. If the property is in this State for any part of a day, that time shall be counted as a full day.

Examples.

7.2.b. Corporation A was formed in Ohio and has its main offices there. Corporation A owns an apartment complex in West Virginia and leases computers to users located in West Virginia. The net rental income from the rental of the apartment complex is allocated to West Virginia for purposes of the West Virginia Corporation Net Income Tax. Likewise, the net rental income received by Corporation A as a lessor of computers in this State is allocated to this State.

7.2.c. Corporation Z was formed in State X and has its commercial domicile in the State of West Virginia. Corporation Z leases tangible personal property to customers in State K, which has no corporation net income tax. The net receipts from leasing tangible personal property in State K are allocated entirely to the State of West Virginia.

7.2.d. Corporation Alpha, organized and headquartered in California, leases coal mining equipment in West Virginia. Alpha began leasing equipment in West Virginia on April 1, and is a calendar year taxpayer. The coal mining equipment was not in this State until April 1, the date the lease commenced. The property is leased in this State for 275 of the 365 days in the year. If Alpha Corporation netted $15,000 for leasing this equipment for the entire year, Alpha would include in West Virginia income the following amount: 275/365 x $15,000 = $11,301.37.

7.2.d.1. If Alpha Corporation has adequate records to show the net rental income from the equipment while the equipment was leased in this State, then it may use such actual net rental income and not "apportion" its allocation of net rental income.

7.3. Business activities partially within and partially without this State.

7.3.a. Where a corporation has income from business activities partially within this State and partially outside of this State, all net income, after deducting those items specifically allocated under W. Va. Code §11-24-7(d), shall be apportioned to this State

by multiplying such net income by a fraction, the numerator of which is the property factor plus the payroll factor plus two times the sales factor, and the denominator of which is four, reduced by the number of factors, if any, having no denominator except if the sales factor has a denominator of zero, the denominator of the apportionment fraction shall be reduced by two.

Example:

The following is an example of how the apportionment formula works in the context of the corporation net income tax:

A hypothetical corporation has facilities and operations in Pennsylvania, West Virginia, New York and California.

The corporation has sales in 47 of the 50 states of the USA.

The apportionment formula is as follows:

$$\frac{\frac{\text{Average value of property in WV}}{\text{Average value of property in USA}} + \frac{\text{Payroll in WV}}{\text{Payroll in USA}} + \left(2x \left(\frac{\text{Sales in WV}}{\text{Sales in USA}} \right) \right)}{4}$$

Federal Taxable Income -- The corporation has **$10,000,000 federal taxable income from all operations in the USA after West Virginia modifications and adjustments.** These modifications and adjustments are, for certain items that are required to be added to, or subtracted from, federal taxable income before apportionment.

Average value of property in the USA -- Total average value of property owned and leased by the corporation during the tax year in the USA (including property in Pennsylvania, West Virginia, New York and California) is **$517,050,000**.

Average value of property in the West Virginia -- Total average value of property owned and leased by the corporation during the tax year in West Virginia is **$15,000,000**.

Payroll in the USA -- Total annual payroll paid to all employees of the corporation in the USA (including payroll paid in Pennsylvania, West Virginia, New York and California) during the tax year is **$65,628,000**.

Payroll in West Virginia -- Total annual payroll paid to all employees of the corporation in West Virginia is **$2,499,000**.

Sales in the USA --Total sales of the corporation in the entire USA (all of the 47 states in which the corporation has sales) are **$435,009,000**.

The corporation sells almost all of its production outside of West Virginia.

Sales in West Virginia --Total sales of the corporation in West Virginia are **$4,000**.

The apportionment formula, using the values set forth above, would be as follows:

$$\frac{\dfrac{\text{Avg. property in WV } \$15{,}000{,}000.}{\text{Avg. property in USA } \$517{,}050{,}000} + \dfrac{\text{WV Payroll } \$2{,}499{,}000}{\text{USA Payroll } \$65{,}628{,}000} + \left(2x \left(\dfrac{\text{Sales in WV } \$4{,}000}{\text{Sales in USA } \$435{,}009{,}000} \right) \right)}{4}$$

The math works out as follows:

$$\frac{\text{Property factor } 0.029011 + \text{Payroll factor } 0.038078 + \left(2x \left(\text{Sales factor } 0.000009 \right) \right)}{4}$$

OR

$$\frac{\text{Property factor } 0.029011 + \text{Payroll factor } 0.038078 + \text{Double weighted sales factor } 0.000018}{4}$$

OR

$$\frac{0.067107}{4}$$

OR

0.016777 -- This is the apportionment factor.

Assuming that corporation has no allocable WV income, out of all of the operations in the USA, slightly over one percent (*i.e.*, 0.016777) of the operations of the corporation are attributable to West Virginia operations and activity.

Net federal taxable income from all operations in the USA, after WV modifications and adjustments is $10,000,000.

Applying the apportionment formula, West Virginia taxable income is:

Federal Taxable Income (After Adjustments)		Apportionment Factor		WV Taxable Income
$10,000,000	**x**	**0.016777**	**=**	**$167,770.00**

The final computation of the tax is as follows. The hypothetical corporation has federal taxable income after modifications and adjustments allocated and apportioned to West Virginia in the amount of **$167,770.00**. The tax rate for the given year is 8.75%.

Tax is .0875 x $167,770.00 = $14,679.88 (rounded)

Tax is $14,679.88.

7.3.b. Example. -- Pro Inc. is a service corporation doing business in several states, including West Virginia. Pro Inc. owns no property anywhere. In this case, the allocation formula for Pro Inc. will be:

$$\frac{\frac{\text{WV Payroll}}{\text{Total Payroll}} + 2\,\frac{\text{(WV Sales)}}{\text{(Total Sales)}} + \frac{\text{0 WV Property}}{\text{0 Total Property}}}{3}$$

If, for some unusual reason, a corporation has no sales anywhere, since the sales factor is double weighted, the overall denominator would be reduced by 2.

7.4. "Business activities" include all activities engaged in by the corporation, and includes those activities giving rise to both business income and nonbusiness income.

7.4.a. All income of a corporation, including both business income and nonbusiness income, is apportioned, except nonbusiness income specifically identified in W. Va. Code §11-24-7(d), which is allocated.

7.4.a.1. All other nonbusiness income and all business income shall be apportioned.

7.4.b. Where a corporation has business activities that are in West Virginia and other states, its other net nonbusiness income that was not allocated under W. Va. Code §11-24-7(d) and all of its net business income will be apportioned.

7.5. Property factor.

7.5.a. Property factor. -- The property factor is a fraction, the numerator of which is the average value of the taxpayer's real and tangible personal property owned or rented and used by it in this State during the taxable year and the denominator of which

is the average value of all the taxpayer's real and tangible personal property owned or rented and used by the taxpayer during the taxable year, which is reported on Schedule L of Federal Form 1120, plus the average value of all real and tangible personal property leased and used by the taxpayer during the taxable year.

7.5.a.1. The common law definition of real and personal property will be used, *i.e.*, real property is land and all things firmly and permanently attached thereto, and personal property is all other property.

7.5.a.2. Only real and tangible personal property is counted in the property factor. The common law definition of tangible personal property is used. Examples of tangible personal property include, but are not limited to, books, equipment, supplies, inventories and virtually any other form of personalty that can be held or touched. Tangible personal property does not include money, chooses in action, or any other intangibles.

7.5.a.3. The average value of real and tangible personal property means the beginning and ending year balances of the relevant accounts reported on Schedule L of Federal Form 1120, or its successor. However, the Tax Commissioner may require use of a monthly average of such accounts or such other determination of the average value of such property as may be appropriate for an accurate determination of the factor.

7.5.b. Value of property.

7.5.b.1. Property owned by the taxpayer shall be valued at its original cost, adjusted by subsequent capital additions or improvements thereto and by partial or total disposition thereof by reason of sale, exchange, abandonment, loss or destruction or other alienation of, or loss of, the property. Where records of original cost are unavailable or cannot be obtained without unreasonable expense, property shall be valued at current market value. Property rented by the taxpayer from others shall be valued at eight times the net annual rental rate. The term "net annual rental rate" is the annual rental paid, directly or indirectly, by the taxpayer, or for its benefit in money or other consideration for the use of the property.

7.5.b.1.A. Net annual rental rate includes any amount payable for the use of real or tangible personal property, or any part thereof, whether designated as a fixed sum of money or as a percentage of sales, profits or otherwise.

7.5.b.1.B. Any amount payable as additional rent or in lieu of rents, such as interest, taxes, insurance, repairs or any other items which are required to be paid by the terms of the lease or other arrangement, not including amounts paid as service charges, such as utilities, janitor services and the like are also included in the term "net annual rental rate." If a payment includes rent and other charges which are not separately set forth, the amount of rent shall be determined by consideration of the relative values of the rent and the other items.

7.5.b.1.C. Real or personal property owned by one corporation which is used in this State by another corporation to which the property is rented is to be included in the property factor by both corporations unless the rental income is nonbusiness income to the receiving corporation.

7.5.b.1.C.1. Example. -- X Corporation owns certain real property located in West Virginia, which is leased by Y Corporation for the entire taxable year of both corporations. Rental income received by X Corporation is allocated to the State of West Virginia and the value of the property is not included in the apportionment factor for X Corporation's apportionable income in either the numerator of the property factor (value of taxpayer's West Virginia real and tangible personal property) and in the denominator of the property factor (value of taxpayer's real and tangible personal property owned or rented by the taxpayer for the taxable year). Eight times the annual rental rate of the property will be included in both the numerator and the denominator of the property factor for Y Corporation.

7.5.c. Movable property.

7.5.c.1. The value of movable tangible personal property used both within and outside of this State shall be included in the numerator to the extent of its utilization in this State. The extent of utilization in this State is determined by multiplying the original cost of such property by a fraction, the numerator of which is the number of days of physical location of the property in this State during the taxable period, and the denominator of which is the number of days of physical location of the property everywhere during the taxable period. The number of days of physical location of the property may be determined on a statistical basis or by such other reasonable method acceptable to the Tax Commissioner.

7.5.d. Leasehold improvements.

7.5.d.1. For purposes of the property factor, leasehold improvements are treated as property owned by the taxpayer regardless of whether the taxpayer is entitled to remove the improvements or whether the improvements revert to the lessor upon expiration of the lease. Leasehold improvements are included in the property factor at their original cost.

7.5.d.1.A. Example. -- Alpha Corporation leases a building to Beta Corporation. The building is located in West Virginia. Beta Corporation makes certain leasehold improvements to the property totaling $100,000 some of which the lease permits Beta Corporation to remove. The entire value of the leasehold improvements is included in Beta Corporation's property factor. The value of the leasehold improvements is also included in Alpha Corporations property factor.

7.5.e. Average value of property.

7.5.e.1. The average value of property is determined by averaging the values of the property at the beginning and the ending of the taxable year.

7.5.e.1.A. If there are substantial fluctuations in the values of property during the taxable year, or where property is acquired or disposed of after the beginning of the taxable year, or where the rental or lease contract ceases before the end of a taxable year, the Tax Commissioner may require the averaging of monthly values of the property during the taxable year or the pertinent part thereof.

7.5.e.1.A.1. If a unitary member does not have nexus with the state of West Virginia, or if the unitary member is not taxable by West Virginia under the protections of Public Law 86-272 (15 U.S.C.A. §381), then that unitary member's income shall be include in the combined report of the combined group. However, that unitary member's factor attributes shall not be included in the numerator of the property factor, but shall be included in the denominator of the property factor.

7.6. Payroll factor.

7.6.a. The payroll factor is a fraction, the numerator of which is the total compensation paid in this State during the taxable year by the taxpayer for compensation, and the denominator of which is the total compensation paid by the taxpayer during the taxable year, as shown on the taxpayer's federal income tax return filed with the Internal Revenue Service, as reflected in the schedule of wages and salaries and that portion of cost of goods sold which reflects compensation, or as shown on a pro forma return.

7.6.b. Compensation.

7.6.b.1. The term "compensation" means wages, salaries, commissions and any other form of remuneration paid to employees for personal services. Payments made to an independent contractor or to any other person not properly classified as an employee shall be excluded. Only those amounts paid directly to employees are included in the payroll factor. Amounts considered as paid directly to employees include the value of board, rent, housing, lodging and other benefits or services furnished to employees by the taxpayer in return for personal services, provided such amounts constitute income to the recipient for federal income tax purposes. Compensation for each employee shall be the amount of wages and salary shown on the Federal Form W-2 for the employee, in accordance with federal income tax law.

7.6.b.2 Employee.

7.6.b.2.A. For purposes of determining the payroll factor, an employee is any officer of a corporation or any individual who, under the usual common-law rule applicable in determining the employer-employee relationship, has the status of an employee.

7.6.b.2.B. An employee is a person in the service of another under any contract of hire, express or implied, oral or written, where the employer has the power or right to control and direct the employee in the material details of how the work is to be performed.

7.6.c. When compensation is paid in this State.

7.6.c.1. Compensation is paid or accrued in this State if an employee's services are performed entirely within this State or if an employee's services are performed both within this State and outside of this State, but the services performed outside of this State are incidental to that employee's services within this State. The converse is not true. In all circumstances, services performed in this State are to be included in the payroll factor as services performed in this State. "Incidental", as used herein, means any service which is temporary or transitory in nature, or which is rendered in connection with an isolated transaction. Compensation is also paid or accrued in this State if some of the employee's service is performed in this State and the employee's base of operation, or if there is no base of operation, the place from which the service is directed or controlled is in this State, or the base of operations or the place from which the service is directed or controlled is not in any state in which some part of the service is performed, but the employees residence is within this State.

7.6.c.2. As used herein, the term "base of operations" is the place of more or less permanent nature from which the employee starts his work and to which he or she customarily returns in order to receive instructions from the taxpayer or communications from his customers or with other persons or to replenish stock or other materials, repair equipment, or perform any other functions necessary to the exercise of his trade or profession at some other point or points. The term "place from which the service is directed or controlled" refers to the place from which the power to direct or control is exercised by the taxpayer.

7.6.c.3. Example. -- P Corporation has salesmen in several states. West Virginia customers are serviced by a salesman living in Ohio. The salesmen are directed from a regional office located in Pennsylvania. Compensation attributable to the time spent in West Virginia on employer business would be included in the taxpayer's West Virginia payroll factor.

7.6.c.4. If a unitary member does not have nexus with the state of West Virginia, or if the unitary member is not taxable by West Virginia under the protections of Public Law 86-272 (15 U.S.C.A. §381), then that unitary member's income shall be include in the combined report of the combined group. However, that unitary member's factor attributes shall not be included in the numerator of the payroll factor, but shall be included in the denominator of the payroll factor.

7.7. Sales factor.

7.7.a. The sales factor is a fraction, the numerator of which is the gross receipts of the taxpayer derived from transactions and activity in the regular course of its trade or business in this State during the taxable year, less returns and allowances attributable to the gross receipts from the West Virginia activity. The denominator of the fraction is the total gross receipts derived by the taxpayer from transactions and activity in the regular course of its trade or business during the taxable year, and reflected in its gross income reported and as appearing on the taxpayer's Federal Form 1120, and consisting of those certain pertinent portions of the elements of gross income set forth. If either the numerator or the denominator includes interest or dividends from obligations of the United States government which are exempt from taxation by this State, the amount of such interest and dividends, if any, shall be subtracted from the numerator or denominator in which it is included.

7.7.a.1. The only sales to be included in the sales factor are those which produce business income.

7.7.a.2. Rules for determining sales in certain circumstances.

7.7.a.2.A. In the case of a taxpayer engaged in manufacturing and selling or purchasing and reselling goods or products, "sales" includes all gross receipts from the sales of such goods or products (or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the tax period) held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business. Gross receipts for this purpose means gross sales less returns and allowances, and includes all interest income, service charges, carrying charges, or time-price differential charges incidental to such sales. Federal and state excise taxes (including sales taxes) shall be included as part of such receipts if such taxes are passed on to the buyer or included as part of the selling price of the product.

7.7.a.2.B. In the case of cost fixed fee contracts, such as the operation of a government-owned plant for a fee, "sales" includes the entire reimbursed cost, plus the fee.

7.7.a.2.C. In the case of a taxpayer engaged in providing services, such as the operation of an advertising agency, or the performance of equipment service contracts, or research and development contracts, "sales" includes the gross receipts from the performance of such services including fees, commissions, and similar items.

7.7.a.2.D. In the case of a taxpayer engaged in renting real or tangible property, "sales" includes the gross receipts from the rental, lease, or licensing of the use of the property.

7.7.a.2.E. In the case of a taxpayer engaged in the sale, assignment, or licensing of intangible personal property such as patents and copyrights, "sales" includes the gross receipts the therefrom.

7.7.b. In filing returns with this State, if the taxpayer departs from or modifies the basis for excluding or including gross receipts in the sales factor used in returns for prior years, the taxpayer shall disclose such information by attaching a statement, setting forth the nature and effect of the change, to the corporation net income tax return for the current year.

7.7.c. Sales factor denominator.

7.7.c.1. The denominator of the sales factor includes the total gross receipts derived by the taxpayer from transactions and activity in the regular course of its trade or business, unless otherwise excluded herein.

7.7.d. Sales factor numerator.

7.7.d.1. The numerator of the sales factor shall include gross receipts attributable to this State and derived by the taxpayer from transactions and activity in the regular course of its trade or business. All interest income, service charges, carrying charges, or time-price differential changes incidental to such gross receipts shall be included regardless of the place where the accounting records are maintained or the location of the contract or other evidence of indebtedness.

7.7.d.2. *Joyce* or *Finnegan*.

The ***Joyce*** case and the ***Finnegan*** case were tax matters brought before the California State Board of Equalization –

Appeal of Joyce, Inc., 66 SBE 069, 1966 WL 1411 (Cal. St. Bd. Eq.) (Nov. 23, 1966).

Appeal of Finnigan Corp., 88- SBE-022-A, 1990 WL 15164 (Cal. St. Bd. Eq.) (Jan. 24, 1990).

The issue for which these cases have become known relates to the determination of the sales that are included in the numerator of the sales factor for purposes of the apportionment formula.

In synopsis, the basic distinction is as follows:

> ***Joyce*** – If a unitary group member has nexus with the state, then "in state" gross receipts of that member are included in the sales factor numerator, but **not** if the member does **not** have nexus with the state, determined on a "stand alone" basis.
>
> ***Finnigan*** – If one or more unitary group members has nexus with the state, then "in state" gross receipts of all unitary group members are included in the sales factor numerator, including "in state" gross receipts of a unitary

group member that, itself, does not have nexus with the state, determined on a "stand alone" basis.

West Virginia is a "*Joyce* State."

If the unitary member does not have nexus with West Virginia or If the unitary member is not taxable under the protections of PL 86-272, then that unitary member's gross receipts derived from transactions and activity in the regular course of its trade or business in West Virginia are **not** included in the numerator of the sales factor.

7.7.e. Dock sales.

7.7.e.1. Where tangible personal property is sold and the terms of the sale require the purchaser to pick up the property or otherwise receive the property in this State, the sale is to be treated as a sale taking place in this State for purposes of the sales factor.

7.7.e.2. In the case of sales requiring by their terms delivery of tangible personal property by common carrier, contract carrier or by other means of transportation excluding pickup by the customer in this State, whether directly or indirectly, the place at which the property is ultimately received after all transportation has been completed shall be considered as the place at which such property is received by the purchaser.

7.7.e.3. Direct delivery in this State, other than for purposes of transportation, to a person or firm designated by a purchaser constitutes delivery to the purchaser in this State regardless of where title passes or other conditions of sale.

7.7.e.4. Direct delivery outside this State to a person or firm designated by a purchaser does not constitute delivery to the purchaser in this State, regardless of where title passes or other conditions of sale.

7.7.e.5. Examples.

7.7.e.5.A. Baubles, Inc. is located in Huntington, West Virginia, and makes sales of tangible personal property to an Ohio company. The terms of the sale require the Ohio company to pick up the merchandise from the loading dock at Baubles. The sale is to be treated by Baubles as a sale taking place in this State.

7.7.e.5.B. Alpha Corporation, which manufactures a highly sophisticated device used in mining, purchases certain tangible personal property from a company located in Virginia. Alpha Corporation, located in Bergoo, West Virginia is required by the terms of the sales contract to pick up the merchandise at the Virginia company's loading dock in Virginia. The sale is to be treated as not occurring in West Virginia by the Virginia company absent other nexus with West Virginia.

7.7.e.5.C. RPS, Inc., is located in Morgantown, West Virginia and makes sales of tangible personal property. Some of the sales contracts require RPS to ship the goods to companies located outside of this State via common carrier. The sales of the tangible personal property shipped by the carrier are not included as West Virginia sales.

7.7.f. Special rules.

7.7.f.1. Where substantial amounts of gross receipts arise from an incidental or occasional sale of a fixed asset used in the regular course of the taxpayer's trade or business, such gross receipts shall be excluded from the sales factor. For example, gross receipts from the sale of a factory or plant will be excluded.

7.7.f.2. Insubstantial amounts of gross receipts arising from incidental or occasional transactions or activities may be excluded from the sales factor unless such exclusion would materially affect the amount of income apportioned to this State. For example, the taxpayer ordinarily may include or exclude from the sales factor gross receipts from such transactions as the sale of office furniture, business automobiles, etc.

7.7.f.3. Where the income producing activity of a taxpayer other than a banking or financial institution in respect to business income from intangible personal property can be readily identified, such income is included in the denominator of the sales factor and, if the income producing activity occurs in this State, the numerator of the sales factor as well. For example, usually the income producing activity can be readily identified in respect to interest income received on deferred payments on sales of tangible property and income from the sale, licensing or other use of intangible personal property.

7.7.f.4. Where the business income from intangible property cannot readily be attributed to any particular income producing activity of a taxpayer other than a banking or financial institution, such income cannot be assigned to the numerator of the sales factor for any state and shall be excluded from the denominator of the sales factor. For example, where business income in the form of dividends received on stock, royalties received on patents or copyrights, or interest received on bonds, debentures or government securities results from the mere holding of the intangible personal property by the taxpayer, such dividends and interest shall be excluded from the denominator of the sales factor.

7.7.g. Allocation of sales of tangible personal property.

7.7.g.1. Sales of tangible personal property are in this State if the property is received in this State by the purchaser, other than the United States government, regardless of the f.o.b. point or other conditions of the sale. In the case of delivery by common carrier or other means of transportation, the place at which such property is ultimately received after all transportation has been completed shall be considered as

the place at which such property is received by the purchaser, regardless of where title passes or other conditions of sale. Direct delivery in this State, other than for purposes of transportation, to a person or firm designated by the purchaser, constitutes delivery to the purchaser in this State, and direct delivery outside this State to a person or firm designated by the purchaser does not constitute delivery to the purchaser in this State, regardless of where title passes or other conditions of sale. The sales of tangible personal property are also in this State if the property is shipped from an office, store, warehouse, factory or other place of storage in this State and the purchaser is the United States government.

7.7.g.2. Throwout rule -- All other sales of tangible personal property delivered or shipped to a purchaser within a state in which the taxpayer is not taxed are excluded from the denominator of the sales factor.

7.7.g.2.A. "Not taxed in another state" means in that state the taxpayer is not subject to a net income tax, a franchise tax measured by net income, a franchise tax for the privilege of doing business, or a corporation stock tax or that a state has no jurisdiction to subject the taxpayer to a net income tax.

7.7.h. Allocation of other sales.

7.7.h.1. Sales, other than sales of tangible personal property are in this State if the income-producing activity is performed in this State or the income-producing activity is performed both in and outside this State and a greater proportion of the income-producing activity is performed in this State than in any other state, based on costs of performance, or the sale constitutes business income to the taxpayer, or the taxpayer is a financial organization not having its commercial domicile in this State, and in either case the sale is a receipt described as attributable to this State in W. Va. Code §11-24-7b.

7.7.i. If a unitary member does not have nexus with the state of West Virginia, or if the unitary member is not taxable by West Virginia under the protections of Public Law 86-272 (15 U.S.C.A. §381), then that unitary member's income shall be include in the combined report of the combined group. However, that unitary member's factor attributes shall not be included in the numerator of the sales factor, but shall be included in the denominator of the payroll factor. However, if the member has sales subject to the throwout rule, then its sales factor attributes for those sales not taxed in another state are excluded from both the numerator and the denominator.

7.7.j. The term "income-producing activity" applies to each separate item of income and means the transactions and activity directly engaged in by the taxpayer in the regular course of its trade or business for the ultimate purpose of obtaining gain or profit. Such activity does not include transactions and activities performed on behalf of the taxpayer, such as those conducted on its behalf by an independent contractor. "Income-producing activity" includes, but is not limited to:

7.7.j.1 Rendering of personal services by employees with utilization of tangible and intangible property by the taxpayer in performing a service;

7.7.j.1.A. The sale, rental, leasing, licensing or other use of real property;

7.7.j.1.B. The sale, rental, leasing, licensing or other use of tangible personal property; or

7.7.j.1.C. The sale, licensing or other use of intangible personal property. The mere holding of intangible property is not, in itself, an income-producing activity: Provided, That the conduct of the business of a financial organization shall constitute an income-producing activity.

7.7.k. The term "cost of performance" means direct costs determined in a manner consistent with generally accepted accounting principles and in accordance with accepted conditions or practices in the trade or business of the taxpayer.

7.7.l. Application and special rules.

7.7.l.1. Gross receipts from the sale, lease, rental or licensing of real property are located in this State if the real property is located in this State.

7.7.l.2. Gross receipts from the sale, rental, lease, or licensing of tangible personal property are in this State if the property is located within this State. The rental, lease, licensing or other use of tangible personal property in this State is a separate income producing activity from the rental, lease, licensing or other use of the same property while located in another state; consequently, if property is within and without this State during the rental, lease or licensing period, gross receipts attributable to this State shall be measured by the ratio which the days the property was physically present or was used in this State bears to the total days of the physical location or use of the property everywhere during such period.

7.7.l.3. Example. -- Taxpayer is the owner of ten railroad cars. During the current tax year, the total of the days each railroad car was present in this State was 60 days. The receipts attributable to the use of each of the railroad cars in this State are a separate item of income and shall be determined as follows:

$$\left(\frac{\text{10 cars X 60 days each}}{\text{365 days in 1 year X 10 cars}} \right) \text{ X Total receipts = Receipts attributable to this State.}$$

7.7.l.4. Gross receipts for the performance of personal services are attributable to this State to the extent such services are performed in this State. If services relating to a single item of income are performed partly within and partly outside of this State, the gross receipts for the performance of such services shall be attributable to this State only if a greater proportion of the services was performed in the state, based upon costs of performance. Usually, where services are performed partly

within and partly outside of this State, the services performed in each state will constitute a separate income producing activity; in such case the gross receipts for the performance of services attributable to this State shall be measured by the ratio which the time spent in performing such services in this State bears to the total time spent in performing such services everywhere. Time spent in performing services includes the amount of time expended in the performance of a contract or other obligation which gives rise to such gross receipts. Personal service not directly connected with the performance of the contract or other obligation, as for example time spent in negotiating the contract, is excluded from the computations.

7.7.I.5. Example. -- Taxpayer, a road show, gave theatrical performances at various locations in State X and in this State during the tax period. All gross receipts from performances given in this State are attributable to this State as each performance is a separate income producing activity.

7.7.I.6. Example. -- Taxpayer, a public opinion survey corporation, conducted a poll by its employees in State F and in this State for the sum of $10,000. The project required 800 man hours to obtain the basic data and to prepare the survey report. Three hundred of the 800 man hours were expended in this State. The receipts attributable to this State are: 300/800 X $10,000 = $3,750.

7.7.I.7. Example. -- Boil Laboratories, Inc. performs certain medical tests. Boil Laboratories is located in Virginia, where all analysis is performed. Boil Labs also has a location in this State where tissue specimen are collected, as well as a truck and routeman in this State who collects samples from various doctor's offices and hospitals. Boil Labs has a similar set-up in Virginia. It costs Boil Labs $18 to analyze each specimen. All but $5 of the $18 of these costs are incurred in the State of Virginia. Each sample or specimen is a separate income-producing activity and is not the sale of tangible personal property. Since the income-producing activity is performed both in and outside of this State, and a greater proportion of the income producing activity is not performed in this State, then none of the charges for the analysis of samples or specimens drawn in this State will be included as sales in this State for purposes of the sales factor.

§110-24-7a — Special Apportionment Rules.

7a.1. For purposes of this rule, any member of a unitary group that is required or permitted to use an apportionment formula or apportionment method other than an apportionment formula or apportionment method prescribed by West Virginia Code §11-24-7 is a "special apportionment member."

7a.1.a. A special apportionment member shall be included in a combined reporting group with other unitary group member corporations, and if the special apportionment member uses an apportionment formula or apportionment method other than an apportionment formula or apportionment method prescribed by West Virginia

Code §11-24-7, the special apportionment member shall apply the special apportionment formula or method against the unitary group income.

7a.1.b. In lieu of the method described in section 7a.1.a and 7a.1.c of this rule, a special apportionment member may seek authorization of the Tax Commissioner to report and file its tax based on designation of a combined reporting group limited to unitary group members who are required or permitted to use a special apportionment formula or method, and who do in fact use the same special apportionment formula or method as the special apportionment member. Issuance of such an authorization is within the sole discretion of the Tax Commissioner. However, if such an authorization is issued, the income and the factors of a special apportionment member shall not be included in the combined reporting group comprised of the remainder of the unitary group that are not special apportionment members, that use an apportionment formula other than the apportionment formula of the particular special apportionment member.

7a.1.c. In lieu of the method described in sections 7a.1.a and 7a.1.b of this rule, a special apportionment member may seek authorization of the Tax Commissioner to report and file its tax on a separate return basis, pursuant to such accounting and allocation and apportionment requirements as the Tax Commissioner may on a case by case basis prescribe.

7a.1.d. Motor carriers -- Motor carries required to use the apportionment formula or apportionment method specified in West Virginia Code §11-24-7a(b) are special apportionment members.

7a.1.e. Financial organizations – Financial organizations required to use the apportionment formula or apportionment method specified in West Virginia Code § 11-24-7b are special apportionment members.

7a.1.f. The Tax Commissioner has the authority and discretion to designate a Taxpayer that is using allocation methods and an apportionment formula or apportionment methods required by the Tax Commissioner pursuant to the provisions of West Virginia Code §11-24-7(h) to be a special apportionment member. However, unless specifically designated by the Tax Commissioner to be a special apportionment member, a corporation using an allocation method and an apportionment formula or apportionment methods required by the Tax Commissioner pursuant to the provisions of West Virginia Code §11-24-7(h) is deemed to be a Taxpayer which uses an allocation method and an apportionment formula or apportionment methods prescribed by West Virginia Code §11-24-7, and shall not be designated or deemed to be a special apportionment member.

§110-24-8. Accounting Periods And Methods Of Accounting.

8.1. Period of computation of West Virginia taxable income.

8.1.a. For purposes of the tax imposed by this article, a taxpayer's taxable year shall be the same as the taxpayer's taxable year for federal income tax purposes.

8.2. Change of taxable year.

8.2.a. If a taxpayer's year is changed for federal income tax purposes, the taxpayer's taxable year for purposes of this article shall be similarly changed.

8.3. Methods of accounting.

8.3.a. Same as federal.

8.3.a.1. A taxpayer's method of accounting under this article shall be the same as the taxpayer's method of accounting for federal income tax purposes. In the absence of any method of accounting for federal income tax purposes, West Virginia taxable income for purposes of this article shall be computed under such method that in the opinion of the tax commissioner clearly reflects such income.

8.3.b. Change of accounting methods.

8.3.b.1. If a taxpayer's method of accounting is changed for federal income tax purposes, his method of accounting for purposes of this article shall be changed so that it conforms to the method used for federal income tax purposes.

8.4. Adjustments.

8.4.a. In computing a taxpayer's West Virginia taxable income for any taxable year under a method of accounting different from the method under which the taxpayer's West Virginia taxable income for the previous year was computed, there shall be taken into account those adjustments which are determined, to be necessary solely by reason of the change in order to prevent amounts from being duplicated or omitted.

8.5. Limitation on additional tax.

8.5.a. Change other than to installment method.

8.5.a.1. If a taxpayer's method of accounting is changed, other than from an accrual to an installment method, any additional tax which results from adjustments determined to be necessary solely by reason of the change shall not be greater than if such adjustments were ratably allocated and included for the taxable year of the change and the preceding taxable years, not in excess of two, during which the taxpayer used the method of accounting from which the change is made.

8.5.a.2. Procedure for determining tax liability under the provisions of W. Va. Code §11-24-8(e).

8.5.a.2.A. Compute the tax for the current year using the regular method, including determination of effective tax rate.

8.5.a.2.B. Multiply the dollar amount of the income adjustment included in the West Virginia taxable income by the current year effective tax rate.

8.5.a.2.C. Prorate the adjustments over the current tax year and over no more than two of the preceding tax years.

8.5.a.2.D. Multiply the dollar amount of the adjustments allocated to each of the years, to the extent the adjustments were included in West Virginia taxable income, by the effective tax rate applicable to each of the years.

8.6. Change from accrual to installment method.

8.6.a. If a taxpayer's method of accounting is changed from an accrual to an installment method, any additional tax for the year of such change of method and for any subsequent year which is attributable to the receipts of installment payments properly accrued in a prior year shall be reduced by the portion of tax for any prior taxable year attributable to the accrual of such installment payments.

8.7 Coordination of reporting year among combined reporting unitary group members having diverse tax years.

8.7.a. Principal member. For purposes of this rule, "Principal member" is the member of the combined reporting group whose accounting period is used as a reference period for all members of the combined reporting group to aggregate and apportion combined report business income of the group. A principal member need not be a taxpayer member.

8.7.a.1. Corporations Described. Once a principal member has been determined under this subsection, that member shall remain the principal member for all succeeding periods that it is a member of the combined reporting group. However, the Tax Commissioner may authorize designation of a different principal member. Except as otherwise provided, the "principal member" is the corporation first described below:

8.7.a.1.A. The parent corporation to all members of the combined reporting group. For purposes of this determination, a corporation which owns on average during the taxable year more than fifty percent of the stock of all classes of another corporation is defined to be the "parent corporation" of the corporation which is so owned.

8.7.a.1.B. If the group does not have a parent corporation which is a member of the combined reporting group, as so defined, the "principal member" is a corporation which is a lower tier parent to all members of the combined report. A "lower tier parent" is the first corporation, down the chain of corporations, which is a member of the combined reporting group and which would have constituted a "parent corporation"

to all members of the combined group if all corporations which own or constructively own that corporation were disregarded.

8.7.a.1.C. If the group does not have a "lower tier parent" corporation which is a member of the combined reporting group, the "principal member" is the taxpayer member of the combined reporting group expected to have, on a recurring basis, the largest amount, by value, of real and tangible personal property in West Virginia. The value of real and tangible personal property shall be determined pursuant to the property factor provisions of West Virginia Code §§11-24-1, *et seq.* and this rule.

8.7.a.D. Election to Designate Principal Member. Notwithstanding the preceding provisions of this subdivision, in the first income year in which a combined report is required, the taxpayer members of the combined reporting group may elect to treat any other member of the combined reporting group as the "principal member," so long as it is consistently treated as such for the year of the election and thereafter. Thereafter, the taxpayer members may change their principal member only with consent of the Tax Commissioner .

8.7.b. Inconsistent Principal Member. In the event that members of a combined reporting group have filed with inconsistent principal members (including cases where two or more groups of corporations erroneously filed as distinct combined reporting groups) the determination of the appropriate principal member shall be made in accordance with the provisions of subdivision 8.7.a., unless, in the discretion of the Tax Commissioner, selection of another principal member is authorized or mandated by the Tax Commissioner.

8.8. Fiscalization to Principal Member's Year. "Fiscalization" is the process under which a member of a combined reporting group aligns the income and apportionment data from its accounting period to the accounting period of the principal member. If the accounting period of the principal member and one or more of the other members of the combined reporting group do not begin and end on the same dates, adjustments must be made to fiscalize the other members' combined report business income and apportionment data in order to assign an appropriate amount of those values to the accounting period of the principal member.

8.8.a. Combined report business income of a taxpayer member, determined under West Virginia Code §§11-24-1, *et seq.* and this rule, is proportionately assigned to the applicable portion of that member's income year, based on the number of months falling within the common accounting period of the principal member. The resulting income from such portions is then aggregated (or netted) together for the member's income year to determine that member's business income attributable to the combined reporting group.

8.8.a.1. If the accounting period of a principal member and one of the other members of a combined reporting group do not begin and end on the same dates, adjustments must be made to the other members' combined report business income and apportionment data to assign an appropriate amount of those values to the accounting period of the principal member in order for total group combined report business income to be apportioned. Each member of the group should generally use

combined report business income and apportionment data from its books of account earned during the accounting period of the principal member. This will require an interim closing of the books for members whose normal accounting period differs from the principal member. However, a pro rata method of converting income to the principal member's accounting period will be accepted as long as the method does not produce a material misstatement of income apportioned to this state. Unless otherwise permitted or required by the Tax Commissioner, the treatment of both the income and the apportionment data of any particular member must use the same method. If one method was used to account for a member's income and apportionment data in the combined report for the principal member's preceding accounting period and another method will be used in the combined report for the principal member's next accounting period, adjustments to income and apportionment data of the member shall be made to prevent income and apportionment data from being omitted or duplicated.

8.8.a.2. Interim closing method.

8.8.a.2.A. The combined report business income and expense of a member of the combined reporting group is determined by reference to the sum (or net) of such income from the actual books and records of that member for each of the partial accounting periods of the member shared with the principal member. For example, if the principal member has an accounting period ending on December 31, 2010, and another member has an accounting period ended March 31, 2011, the other member determines its income from its actual books and records for the partial accounting periods beginning January 1, 2010, and ending March 31, 2010, and from April 1, 2010 and ending December 31, 2010.

8.8.a.2.B. The apportionment data (property, payroll, and sales in West Virginia, and everywhere) shall also be determined by reference to the member's books and records, West Virginia Code §§11-24-1 *et seq.* and this rule, for the appropriate partial accounting year. Under the interim method, the property factor computation should reflect the actual, not prorated, property owned and rented during the principal member's accounting period.

8.8.a.2.B.1. Example. If the principal member has an accounting period ending on December 31, 2010, and another member has an accounting period ended March 31, 2011, the other member will determine its total property and its West Virginia property from its actual books and records on the basis of the period from January 1, 2010 to December 31, 2010.

8.8.a.2.C. Interim combined report business income and apportionment data from the respective partial periods is then combined with the income and apportionment data of the accounting period of the principal member, along with business income and apportionment data of other members of the combined reporting group for the same period, using, if applicable, the methods prescribed in West Virginia Code §§11-24-1, *et seq.* and this rule.

8.8.b. Pro rata method.

8.8.b.1 At the election of the members of a combined reporting group and with the express authorization of the Tax Commissioner, fiscalization of combined report

business income of one or more members of the group to the accounting period of the principal member may be determined by use of a pro rata method. However, the election is not available if that method produces a material misstatement of income. Under the pro rata method, the apportionment data and combined report business income from the member's adjusted separate books of account (*i.e.*, adjusted to reflect the determination of income under West Virginia Code §§11-24-1, *et seq.* and this rule) is assigned to the respective portion of the principal member's accounting period based on the ratio of months in common with that member. For example, if the principal member's accounting period ends on December 31, 2010, a member whose income year ends on March 31 will reflect 3/12ths of its adjusted separate combined report business income and its property, payroll and sales for its income year ended March 31, 2010 in the December 31, 2010 accounting period of the principal member. That member will then reflect 9/12ths of its adjusted separate combined report business income and its property, payroll and sales for its income year ended March 31, 2011 in the December 31, 2010 accounting period of the principal member.

8.8.b.2. The combined report business income and apportionment data from the respective partial periods is then combined with the income and apportionment data of the accounting period of the principal member, along with business income and apportionment data of other members of the combined reporting group for the same period, using, if applicable, the methods prescribed in West Virginia Code §§11-24-1, *et seq.* and this rule. The combined business income is then apportioned to each of the taxpayer members of the group.

8.8.b.3. In the event that the pro rata method requires the determination of income and apportionment data of a corporation whose accounting period has not yet closed, and the information cannot be obtained in time for the other members to file an accurate return, the income and apportionment data for that period shall be estimated based on available information. If the use of actual income and apportionment data results in a material change in the tax liabilities of the taxpayer members of the group, the taxpayer members must file an amended return to reflect the change.

8.8.c. After the combined reporting group's income is apportioned to West Virginia, West Virginia combined report business income of a taxpayer member is then proportionately assigned to the applicable portion of that member's income year, based on the number of months falling within the common accounting period of the principal member. For example, if the principal member's accounting period year ends on December 31, 2010, a taxpayer member whose income year ends on March 31 will reflect 3/12ths of its share of apportioned income from the principal member's December 31, 2010 accounting period in its income year ended March 31, 2010, and 9/12ths of its share of such income in its income year ended March 31, 2011. The resulting income from such segments is then aggregated (or netted) together for the member's income year to determine that member's West Virginia business income attributable to the combined reporting group.

8.9. Partial Combined Reporting Periods.

8.9.a. If a member of a combined reporting group is not a member of the combined reporting group during the entire accounting period of the principal member (*e.g.*, because of lack of a unitary relationship, or termination of a unitary relationship), modified combined reporting procedures apply as provided herein. Business income and apportionment data of a member is included in the combined report of the remaining members only for the period (or partial period) for which all of the members are in the combined reporting group. Thus, if a member of a combined reporting group enters or leaves the group at a time during the middle of the accounting period of the principal member, a separate combined report determination is required to be made only for the partial period of combination. The partial period combination is made using the same combined reporting procedures for a 12 month period, except that income, payroll, property and sales data will reflect only the amounts applicable to the partial period. With express permission of the Tax Commissioner, a pro rata method may be used to determine each member's income and apportionment data for the partial period, unless it results in a material misstatement of income. If so, the interim closing method must be used. Establishment or termination of a combined reporting relationship will not, by itself, cause a short period filing requirement.

8.9.a.1. Example: Corporations A, B, and C are members of a combined reporting group. Corporation A is the principal member, and has a calendar year accounting period. On May 1, Corporation A acquires Corporation D. Because of substantial preexisting business relationships, Corporation D immediately becomes a member of the combined reporting group on that date. Only Corporations B and C are West Virginia taxpayers. As provided in this subsection, two combined report calculations are required. The first combined report calculation includes the combined report business income and apportionment data of Corporations A, B, and C from January 1 through April 30. The combined report business income for that period is then apportioned to West Virginia taxpayer members B and C, for the period January 1 through April 30. The second combined report calculation includes the combined report business income and apportionment data of Corporations A, B, C, and D from May 1 through December 31. The combined report business income for that period is then apportioned to West Virginia taxpayer members B and C for the period May 1 through December 31.

8.9.b. If a taxpayer member's income year does not begin and end on the same dates as the partial period combination (*e.g.*, a short-period return is not required), the taxpayer member's West Virginia income earned during that portion of the income year before and after the partial period combination is aggregated (or netted) with the taxpayer member's West Virginia combined report income from the partial period combination. On occasion, the West Virginia income so described will include income from two or more partial period combinations.

8.9.b.1. Example: Corporation P owns all of the stock of Corporation S for the 12 month period ended December 31, 2011. Corporations P and S are unitary and are obligated to file a combined report for the entire period. Corporation P acquires 51% of the stock possessing voting power of Corporation A on March 7, 2011. The acquisition does not compel the filing of a short period return by Corporation A. All of the Corporations have a calendar year accounting period. Corporation A becomes unitary

with Corporations P and S on July 1, 2011 and is obligated to file a combined report with Corporations P and S for the partial period beginning on July 1, 2011. The income and apportionment data of Corporation A for the period prior to July 1, 2011 cannot be included in a combined report with Corporations P and S. Under West Virginia Code §§11-24-1 *et seq.* and this rule, two separate partial period combined report calculations are required. One is for the P-S group for the partial period ended June 30, 2011, and the other is for the P-S-A group for the partial period from July 1, 2011 to December 31, 2011.

Assume that Corporation P's West Virginia combined report income is $ 250,000 for the partial period ended June 30, 2011 and P has a $ 60,000 West Virginia net operating loss for the partial period ended December 31, 2011. Corporation P's West Virginia combined reporting income for its income year ended December 31, 2011 is $ 190,000. Assume that Corporation A has West Virginia income from its unaffiliated and non unitary partial period (or from another combined reporting group, if applicable) of $ 50,000 and A has a West Virginia net operating loss of $ 30,000 for the combined report partial period after it joined the combined reporting group. Corporation A's West Virginia income for its income year ended December 31, 2011 is $ 20,000.

8.9.c. In lieu of partial period combination method described by subdivisions 8.9.a and 8.9.b, the taxpayer members of the commonly controlled group may elect to utilize the method provided in this subdivision. The election must be consistently used by all taxpayer members. The election may not be utilized if the results of that method, compared with the provisions of subdivisions 8.9.a and 8.9.b of this regulation, results in a material misstatement of the taxpayer member's West Virginia income. Under the method described in this subdivision, the partial period combined reporting income of a member, which is not in a combined reporting relationship with the principal member for the entire accounting period of the principal member, is considered to be reflected by the relative weighting of the apportionment data of the partial period member to the apportionment data of the rest of the combined reporting group for the accounting period of the principal member. The method applies as follows:

8.9.c.1. The principal member's income and apportionment data are determined for its entire accounting period (usually a 12 month period). All other members which were members of the combined reporting group during the entire period of the principal member also include their income and apportionment data for that period, using fiscalization methods, if appropriate.

8.9.c.2. Members who were not members of the combined reporting group for the entire accounting period of the principal member include in the combined report only their income for the partial period during which they were a member. Normally this income will be determined by an interim closing of the member's books of account. Similarly, the apportionment data of that member is included only for that same partial period.

8.9.c.3. Property factor data for the partial period member (both West Virginia property and total property) must be adjusted to reflect the fact that the property was not utilized in the combined reporting group for the entire period of the principal member. For example, if the partial period member was in the combined reporting group

for only 7 months of the 12 month accounting period of the principal member, only 7/12's of the member's average West Virginia and total property for the period are reflected in the combined report.

8.9.c.4. Apportionment is then computed using the amounts included in paragraphs 8.9.c.1 through 8.9.c.3 of this regulation, as if the partial period members were members for the entire accounting period of the principal member. The amounts apportioned to the individual taxpayer members then reflects the member's West Virginia combined reporting income for the partial period. That member then aggregates (or nets) West Virginia combined reporting income with its West Virginia income from other activity to compute income subject to taxation for the entire income year.

8.9.c.4.A. Example: Assume the same facts as provided in Example 8.9.a.1.of this subsection, except that the members of the group elect to report under subdivision 8.9.c. of this regulation. Under that election, Corporation A, B, and C determine their income and apportionment data for the entire 12 months of the calendar year. Corporation D determines its income and apportionment data for the period May 1-December 31. However, because Corporation D was not a member of the combined reporting group for the entire calendar year, the property factor values for the combined reporting period must be multiplied by 8/12ths to reflect a weighted average value of that property in the principal member's accounting period. The West Virginia combined report income of Corporations B and C are then determined as if Corporation D's income and apportionment data were entirely earned in the principal member's accounting period.

8.9.c.4.B. Example: Assume the same facts as Example 8.9.c.4.A., except that Corporation D is a calendar year West Virginia taxpayer, and its addition to the combined reporting group did not cause a short period filing requirement. Corporation D's West Virginia combined report income, determined under this subdivision, would be treated as earned for the period May 1 through December 31. That West Virginia income would be aggregated (or netted) with its other West Virginia income for the entire calendar year, as provided in subdivision 8.9.b of this regulation.

§§110-24-9 through 13. Reserved for future use.

§110-24-13a. Combined Reporting.

13a.1. For tax years beginning on and after the January 1, 2009 any taxpayer engaged in a unitary business with one or more other corporations shall file a combined report which includes the income, determined under West Virginia Code §§ 11-24-13c or 13d, and the allocation and apportionment of income provisions of West Virginia Code §§11-24-1, *et seq.*, of all corporations that are members of the unitary business.

13a.1.a The income of an insurance company, shall not be included in a combined report filed under West Virginia Code §§11-24-1, *et seq.* and the allocation or apportionment of income related thereto shall not be included and the apportionment

factors of an insurance company shall not be included in the combined report, unless specifically required to be included by the Tax Commissioner.

13a.1.b Insurance companies, unless otherwise exempt from or excluded from tax under West Virginia Code §§11-24-1, *et seq.* or other provisions of the West Virginia Code, shall file a separate corporate net income tax return.

13a.2. Determination of unitary business The term "unitary business" is defined in West Virginia Code §§11-24-1, *et seq.* as a single economic enterprise that is made up either of separate parts of a single business entity or of a commonly controlled group of business entities that are sufficiently interdependent, integrated and interrelated through their activities so as to provide 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.

13a.2.a For purposes of West Virginia Code §§11-24-1, *et seq.* and West Virginia Code §§11-23-1, *et seq.* a partnership shall be treated as conducted by its partners, whether directly held or indirectly held through a series of partnerships, to the extent of the partner's distributive share of the partnership's income, regardless of the percentage of the partner's ownership interest or the percentage of its distributive or any other share of partnership income. A business conducted directly or indirectly by one corporation through its direct or indirect interest in a partnership is unitary with that portion of a business conducted by one or more other corporations through their direct or indirect interest in a partnership if there is 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 and the corporations are members of the same commonly controlled group.

13a.2.b. Fifty percent ownership rule -- For purposes of this rule, the term commonly controlled group, with reference to any Taxpayer, means and includes all related entities as herein defined, in the aggregate.

13a.2.b.1 The term "related entity" means:

13a.2.b.1.1. An individual, corporation, partnership, affiliate, association or trust or any combination or group thereof controlled by the taxpayer;

13a.2.b.1.2. An individual, corporation, partnership, affiliate, association or trust or any combination or group thereof that is in control of the taxpayer;

13a.2.b.1.3.An individual, corporation, partnership, affiliate, association or trust or any combination or group thereof controlled by an individual, corporation, partnership, affiliate, association or trust or any combination or group thereof that is in control of the taxpayer; or

13a.2.b.1.4. A member of the same controlled group as the taxpayer, as the term "controlled group" is defined in Section 267 of the Internal Revenue Code of 1986, as amended.

13a.2.b.2. For purposes of this section, "control," with respect to a corporation, means ownership, directly or indirectly, of stock possessing fifty percent or more of the total combined voting power of all classes of the stock of such corporation entitled to vote. "Control," with respect to a trust, means ownership, directly or indirectly, of fifty percent or more of the beneficial interest in the principal or income of such trust. The ownership of stock in a corporation, of a capital or profits interest in a partnership or association or of a beneficial interest in a trust shall be determined in accordance with the rules for constructive ownership of stock provided in Section 267(c) of the United States Internal Revenue Code of 1954, as amended, other than paragraph (3) of such section.

13a.3. Unitary business.

13a.3.a. Determination of a unitary or separate Business.

13a.3.a.1 A corporation subject to taxation may be engaged in more than one "trade or business." In such cases, it is necessary to determine the business income attributable to each separate trade or business. The income of each business is then apportioned by a formula which takes into consideration the instate and out-of-state factors which relate to the respective trade or business subject to apportionment.

13a.3.a.2. In addition, a corporation may be engaged in a single trade or business in combination with another commonly owned and controlled corporation or corporations. In such cases, it is necessary to determine the total business income of all such corporations attributable to the single trade or business. The combined income of the single trade or business is then apportioned by formula which takes into consideration the in-state and out-of-state factors of each corporation which relate to that single trade or business.

13a.3.a.3. When business segments of a single corporation or the business activities of more than one corporation constitute a single trade or business, such single trade or business is said to constitute a "unitary business."

13a.3.a.4. A unitary business exists when the operations of the business segments of a corporation or group of commonly owned and controlled corporations contribute to or depend on each other in such a way as to result in functional integration between such segments. Functional integration refers to transfers between or pooling among business segments of such items as products or services, technical information, marketing information, distribution systems, purchasing and intangibles (such as patents, copyrights, formulas, processes, trade secrets, and the like) in a manner which substantially affects the segments' business operations related to such activities as

development, manufacture, production, extraction, distribution or sale of its products or services.

13a.3.a.5. Evidence of functionally integrating factors. -- The determination of whether or not the operations of business segments are functionally integrated will turn on the facts and circumstances of the case. Several factors may evidence that the operations of business segments are functionally integrated. A non-exclusive list of such factors is found below . Generally, several functionally integrating factors will exist in a unitary business, although a unitary business may exist as a result of few factors or even one factor, if the factor or factors involved are particularly significant. In determining whether a unitary business exists factors should not be examined in isolation. Instead, it should be determined whether the factors which are present, in combination, result in a functionally integrated business. In addition, the presence or absence of any one factor or any particular factors is not necessarily determinative as to whether a unitary business exists, although absence of all of the factors described in this subsection will generally result in a finding that a unitary business does not exist.

13a.3.a.6. Functionally integrating factors. -- A non-exclusive listing of factors to be considered in determining whether business segments are functionally integrated appears below.

13a.3.a.6.A. The existence or non-existence of the following factors will assist in the determination of whether "unity of operations" exits with respect to an affiliated group. The existence or non-existence of any one factor, by itself, is normally not determinative of whether the element has or has not been satisfied. Nor is this list a limitation on the factors that may be considered in determining whether unity of operations exists:

13a.3.a.6.A.1. Common or centralized purchasing;
13a.3.a.6.A.2. Common or centralized advertising;
13a.3.a.6.A.3. Common or centralized employees, including sales force;
13a.3.a.6.A.4. Common or centralized accounting;
13a.3.a.6.A.5. Common or centralized legal support;
13a.3.a.6.A.6. Common or centralized retirement plan;
13a.3.a.6.A.7. Common or centralized insurance coverage;
13a.3.a.6.A.8. Common or centralized marketing;
13a.3.a.6.A.9. Common or centralized cash management;
13a.3.a.6.A.10. Common or centralized research and development;
13a.3.a.6.A.11. Common or centralized offices;
13a.3.a.6.A.12. Common or centralized manufacturing facilities;
13a.3.a.6.A.13. Common, centralized or intercompany financing;
13a.3.a.6.A.14. Common or centralized computer systems and support;
13a.3.a.6.A.15. Common or centralized management;
13a.3.a.6.A.16. Common or centralized labor relations;

13a.3.a.6.A.17. Common or centralized pension plans;
13a.3.a.6.A.18. Common or centralized personnel recruitment;
13a.3.a.6.A.19. Intercompany sales, exchanges, or transfers;
13a.3.a.6.A.20. Common, centralized or intercompany transfer or pooling of technical information;
13a.3.a.6.A.21. Common or centralized distribution system, including but not limited to common or centralized transportation facilities, or common or centralized warehousing facilities, or common or centralized order fulfillment systems, inventory control systems or other distribution systems or subsystems, or any combination thereof.

13a.3.a.7. Intercompany sales, exchanges, or transfers.

13a.3.a.7.A. Sales, exchanges, or transfers (hereinafter "sales") of products, services, intangibles or the like between business segments are important indicia of functional integration. The significance of intercompany sales will be a function of both the character of the items sold and percentage of total sales or purchases represented by the intercompany sales. Intercompany sales at a given level take on greater significance if there is a limited sales or purchasing market for such items or if valuable trade name or other intangibles are associated with such sales, or both.

13a.3.a.7.B. The fact that intercompany sales are at a readily determinable market price does not negate the importance of such sales as a functionally integrating factor, because such sales generally represent an assured market for the seller and a guaranteed source of supply for the purchaser.

13a.3.a.7.C. As the percentage of intercompany sales to the total sales of the selling segment increases or as the percentage of intercompany purchases of the purchasing segment's total purchases increases, the more important such purchases and sales become as a unitary factor.

For purposes of this subdivision, where goods, services, or intangibles are transferred without charge, percentages of cost (or cost of goods sold) may be used in lieu of percentage of sales or purchases. For purposes of this subdivision, management stewardship activities are not considered an intercompany sale or transfer of services. Generally, intercompany sales or purchases in excess of 10% will be considered a significant, although not necessarily determinative, unitary factor. Sales of less than 10% become relatively less significant as the percentage of sales declines, but a small percentage of sales may nevertheless be considered significant if the sales represent goods or services which are particularly important to the purchaser's operations.

13a.3.a.7.C.1. Example. - Business segments A and B are commonly owned and controlled. Segment A grows citrus and other fruit. Segment B manufactures soft drinks. A sells to B oils extracted from the skin of a special variety of fruit for use in B's soft drinks. This oil is not significantly available from other sources. The sales represent only a small portion of A's total sales and B's total purchases. The unusual flavor produced by the oil is a major factor in the character of the soft drink. Consumer taste tests demonstrate a strong preference for the soft drink with this oil as an ingredient. The intercompany sales between A and B would be considered a significant unitary factor.

13a.3.a.7.D. Sales, exchanges or transfers between business segments may be disregarded where intercompany sales are used as a device to assert unitary combination for tax avoidance purposes.

13a.3.a.8. Common marketing.

13a.3.a.8.A. When business segments share substantial common marketing features, such features can be an important characteristic of functional integration when such marketing results in significant mutual advantage. For this purpose, common marketing exists when a substantial portion of the business segments' products, services, intangibles, or the like are distributed or sold to a common customer, or the business segments use a common trade name or other common identification and such common identification is a significant factor in purchasers' decisions to purchase the respective products or services.

13a.3.a.8.A..1. Example. - Business segments A and B are commonly owned and controlled. A manufactures small tools and garden implements. B manufactures auto replacement parts and accessories. Both A and B jointly sell a substantial portion of both segment's total production to various hardware store chains, which then sell both product lines to the public. As a result of such common sales, both segments are able to obtain preference on shelf space and greater merchant participation in product promotion of each segment. Such common sales would be considered a functionally integrating factor.

13a.3.a.8.A.2. Example. - Commonly owned and controlled segments A, B, and C manufacture furniture, carpeting, and household appliances, respectively. All three product lines are sold under the name "Alpha" which is a nationally recognized trade name. A, B and C jointly participate in advertising to portray the "Alpha" name as a symbol of quality and value. Based on consumer studies, the "Alpha" name is a significant factor in the consumer's decision to purchase the respective products. The common use of the trade name "Alpha" would be considered a functionally integrating factor.

13a.3.a.8.B. Common use of an advertising agency does not constitute common marketing, absent circumstances described above. In addition, shared use of a commonly owned and controlled business segment which provides advertising

services is not common marketing described by this subparagraph, absent circumstances described above.

13a.3.a.9. Common, centralized or intercompany transfer or pooling of technical information. -- Evidence of functional integration may be indicated by transfers or pooling of technical information, know-how, or research and development, if such transfer or pooling represents a significant economy of scale or the information shared is particularly important to the segments' operations.

13a.3.a.10. Common distribution system. -- Business segments may demonstrate evidence of functional integration by use of a common distribution system, under which inventory control and accounting, storage, trafficking and transportation are controlled through a common network.

13a.3.a.11. Common purchasing. -- Evidence of functional integration may be indicated by common purchasing of substantial quantities of products, services intangibles, or the like from the same source, where such purchasing results in a significant economy of scale, or where such products, services, intangibles, or the like are not readily available from other sources and are particularly important to each segment's operations or sales.

13a.3.a.12. Centralized management.

13a.3.a.12.A. Centralization of management exists when directors, officers and/or management employees jointly participate in management decisions which significantly affect the respective business segments. Transfer of officers or management employees between business segments may also provide evidence of centralization of management.

13a.3.a.12.B. The mere presence of centralized management is not sufficient to support a finding that the operations of commonly owned and controlled business segments are functionally integrated. Only those centralized management activities which contribute to the integration of the operations under consideration constitute a functionally integrating factor. Centralized efforts to fulfill investment stewardship responsibilities, such as the implementation of a uniform system of internal controls, or regulatory reporting requirements, such as the establishment of centralized information processing, will not be determinative for this purpose.

13a.3.a.12.B.1. Example. -- Business segments A, B, C, D, and E are commonly owned and parts of a large nationwide conglomerate. Segments A, B, C, and D manufacture clothing, furniture, musical instruments, and bakery products, respectively. Segment E is a book publisher. The managers of E receive monthly financial reports from each of the segments, review and approve budgets of each segment, review and approve major acquisitions and new product lines of each segment, review and approve hiring and firing of managers of each segment, and provide for intercompany financing. None of the respective segments has intercompany

sales, common marketing, pooling of technical knowledge, a common distribution system, or common purchases with any other segment. Due to the absence of significant functional integration among each of the respective segments, each business segment constitutes a separate trade or business.

13a.3.a.12.C. Centralization of management is more significant as a unitary factor when business segments are engaged in the same general line of business or constitute steps in a vertically integrated enterprise than in other business contexts, because of the opportunity the respective segments have in making use through such central management of readily transferable knowledge and expertise of the operations of the other segment, and developing coordination between the business segments.

13a.3.a.12.D. Factors accorded little weight. -- Factors such as common legal services, accounting, tax administration, and financial reporting will generally be accorded little weight in the determination of whether business segments are functionally integrated.

13a.3.a.12.E. The presence of a unitary business will be presumptively shown by the presence of the following:

13a.3.a.12.E.1. Same general line of business: There is a strong presumption that a corporation or a commonly owned and controlled group of corporations is engaged in a unitary business when its activities are in the same general line. For example, a corporation which operates a chain of retail grocery stores will almost always be engaged in a unitary business.

13a.3.a.12.E.2. Steps in a vertical process: A corporation or a commonly owned or controlled group of corporations is almost always engaged in a unitary business when its various divisions or segments are engaged in different steps in a vertically structured enterprise. For example, a corporation which explores for and mines copper ores; concentrates, smelts and refines the copper ores; fabricates the refined copper into consumer products and distributes such products (whether by intercompany fee or purchase, or without charge) is engaged in a unitary business, regardless of the fact that the various steps in the process are operated substantially independently of each other with only general supervision from the corporation's executive offices.

13a.3.a.12.F. Business segments which are neither in the same general line of business nor steps in a vertical process are presumptively engaged in separate businesses, absent a determination that the respective segments are functionally integrated.

13a.3.a.12.F.1. In the event that a business segment is functionally integrated with a second business segment and the second business segment is functionally integrated with a third business segment, the first, second and third

business segments constitute a unitary business notwithstanding the fact that the first and third business segments are not functionally integrated with each other. The preceding sentence shall not apply where the second business segment's functional integration is not substantial viewed from the perspective of either the first or third business segment.

13a.3.a.12.F.1.1. Example. – Business segments A, B, and C are commonly owned and controlled. A is an architectural firm. B is a construction company which builds office and apartment buildings. C is a manufacturer of finished steel. A provides architectural services to B, representing half of the total architectural services it provides. C designs, fabricates, and sells the superstructures used in the construction of B's office and apartment buildings. The steel superstructures constitute 20% of B's construction purchases. A and C have no intercompany sales, common marketing, pooling of technical knowledge, common distribution system or common purchases. Nevertheless, A, B, and C constitute a unitary business because B is functionally integrated with both A and C.

13a.3.a.12.F.1.2. Example. – Business segments A, B, and C are commonly owned and controlled. A is in the business of oil exploration, extraction and refining. B is a charter air transportation company. C produces motion pictures. A and C have no intercompany sales, common marketing, pooling of technical knowledge, or common distribution system. A uses B's service for transporting oil executives, engineers and geologists to remote oil exploration and drilling sites. C uses B's services for flying movie executives and actors to movie locations and business meetings. A and C's common purchases are limited to the transportation services provided by B. A's use of B's service constitute 20% of B's total charter sales. C's use of B's service constitutes 40% of B's total charter sales. However, B's service represents less than a hundredth of a percent of A's total purchases and only two tenths of a percent of C's total purchases. Despite the fact that B is functionally integrated with both A and C, A, B, and C do not constitute a unitary business.

13a.3.a.12.G. Where the taxpayer asserts that business segments are or are not unitary, the taxpayer shall have the burden of proof. Failure by the taxpayer to produce requested evidence which lies within the control of the taxpayer gives rise to a presumption that the evidence would be unfavorable if provided.

13a.3.a.12.H. No divisional segregation or separation for purposes of determining unitary group member status, income or attributes. If a corporation or other entity is organized into divisions or other functional units or business segments not constituting separate legal entities, the corporation or entity so organized shall, as a whole, be treated as the unitary member. No operations, income or apportionment factor attributes of any such division, functional unit or business segment shall be subtracted, segregated or separated from those of the combined group.

13a.3.a.12.H.1. If the business or operations, of any one division, unit, segment of separate part of a single business entity are unitary with those of other

entities, then the single business entity is a unitary member with those other entities, notwithstanding that the business or operations of one or more other divisions, units, segments of separate parts of that same single business entity are not unitary with the business or operations of such other entities.

13a.3.b. Establishment of unity for acquired entities and newly formed entities.

13a.3.b.1 Newly Acquired Corporations. When a corporation that is a member of a unitary group acquires another corporation, a presumption exists against a finding of a unitary relationship during the first reporting period unless a unitary relationship already existed at the time of the acquisition. The presumption may be rebutted by proving that the corporations are unitary. If such presumption is rebutted, then the corporations shall be considered unitary as of the date of acquisition, unless the evidence shows that unity was established as of another date.

13a.3.b.1.A. In the next succeeding reporting period after the first reporting period subsequent to an acquisition whereby a corporation that is a member of a unitary group acquires another corporation, and for all reporting periods thereafter, a presumption of a unitary relationship exists. The presumption may be rebutted by proving that the corporations are not unitary.

13a.3.b.2. Newly-Formed Corporations or entities. When a corporation that is a member of a unitary group forms another corporation, a presumption exists in favor of finding unity between the two corporations or entities as of the date of formation. Any party may rebut such presumption by proving that the corporations or entities are not unitary or became unitary at a later date

13a.3.b.2.A For purposes of this rule, a newly formed corporation or entity includes but is not limited to: a corporate reorganization whereby a corporate divestiture, split-up or split off occurs, or one or more new subsidiaries is formed, or one or more new subsidiaries is acquired and substantially all of the assets and operations of an existing division or operation are placed into or under the administrative or operational responsibility of the acquired entity, or a partnership is created or formed, or an existing corporation changes its form of doing business from one organizational structure to one or more new organizational structures or merges several subsidiary entities into an existing or newly formed entity.

13a.3.b..3 Unitary members compute their liability relating to a year when a member is added to or departs from the unitary group as follows:

13a.3.b.3.A. If a corporation becomes a member of a unitary group during the group's common accounting period, or ceases to be a member during the period, the other members shall take into account the appropriate portion of the part year member's income and the property, payroll, sales attributes of the part-year member in computing their tax liabilities.

13a.3.b.3.A.1. part-year unitary member computes its liability as follows:

13a.3.b.3.A.1.1 business income attributable to the portion of the year during which the part-year unitary member was a unitary group member is combined with business income of the other unitary group members for the same portion of the year, and the total income is apportioned to West Virginia on a combined apportionment basis; and

13a.3.b.3.A.1.2 business income attributable to the portion of the year during which the part-year unitary member was not a unitary member is apportioned to West Virginia on the basis of the part year member's separate property, payroll, and sales attributes for the part of the year during which the part-year unitary member was not a unitary member. The corporation is required to file a separate return for this portion of its income.

13a.3.c. Holding Companies. The test for a unitary business established by this rule applies in determining whether a holding company is included or excluded from a unitary business

13a.3.d. Statute of limitations. If the statute of limitations applicable to refund claims and assessments is open with respect to a particular member of the combined group, the statute of limitations is open with respect to that particular Taxpayer notwithstanding the fact that the statute of limitations may have expired for one or more other members of the combined group.

13a.3.d.1 The statute of limitations applicable to refund claims and assessments for members of a combined reporting group which have filed their tax return based on a fiscalized reporting period matched to the accounting period of a principal member, shall be the statute of limitations determined and calculated based on the fiscalized accounting period.

13a.3.d.2. If a return is filed pursuant to a combined report, the Tax Commissioner may examine and audit that return, and collect any deficiency from a combined group member for whom the statute of limitations for assessments has not expired, even if the statute of limitations for other members which filed pursuant to the same combined report has expired. Any deficiency assessed pursuant to such audit or examination will not cause a reopening of the statute of limitations for those other members for which the statute of limitations has expired who filed pursuant to the same combined report.

§§110-24-13b. Reserved for future use.

§110-24-13c. Net operating loss (NOL) carryovers earned during a year in which the Taxpayer filed a consolidated tax return.

13c.1 West Virginia computes net operating losses on a post-apportionment basis, including business and non-business income adjustments. NOL's can only be carried forward (or backwards) to be applied against West-Virginia source income of the combined group member to which it is attributable. NOL's cannot be used by other members of the combined group. There is an exception for NOLs earned when the Taxpayer was filing on a consolidated basis. Those NOLs can be carried over and applied against the income of any former member of the consolidated (controlled) group.

13c.1.a. West Virginia Code §11-24-13c(b)(1)(G) reads in relevant part as follows:

> **§ 11-24-13c. Determination of taxable income or loss using combined report.**
>
> **(a)** . . . .
>
> **(b) Components of income subject to tax in this State; application of tax credits and post-apportionment deductions.**
>
> **(1)** Each taxpayer member is responsible for tax based on its taxable income or loss apportioned or allocated to this State, which shall include:
>
> . . . .
>
> **(F)** Its income or loss allocated or apportioned in an earlier year, required to be taken into account as state source income during the income year, other than a net operating loss; and
>
> **(G)** Its net operating loss carryover. If the taxable income computed pursuant to this section and section thirteen-d of this article results in a loss for a taxpayer member of the combined group, that taxpayer member has a West Virginia net operating loss, subject to the net operating loss limitations, and carryover provisions of this article. This West Virginia net operating loss is applied as a deduction in a prior or subsequent year only if that taxpayer has West Virginia source positive net income, whether or not the taxpayer is or was a member of a combined reporting group in the prior or subsequent year: **Provided, That net operating loss carryovers *that were earned during a tax year in which the taxpayer filed a consolidated return* under this article may be applied as a deduction from the West Virginia taxable income of any member of the taxpayer's controlled group until the net operating loss carryover is used or expires pursuant to the net operating loss provisions of this article.**

Emphasis added.

13c.1.a.1. West Virginia Code §11-24-13c(b)(1)(G) specifies that there is an exception for NOLs **earned when the Taxpayer was filing on a consolidated basis**.

13c.1.a.2. An attempt to amend a pre 2009 separate return and file a consolidated return for that year, and to use an NOL on that return that was **earned in a year when the Taxpayer was filing separately** will be disallowed. And the Taxpayer cannot claim those NOLs on the 2009 and forward combined return.

§110-24-13d. Intercompany Transactions

13d.1. In general.

13d.1.a. Purpose. This section provides rules for reporting intercompany transactions of members of a combined reporting group in order to clearly reflect the taxable income (and tax liability) of the taxpayer members that is allocated or apportioned to West Virginia. The general rule is that business income from intercompany transactions (composed of both gains or losses) will be deferred in order to produce the effect of transactions between divisions of a single corporation in a manner similar to Title 26, Code of Federal Regulations, section 1.1502-13 (26 C. F. R. 1.1502-13 or Treasury Regulation section 1.1502-13). See West Virginia Code §11-24-13d(e)

13d.1.b. Conformity to Treasury Regulation section 1.1502-13. Intercompany transactions. Except as otherwise provided, this section 13d incorporates Treasury Regulation section 1.1502-13, as amended through June 30, 2009, to the extent possible consistent with combined reporting principles to enable ease of administration and compliance. This section 13d does not restate all the provisions of the federal regulation in full. However, the methodology adopted under the federal regulation shall apply except as otherwise provided in this section 13d. Exceptions will arise due to the differences between the composition of the federal consolidated group and the combined reporting group, the requirements of West Virginia's allocation and apportionment provisions, jurisdictional limitations, and treatment of members of a combined reporting group as separate entities for many purposes under the West Virginia Code. Exceptions may also arise in those instances when Treasury Regulation section 1.1502-13 incorporates by reference provisions of the Internal Revenue Code to which West Virginia has not conformed. Unless explicitly provided otherwise, conformity to Treasury Regulation section 1.1502-13 in no way implies conformity to any other regulation under section 1502 of the Internal Revenue Code.

13d.1.c. Timing rules as a method of accounting. This section 13d applies the provisions of Treasury Regulation section 1.1502-13(a)(3), except for the reference to Treasury Regulation section 1.1502-17. The rules shall apply to all members of the combined reporting group.

13d.1.d. Other Law. Other applicable law (including nonstatutory authorities) shall apply in addition to this section 13d to the extent that this section 13d does not exclude such application.

13d.1.d.1. Non-applicability of section 304 of the Internal Revenue Code. As provided in Treasury Regulation section 1.1502-80, section 304 of the Internal Revenue Code, to which West Virginia conforms pursuant to West Virginia Code §11-24-3, does not apply to any acquisition of stock of a corporation in an intercompany transaction occurring on or after January 1, 2009.

13d.1.d.2. Non-applicability of section 163(e)(5) of the Internal Revenue Code. As provided in Treasury Regulation section 1.1502-80, section 163(e)(5) of the Internal Revenue Code, to which West Virginia conforms pursuant to West Virginia Code §11-24-3, does not apply to any intercompany obligation (within the meaning of subsection **13d.7.** issued in a tax year beginning on or after January 1, 2009.

13d.1.d.3. Non-applicability of section 1031 of the Internal Revenue Code. As provided in Treasury Regulation section 1.1502-80, section 1031 of the Internal Revenue Code, to which West Virginia conforms pursuant to West Virginia Code §11-24-3, does not apply to any intercompany transaction occurring in income years beginning on or after January 1, 2009.

13d.1.e. Sourcing. In the income year that intercompany items are taken into account, their source shall be determined as if the selling member (S) and the buying member (B) are divisions of a single corporation. Therefore, such intercompany items are treated as current apportionable business income and are apportioned to West Virginia in accordance with West Virginia Code §11-24-1, *et seq.* West Virginia law does not conform to the federal sourcing rules provided or referenced in Treasury Regulation section 1.1502-13, with relation to worldwide unitary reporting and with relation to activity in a tax haven, as specified in West Virginia Code §11-24-1 *et seq.*

13d.1.e.1. Sales Factor.

13d.1.e.1.A. Sales attributable to intercompany items are not included in S's sales factor either in the year of the transaction or in the year(s) in which such intercompany items are taken into account.

13d.1.e.1.B. Gross receipts from the sale generating B's corresponding item will be included in B's sales factor in the year of the sale if otherwise included under West Virginia Code §11-24-1, *et seq.*, unless such gross receipts are excluded under an "other method of allocation and apportionment," as authorized by subsection 11-24-7(h) of the West Virginia Code.

13d.1.e.1.C. Deemed sales under Treasury Regulation section 1.1502-13(d)(1)(ii) will be disregarded for purposes of the sales factor.

13d.1.e.2. Property factor.

13d.1.e.2.A. On the date of the intercompany transaction, the property transferred from S to B will be included in B's property factor at the original cost to S.

13d.1.e.2.B. Intercompany rent expense is not included in the property factor.

13d.1.e.2.C. Intercompany obligations shall not be included in the property factor.

13d.1.e.2.D. If S's intercompany item is accelerated as a result of S or B no longer being members of the same combined reporting group, the value of B's property acquired from S in an intercompany transaction will be adjusted immediately after the acceleration event to reflect B's original cost (the purchase price paid by B to S).

13d.1.e.2.E. Subparagraphs **13d.1.e.2.A** through **13d.1.e.2.D.**. above relating to the property factor shall apply regardless of whether an election is made under this section 13d to treat an intercompany transaction on a separate entity basis.

13d.1.f. Overview. The principal provisions of this section 13d that implement single entity treatment are the matching rule of subsection **13d.3.** and the acceleration rule of subsection **13d.4.** Under the matching rule, Seller (S) and Buyer (B) are generally treated as divisions of a single corporation for purposes of taking into account their items from intercompany transactions. The acceleration rule provides rules for taking the items into account if the effect of treating S and B as divisions cannot be achieved (for example, if S or B leave the combined reporting group or if the asset transferred in the intercompany transaction is converted to nonbusiness use). Intercompany items will be treated as current apportionable business income for the year(s) in which the item is taken into account. Subsection **13d.2.** provides definitions used in the application of this section 13d. Subsection **13d.5.** provides simplifying rules for certain transactions. Subsections 13d.6. and 13d.7. provide additional rules for stock and obligations of members. Subsections 13d.8 and 13d.9 provide anti-avoidance rules and miscellaneous operating rules.

13d.2. Definitions. For purposes of this rule:

13d.2.a. Intercompany transactions.

13d.2.a.1. Except as provided in paragraph **13d.2.a.2.**, the term "intercompany transaction" means a transaction between corporations which are members of the same combined reporting group immediately after such transaction. "S" is the member transferring property or providing services, and "B" is the member receiving the property or services. Intercompany transactions include, but are not limited to --

13d.2.a.1.A. S's sale of property (or other transfer, such as an exchange or contribution) to B;

13d.2.a.1.B. S's performance of services for B, and B's payment or accrual of its expenditures for S's performance;

13d.2.a.1.C. S's licensing of technology, rental of property, or loan of money to B, and B's payment or accrual of its expenditures; and

13d.2.a.1.D. S's distribution to B with respect to S stock.

13d.2.a.2. The term intercompany transaction does not include transactions which produce nonbusiness income or loss to the selling member or income attributable to a separate business activity of the selling member. The term intercompany transaction also does not apply when the asset transferred in the transaction is acquired for the buyer's nonbusiness use or for the use of a separate business activity of the buyer. For purposes of this section 13d, such transactions shall be considered as if between corporations that are not members of a combined reporting group.

13d.2.b. "Combined reporting group" means a group of corporations, that is permitted or required to be included in a particular combined report under West Virginia Code §11-24-1 *et seq.* and any non corporate entities permitted or required to be so included. For purposes of this rule, the members of the combined reporting group include:

13d.2.b.1. Both S and B, when the income and apportionment factors of those corporations are properly included in the same combined report for the income year of the intercompany transaction; and

13d.2.b.2. Any affiliated corporation (or portion thereof) whose income and apportionment factors are properly included in the same combined report in combination with the income and apportionment factors of S and B for that income year.

13d.2.c. "Combined reporting group member" means any corporation or entity that is permitted or required to be included in a particular combined report under West Virginia Code §11-24-1, *et seq.*

13d.2.d. Intercompany items.

13d.2.d.1. In general. S's income, gain, deduction, and loss from an intercompany transaction are its intercompany items. For example, S's gain from the sale of property to B is an intercompany gain. An item is an intercompany item whether it arises directly or indirectly from an intercompany transaction.

13d.2.d.2. Related costs or expenses. S's costs or expenses related to an intercompany transaction are included in determining its intercompany items.

13d.2.d.3. Amounts not yet recognized or incurred. S's intercompany items include amounts from an intercompany transaction that are not yet taken into account in computing its net income under its separate entity method of accounting.

13d.2.e. Corresponding items. B's income, gain, deduction, and loss from an intercompany transaction, or from property acquired in an intercompany transaction, are its corresponding items. If B buys property from S and sells it to a nonmember, B's gain or loss from the sale to the nonmember is a corresponding gain or loss. An item is a corresponding item whether it is directly or indirectly from an intercompany transaction (or from property acquired in an intercompany transaction).

13d.2.f. Recomputed corresponding items. The recomputed corresponding item is the corresponding item that B would take into account if S and B were divisions of a single corporation and the intercompany transaction was between those divisions. For example, if S sells property with a $ 70 basis to B for $ 100, and B later sells the property to a nonmember for $ 90, B's corresponding item is its $ 10 loss, and the recomputed corresponding item is $ 20 of gain (determined by comparing the $ 90 sales price with the $ 70 basis the property would have had if S and B were divisions of a single corporation).

13d.2.g. Treatment as a separate entity. Treatment as a separate entity means treatment without application of the provisions of this section 13d (other than the provisions of subdivision **13d.1.d.**), but with the application of the other provisions of this rule. "Treatment as a separate entity" does not operate to prevent the income or loss taken into account under applicable rules for separate entity treatment from being properly characterized as combined report business income of the combined reporting group.

13d.2.h. Divisions of a single corporation. When S and B are treated as divisions of a single corporation for purposes of this section 13d, such divisional treatment applies only to the unitary, apportionable trade or business operations included in the combined report. For example, neither nonbusiness income of S or B, nor income from activities of S or B that are excluded from a water's-edge combined report, will be considered for purposes of treating S and B as divisions of a single corporation.

13d.2.i. Deferred Intercompany Stock Account ("DISA"). DISA is the accounting mechanism that a distributee corporation, which is a member of the combined reporting group, will use to report and track non-dividend distributions in excess of its adjusted basis in the stock of the distributing subsidiary corporation, which is a member of the same combined reporting group, until this intercompany item is required to be taken into account pursuant to this section 13d. The balance of each DISA account must be disclosed annually on the taxpayer's return.

13d.2.j. Attributes. The attributes of an intercompany item or corresponding item are all of the item's characteristics, except amount, location, and timing, necessary to determine the item's effect on taxable income (and tax liability). For purposes of this section 13d, "location" does not refer to geographical location, but instead refers to location within the combined reporting group, i.e., which member of the combined reporting group realizes the item.

13d.3. Matching rule. S shall take its intercompany items into account in any year where there is a difference between B's corresponding item and the recomputed corresponding item. The separate entity attributes of S's intercompany items and B's corresponding items are redetermined to the extent necessary to produce the same effect on total group combined report business income as if S and B were divisions of a single corporation, and the intercompany transaction was a transaction between divisions. Unless otherwise provided, this section 13d applies the matching rule provisions of Treasury Regulation section 1.1502-13(c). Exceptions will arise due to the reasons stated in subdivision **13d.1.b.**

13d.3.a. Redetermination of separate entity attributes does not apply to the sourcing of the combined report business income. Sourcing of income is described in subdivision **13d.1.e.**

13d.3.b. Examples: For purposes of the examples in this subdivision **13d.3.b**, unless otherwise stated, P, S and B are members of a combined reporting group. P owns all of the stock of S and B. Y is a person (as defined in West Virginia Code §11-24-3a) unrelated to any member of the combined reporting group. The income year of all persons is the calendar year.

Example 1: Intercompany sale of land followed by sale to a nonmember.

(Refer to Treas. Reg. § 1.1502-13(c)(7)(ii), example 1.)

Facts. S holds land with a basis of $ 70 for use in the trade or business of the combined reporting group. On January 1 of Year 1, S sells the land to B for $ 100. B also holds the land for use in the trade or business of the combined reporting group. On July 1 of Year 3, B sells the land to Y for $ 110.

Definitions. S's sale of the land to B is an intercompany transaction. S's $ 30 gain from the sale to B is its intercompany item, and B's $ 10 gain from its sale, to Y is its corresponding item. The total gain of $ 40 is the recomputed corresponding item.

Timing. Under the matching rule, S takes its intercompany item into account in the income year(s) in which there is a difference between B's corresponding item and the recomputed corresponding item. If S and B were unitary divisions of a single corporation and the intercompany sale was a transfer between the divisions, B would succeed to S's $ 70 basis in the land and would have a $ 40 gain from the sale to Y in Year 3, instead of a $ 10 gain. Consequently, S takes no gain into account in Years 1 and 2, and takes the entire $ 30 gain into account in Year 3, to reflect the $ 30 difference in that year between the $ 10 gain B takes into account and the $ 40 recomputed gain (the recomputed corresponding item). In accordance with subdivision **13d.9.d.**, the earnings and profits of S will not reflect S's $ 30 gain until the gain is taken into account in Year 3.

Apportionment. As would be the case if S and B were unitary divisions of a single corporation and the intercompany sale was a transfer between the divisions, that

transfer will not be reflected in the sales factor in Year 1. In Year 3, the $ 110 gross receipts from B's sale of the land to Y will be included in B's sales factor unless the receipts are excluded pursuant to West Virginia Code §11-24-7(h). The land is attributable to B after the intercompany sale, and it will be reflected in B's property factor at S's $ 70 original cost basis until it is sold outside the combined reporting group in Year 3. This is the result that would have occurred had the intercompany transaction been a transfer between unitary divisions. Both S's $ 30 gain and B's $ 10 gain will be treated as current apportionable business income in Year 3.

Example 2: Intercompany sale of depreciable property.

(Refer to Treas. Reg. § 1.1502-13(c)(7)(ii), example 4.)

Facts. On January 1 of Year 1, S buys property with a 10-year useful life for $ 100 and begins to depreciate it under the straightline method. On January 1 of Year 3, S sells the property to B for $ 130. B determines that the useful life of the property is 10 years from the date of B's acquisition, and also uses the straightline method. Both S and B used the property in their unitary trade or business.

Depreciation through Year 3; intercompany gain. S claims $ 10 of depreciation for each of Years 1 and 2 and has an $ 80 basis at the time of the sale to B. Thus, S has a $ 50 intercompany gain from its sale to B ($ 130 sales price - $ 80 adjusted basis). For Year 3, B has $ 13 of depreciation with respect to its $ 130 basis.

Timing. If S and B were divisions of a single entity, that entity would modify its useful life of the property based upon the same change in facts and circumstances that caused B to determine that the useful life would exceed the original 10 year period. Therefore, the recomputed depreciation for Years 3 through 12 would be $ 8 per year ($ 80 remaining basis/redetermined 10-year life). S's $ 50 gain is taken into account to reflect the difference for each income year between B's $ 13 depreciation (B's corresponding item) and the $ 8 recomputed depreciation. Thus, S takes $ 5 of gain into account in each of Years 3 through 12.

Apportionment. As would be the case if the intercompany sale was a transfer between unitary divisions of a single corporation, the transfer will not be reflected in the sales factor. The property will be included in B's property factor at S's $ 100 original cost basis regardless of the subsequent depreciation or intercompany gain taken into account. In each year, S's intercompany gain and B's depreciation deduction will be included in the computation of combined report business income and apportioned using the current apportionment percentage for that year.

Example 3: Intercompany sale followed by installment sale.

(Refer to Treas. Reg. § 1.1502-13(c)(7)(ii), example 5.)

Facts. S holds land with a basis of $ 70 for use in the trade or business of the combined reporting group. On January 1 of Year 1, S sells the land to B for $ 100. B also holds the land for use in the trade or business of the combined reporting group. On July 1 of Year 3, B sells the land to Y in exchange for Y's $ 110 note. The note provides for 24 monthly interest payments beginning August 1 of Year 3, and for principal payments of $ 55 in Year 4 and $ 55 in Year 5. The West Virginia apportionment percentage for the combined reporting group was 10% in Year 3, 90% in Year 4, and 93% in Year 5. The amount of the installment note is substantial in relation to the business activities of the combined reporting group. Therefore, because the deferral of gain recognition under the installment sale provisions should not substantially change the ultimate amount of income apportioned to West Virginia, the installment income shall be apportioned using the apportionment percentage from the year in which the installment sale occurred.

Timing and attributes. Under section 453 of the Internal Revenue Code, B's corresponding items are its $ 5 gain in Year 4, and its $ 5 gain in Year 5. B's recomputed gain, computed as if the intercompany sale were a transfer between unitary divisions, would be $ 20 in Year 4 and $ 20 in Year 5. Thus, S takes $ 15 of intercompany gain into account in each of Years 4 and 5 to reflect the difference between B's $ 5 corresponding gain and $ 20 recomputed gain. B's interest income on the installment note is not a corresponding item, and is taken into account when accrued in Years 3 through 5.

Apportionment. As would be the case if the intercompany sale was a transfer between divisions, there will be no effect on the sales factor in Year 1, and the $ 110 gross receipts from the sale to Y will be included in B's sales factor in Year 3 (assuming that the receipts were not excluded pursuant to West Virginia Code §11-24-7(h). Because the installment sale income is being apportioned to West Virginia using the apportionment percentage from the year of the sale to Y under section 453 of the Internal Revenue Code, both S's $ 15 intercompany gain and B's $ 5 corresponding gain for each of Years 4 and 5 will be apportioned to West Virginia using the 10% apportionment percentage from Year 3. The property will be included in B's property factor at S's $ 70 cost basis until it is sold to Y in Year 3. B's interest income accrued in Years 3, 4 and 5 is current period income and will be apportioned using the current apportionment percentages for those years (10%, 90% and 93%, respectively).

Example 4: Intercompany sale of installment obligation.

(Refer to Treas. Reg. § 1.1502-13(c)(7)(ii), example 6.)

Facts. S holds land with a basis of $ 70. On January 1 of Year 1, S sells the land to Y in exchange for Y's $ 100 note, and S reports its gain on the installment method under section 453 of the Internal Revenue Code. Y's note bears interest at a market rate of interest in excess of the applicable federal rate, and provides for principal payments of $ 50 in Year 5 and $ 50 in Year 6. On July 1 of Year 3, S sells Y's note to B for $ 100, resulting in a $ 30 gain from S's prior sale of the land to Y. Both S's and B's income

would be considered business income. The West Virginia apportionment percentage for the combined reporting group was 8% in Year 1, 15% in Year 3, and 90% in Years 5 and 6. The amount of the installment note is substantial in relation to the business activities of the combined reporting group. Therefore, because the deferral of gain recognition under the installment sale provisions should not substantially change the ultimate amount of income apportioned to West Virginia, the installment income will be apportioned pursuant to West Virginia Code §11-24-7(h) using the apportionment percentage from the year in which the installment sale occurred.

Timing and attributes. S's sale of Y's note to B is an intercompany transaction, and S's $ 30 gain is an intercompany gain. S takes $ 15 of the gain into account in each of Years 5 and 6 to reflect the difference between B's $ 0 corresponding gain and B's $ 15 recomputed gain. S's gain continues to be treated as its gain from the sale to Y, and the deferred tax liability of each taxpayer member remains subject to the interest charge under section 453A(c) of the Internal Revenue Code.

Apportionment. The $ 100 gross receipts from the sale of the land to Y will be included in S's sales factor in Year 1. When S's gain is taken into account in Years 5 and 6, it should be apportioned to West Virginia using the 8% apportionment percentage from Year 1. This is the same result that would have occurred had the intercompany sale of the installment note been a transfer between unitary divisions.

Worthlessness. Assume that Y's note becomes worthless on December 1 of Year 3 and B has a $ 100 loss on a separate entity basis (a $ 100 corresponding loss). S takes its $ 30 gain into account in Year 3 to reflect the difference between B's $ 100 corresponding loss and B's $ 70 recomputed loss. On a separate entity basis, S's $ 30 gain would be an installment gain. However, there would be no net installment income if S and B were divisions of a single corporation. Therefore, when the separate entity attributes of S's intercompany items and B's corresponding items are redetermined under Treasury Regulation section 1.1502-13(c)(1)(i) to produce the same effect as if S and B were divisions of a single corporation, both S's $ 30 gain and B's $ 100 loss will be apportioned to West Virginia using the 15% apportionment percentage from Year 3.

Example 5: Performance of services by a member for a member.

(Refer to Treas. Reg. § 1.1502-13(c)(7)(ii), example 7.)

Facts. S is a driller of water wells. B operates a ranch and requires water to maintain its cattle. During Year 1, B pays S $ 100 to drill an artesian well on B's ranch, and S incurs $ 80 of expenses related to drilling the well. B capitalizes its $ 100 cost for the well, and takes into account $ 10 of depreciation deductions in each of Years 2 through 11. If S and B were divisions of a single corporation, the $ 80 costs incurred in drilling the well would be capitalized and the depreciation deduction would be $ 8 in each of Years 2 through 11.

Timing. S has intercompany income of $ 20 ($ 100 receipts less $ 80 expenses). In each of Years 2 through 11, S takes $ 2 of its intercompany income into account to reflect the annual difference between B's $ 10 corresponding depreciation deduction and the $ 8 recomputed depreciation deduction.

Apportionment. As would be the case if the services were performed between unitary divisions of a single corporation, the transaction will not be reflected in the sales factor. If S's expenses related to drilling the well included payroll expenses, those expenses would be included in the payroll factor in Year 1. When the well is placed in service, it will be included in B's property factor at its capitalized cost to S of $ 80. In each year, S's $ 2 intercompany income and B's $ 10 depreciation deduction will be included in current apportionable business income for that year.

Example 6: Intercompany rental of property.

(Refer to Treas. Reg. § 1.1502-13(c)(7)(ii), example 8.)

B operates a ranch that requires grazing land for cattle. S owns land adjoining B's ranch. On January 1 of Year 1, S leases grazing rights for one year to B for $ 100. S takes its $ 100 rental income into account in Year 1 to reflect the $ 100 difference between B's $ 100 corresponding rental deduction and the $ 0 recomputed rental deduction. To achieve the effect of the rental transaction occurring between unitary divisions of a single corporation, the intercompany rental income will not be included in S's sales factor. The land will continue to be included in S's property factor at its original cost, and B's property factor will not reflect B's rent expense related to the land.

Example 7: Source of income subject to section 863 of the Internal Revenue Code.

(Refer to Treas. Reg. § 1.1502-13(c)(7)(ii), example 14.)

Facts. S manufactures inventory in the United States, and recognizes $ 75 of income on sales to B in Year 1. B resells the inventory in Country F and recognizes $ 25 of income on sales to Y, also in Year 1.

Timing. Under the matching rule, S's $ 75 intercompany income and B's $ 25 corresponding income are taken into account in Year 1.

Apportionment. West Virginia law does not conform to the federal sourcing rules under section 863 of the Internal Revenue Code except that section 863 of the Internal Revenue Code is adopted pursuant to this rule for purposes of determining the extent to which a corporation's income and apportionment factors are included in a combined report. Furthermore, subdivision **13d.3.a.** provides that the redetermination of attributes described in Treasury Regulation section 1.1502-13(c)(1)(i) does not apply to the sourcing of West Virginia combined report business income. In order to achieve the results that would occur if S and B were divisions of a single corporation, B's receipts from its sales to Y will be reflected in B's sales factor in Year 1. Both S's $ 75

intercompany income and B's $ 25 corresponding item will be treated as current apportionable business income in Year 1.

13d.4. Acceleration rule. S's intercompany items and B's corresponding items are taken into account to the extent they cannot be taken into account to produce the effect of treating S and B as divisions of a single corporation. For example, except as provided in paragraph **13d.4.a.2.**, such effect cannot be produced if S and B are no longer in the same combined reporting group. Unless otherwise provided, this section 13d applies the acceleration rule provisions of Treasury Regulation section 1.1502-13(d). Exceptions will arise due to the reasons stated in subdivision **13d.1.b.**

13d.4.a. Additional circumstances which will cause the acceleration rule to be applied include:

13d.4.a.1. the asset which was transferred in the intercompany transaction is converted to nonbusiness use, or

13d.4.a.2. see subdivision **13d.9.c.** for additional acceleration rules applicable for corporations partially included in a water's-edge combined reporting group.

13d.4.b. Circumstances not known by end of year. In the event that circumstances which would cause the acceleration rule to be triggered during an income year are not known or have not occurred in time for the taxpayer members to file an accurate return, it may be necessary to make an estimate based on available information and amend the return at a later date.

13d.4.c. Examples. The acceleration rule of this subsection **13d.4.** is illustrated by the following examples.

Example 1: Becoming a nonmember.

(Refer to Treas. Reg. § 1.1502-13(d)(3), example 1.)

Facts. S owns land with a basis of $ 70, which it uses in the trade or business of the combined reporting group. On January 1 of Year 1, S sells the land to B for $ 100. B also uses the land for unitary business purposes. On July 1 of Year 3, P sells 60% of S's stock to Y and, as a result, S becomes a nonmember of the combined reporting group.

Matching rule. Under the matching rule, none of S's $ 30 intercompany gain is taken into account in Years 1 through 3 because there is no difference between B's $ 0 gain or loss taken into account and the recomputed gain or loss.

Acceleration of S's intercompany items. Once the stock of S is sold, S is no longer a member of the combined reporting group and the effect of treating the unitary operations of S and B as divisions of a single corporation cannot be produced.

Therefore, under the acceleration rule of this subsection **13d.4.**, S's $ 30 gain is taken into account in Year 3 immediately before S becomes a nonmember.

West Virginia does not conform to the stock basis adjustments required for federal consolidated filing purposes by Treasury Regulation section 1.1502-32. P's basis in S's stock will be P's original cost, increased by any capital contributions and decreased by any returns of capital.

Apportionment. The intercompany sale is not reflected in the sales factor in Year 1. In Year 3, P's receipts from the sale of S stock may be included in the sales factor if not otherwise excluded under West Virginia Code 1-24-1, *et seq.* or these rules. The land will be included in B's property factor at S's $ 70 original cost until S's intercompany gain is accelerated. Immediately after S's gain is taken into account, the $ 70 value of the land in B's property factor will be stepped up to reflect B's $ 100 cost. S's intercompany gain will be treated as current apportionable business income in Year 3.

Example 2: Conversion to nonbusiness use.

Facts. S owns land with a basis of $ 70 which it holds for use in the trade or business of the combined reporting group. On January 1 of Year 1, S sells the land to B for $ 100. B also uses the land in its trade or business. On July 1 of Year 3, B converts the land to a nonbusiness use.

Acceleration of S's intercompany items. Because the effect of treating the unitary operations of S; and B as divisions of a single corporation cannot be achieved once the land is removed from the unitary trade or business, the acceleration rule causes S to take its $ 30 gain into account immediately before the conversion to nonbusiness use takes place.

Apportionment. If the land had been transferred between divisions of a single corporation and then converted to nonbusiness use, those transactions would have no effect on the sales factor. Thus, neither the intercompany sale in Year 1 nor the acceleration of S's intercompany gain in Year 3 will be reflected in the sales factor. The land will be included in B's property factor at S's $ 70 original cost until it is converted to nonbusiness use, at which time it will be removed from the property factor. S's accelerated intercompany gain will be treated as current apportionable business income in Year 3.

13d.5. Simplifying rules.

13d.5.a. Unless otherwise provided, this section 13d applies the simplifying rules of Treasury Regulation section 1.1502-13(e), unless differences occur due to non-conformity of West Virginia Code §11-24-1 *et seq.* with federal treatment.

13d.5.b. Election to treat intercompany transactions on a separate entity basis.

13d.5.b.1. If members of the combined reporting group make a federal election to treat intercompany transactions on a separate entity basis under Treasury Regulation section 1.1502-13(e)(3), the taxpayer members will be treated as having made a similar election for West Virginia purposes, unless an election to the contrary is made for West Virginia purposes. A separate West Virginia election must be made by the taxpayer members to prevent the federal election from applying for West Virginia purposes. The election shall be subject to the approval of the Tax Commissioner, and approval or disapproval of such an election is within the sole discretion of the Tax Commissioner. A taxpayer which is qualified to request federal consent to treat intercompany transactions on a separate entity basis under Treasury Regulation section 1.1502-13(e)(3), but does not so request or is not granted consent by the Internal Revenue Service, may not elect such treatment for West Virginia purposes.

13d.5.b.2. If the members of the combined reporting group properly report transactions on a separate entity basis for federal or foreign national tax purposes and paragraph **13d.5.b.1.** does not apply, the taxpayer members may elect to treat those transactions on a separate entity basis for West Virginia purposes. The election shall be subject to the approval of the Tax Commissioner, and approval or disapproval of such an election is within the sole discretion of the Tax Commissioner. The election may be made for all items, or for items from a class or classes of transactions. For example, intercompany sales of inventory to a controlled foreign corporation included in a water's-edge combined reporting group pursuant to West Virginia Code §11-24-13f may be considered a class of transactions for which a separate state election may be made.

13d.5.b.3. Elections described by subdivision **13d.5.b.** are made by reporting the intercompany transactions in the manner required by the election on a timely filed original tax return (not an amended return) for the first year to which the election is to apply. An election under this subsection shall be treated as an accounting method, and shall be effective for all intercompany transactions occurring in the year to which the election is first applied, and for each year thereafter. The election shall be subject to the approval of the Tax Commissioner, and approval or disapproval of such an election is within the sole discretion of the Tax Commissioner.

13d.5.b.4. An election made under subdivision **13d.5.b.** does not apply for purposes of taking into account:

13d.5.b.4.A. losses and deductions deferred under section 267(f) of the Internal Revenue Code, or

13d.5.b.4.B. items from intercompany transactions with respect to stock or obligations of members.

13d.6. Stock of members.

13d.6.a. Unless otherwise provided, this section 13d applies the provisions of Treasury Regulation section 1.1502-13(f) relating to stock of members; however, the provisions of subsection (f)(6) of that section shall not apply.

13d.6.a.1. Exception for distributee member. Treasury Regulation section 1.1502-13(f)(2)(ii) shall not apply to exclude intercompany distributions from the gross income of the distributee member. Intercompany dividend distributions described by section 301(c)(1) of the Internal Revenue Code are included in the income of the distributee member unless subject to elimination or deduction under other applicable federal law or West Virginia law. The treatment of intercompany distributions described by section 301(c)(3) of the Internal Revenue Code is provided by paragraph **13d.6.a.2.**

13d.6.a.2. Deferred intercompany stock account (DISA). That portion of an intercompany distribution which exceeds West Virginia earnings and profits and P's basis in S's stock (the portion of a distribution described by section 301(c)(3) of the Internal Revenue Code) will create a DISA. In this subsection, P is treated like the Buyer (B) for purposes of calculating corresponding and recomputed items.

The DISA will be treated as deferred income. To the extent of a sale, liquidation or any other disposition of shares of the stock, the balance of the DISA with respect to such shares will be taken into account as income or gain to P even if S and P remain members of the same combined reporting group. The disposition shall be treated as a sale or exchange for purposes of determining the character of the DISA income or gain. The DISA is held by the distributee.

13d.6.a.2.A. A disposition of all the shares shall be deemed to have occurred if either S or P becomes a non-member of the combined reporting group or if the stock of S becomes worthless.

13d.6.a.2.B. Because P's DISA is deferred income and not negative basis, the DISA is taken into account upon liquidation, including complete liquidation into the parent. The deferred income restored as a result of the liquidation will be taken into account ratably over 60 months unless the taxpayer elects to take the income into account in full in the year of liquidation. For example, if S liquidates and the exchange of P's S stock is subject to section 332 of the Internal Revenue Code, P's DISA income taken into account under paragraph **13d.6.a.2.** is recognized over 60 months, unless an election is made to recognize the deferred income in the year of liquidation. Nonrecognition or deferral shall not apply to DISA income or gain taken into account as a result of an event described in subparagraph **13d.6.a.2.A.**

13d.6.a.2.C. If P transfers the stock of S to another member of the combined reporting group, P's DISA income will be an intercompany item and deferred under the provisions of this section 13d.

13d.6.b. Examples. The application of this section to intercompany transactions with respect to stock of members is illustrated by the following examples.

Example 1: Dividend exclusion and property distribution.

(Refer to Treas. Reg. § 1.1502-13(f)(7), example 1.)

Facts. S owns land that is used in the trade or business of the combined reporting group with a $ 70 basis and $ 100 value. On January 1 of Year 1, P's basis in S's stock is $ 100, and S has accumulated earnings and profits of $ 500 from prior years' combined reports of S and P.

During Year 1, S declares and makes a dividend distribution of the land to P. P also uses the land in the unitary business. Under section 311(b) of the Internal Revenue Code, S has a $ 30 gain. Under section 301(d) of the Internal Revenue Code, P's basis in the land is $ 100. West Virginia law generally conforms to Internal Revenue Code sections 301-385. On July 1 of Year 3, P sells the land to Y for $ 110.

Dividend treatment. S's distribution of the land is an intercompany distribution to P in the amount of $ 100. Because the distribution is paid out of earnings and profits of S, which have been included in a combined report of S and P, it will be eliminated from P's income pursuant to West Virginia Code §11-24-13d. The payment of the dividend has no effect on P's basis in the stock of S.

Matching rule. Under the matching rule (treating P as the buying member and S as the selling member), S takes its $ 30 intercompany gain into account in Year 3 to reflect the $ 30 difference between P's $ 10 corresponding gain ($ 110-$ 100 basis in the land) and the $ 40 recomputed gain ($ 110-$ 70 basis that the land would have had if S and P were divisions).

Apportionment. The intercompany distribution is not reflected in the sales factor in Year 1. In Year 3, unless otherwise excluded, the $ 110 gross receipts from P's sale of the land will be included in P's sales factor. After the distribution in Year 1, the land will be included in P's property factor at S's $ 70 original cost basis. Both S's $ 30 gain and P's $ 10 gain relative to the distributed land will be treated as current apportionable business income in Year 3.

Example 2: Dividends paid from pre-unitary earnings and profits.

Facts. The facts are the same as in Example 1 except that S's earnings and profits from prior combined reports of S and P is only $ 10. S also has $ 490 of earnings and profits that arose in years before a unitary relationship existed between S and P.

Dividend treatment. Because only $ 10 of S's distribution was paid from earnings and profits attributable to business income included in a combined report of S and P, only $ 10 is eliminated under West Virginia Code §11-24-13d. The remaining $ 90 of the dividend will be taken into account by P in Year 1, subject to any applicable deductions under West Virginia Code §11-24-1 *et seq.*

Matching rule. P's corresponding item is not its dividend income, but its income, gain, deduction or loss from the property acquired in the intercompany distribution. Therefore, none of S's intercompany gain will be taken into account in Year 1. As in Example 1, S will take its $ 30 intercompany gain into account in Year 3 to reflect the $ 30 difference between P's $ 10 corresponding gain and the $ 40 recomputed gain.

Apportionment. The apportionment results are the same as in Example 1, except that to the extent that the Year 1 dividend is not eliminated under West Virginia Code §11-24-13d or deducted for purposes of West Virginia Code §11-24-1 *et seq.*, P's dividend income will be treated as current apportionable business income in Year 1. The intercompany distribution is not included in the sales factor in Year 1.

Example 3: Deferred intercompany stock accounts.

(Refer to Treas. Reg. § 1.1502-13(f)(7), example 2.)

Facts. S owns all of T's stock with a $ 10 basis and $ 100 value. S has substantial earnings and profits which are attributable to business income included in a combined report of S, T and P. T has $ 10 of accumulated earnings and profits, all of which are attributable to business income included in a combined report of S, T and P. On January 1 of Year 1, S declares and distributes a dividend of all of the T stock to P. Under section 311(b) of the Internal Revenue Code, S has a $ 90 gain. Under section 301(d) of the Internal Revenue Code, P's basis in the T stock is $ 100. During Year 3, T borrows $ 90 from an unrelated party and declares and makes a $ 90 distribution to P to which section 301 of the Internal Revenue Code applies. During Year 6, T has $ 5 of current earnings which is attributable to business income included in the combined report of S, T and P. On December 1 of Year 9, T issues additional stock to Y and, as a result, T becomes a nonmember.

Dividend elimination. P's $ 100 of dividend income from S's distribution of the T stock, and its $ 10 dividend income from T's $ 90 distribution, are eliminated from income under West Virginia Code §11-24-13d.

Matching and acceleration rules. P has no deferred intercompany stock account (DISA) with respect to T stock because T's $ 90 distribution did not exceed T's $ 10 of earnings and profits and $ 100 stock basis. Therefore, P's corresponding item in Year 9 when T becomes a nonmember is $ 0. Treating S and P as divisions of a single corporation, the T stock would continue to have a $ 10 basis after the distribution from S to P. T's $ 90 distribution in Year 3 would first reduce T's $ 10 earnings and profits to zero, then reduce the $ 10 recomputed basis in T stock to zero and create a $ 70 recomputed DISA. T's $ 5 of earnings in Year 6 does not affect the amount of the DISA. Because the recomputed DISA would be taken into account upon T becoming a nonmember in Year 9, P will have a $ 70 recomputed corresponding item. Under the matching rule, S takes $ 70 of its intercompany gain into account in Year 9 to reflect the difference between P's $ 0 corresponding gain and the $ 70 recomputed gain. S's

remaining $ 20 of gain will be taken into account under the matching and acceleration rules based on subsequent events (for example, under the matching rule if P subsequently sells its T stock, or under the acceleration rule if S becomes a nonmember or if the stock of T becomes a nonbusiness asset.)

Apportionment. Neither the distributions in Years 1 and 3, nor T becoming a nonmember in Year 9, have any effect on the sales factor. S's $ 70 intercompany gain will be treated as current apportionable business income in Year 9.

Example 4: Deferred intercompany stock accounts, reverse sequence.

(Refer to Treas. Reg. § 1.1502-13(f)(7), example 2(d).)

Facts. The facts are the same as in Example 3, except that T borrows the $ 90 and makes its $ 90 distribution to S before S distributes T's stock to P. To the extent of T's $ 10 earnings and profits, T's distribution to S is a dividend and is eliminated under section 25106 of the Revenue and Taxation Code. The remaining distribution reduces S's $ 10 basis in T stock to $ 0, and creates a $ 70 DISA. The fair market value of T's stock after T incurs the $ 90 debt and distributes the proceeds is $ 10. Under section 311(b) of the Internal Revenue Code and the provisions of this section 13d, S has an $ 80 gain from the distribution of T stock to P ($ 10 value less $ 0 basis, plus $ 70 DISA recaptured). Under section 301(d) of the Internal Revenue Code, P's initial basis in the T stock is the $ 10 fair market value of the stock. T's $ 5 of earnings in Year 6 has no effect on P's basis in the T stock.

Matching and acceleration rule. P's corresponding item in Year 9, when T becomes a nonmember, is $ 0. Treating S and P as divisions of a single corporation, the T stock would continue to have a $ 0 basis after the distribution from S to P, and a $ 70 balance would remain in the DISA. When T becomes a nonmember in Year 9, P must include the amount of its DISA in recomputed income, and therefore has a $ 70 recomputed corresponding item. Under the matching rule, S takes $ 70 of its intercompany gain into account in Year 9 to reflect the difference between P's $ 0 corresponding gain and the $ 70 recomputed gain. S's remaining $ 10 of gain will be taken into account under the matching and acceleration rules based on subsequent events.

Apportionment. Neither the distributions in Year 1 nor T becoming a nonmember in Year 9 have any effect on the sales factor. S's $ 70 intercompany gain taken into account in Year 9 is treated as current apportionable business income in Year 9.

Example 5: Partial stock sale.

(Refer to Treas. Reg. § 1.1502-13(f)(7), example 2(e).)

Facts. The facts are the same as in Example 3, except that P sells 10% of T's stock to Y on December 1 of Year 9 for $ 1.50 (rather than T issuing additional stock and becoming a nonmember). T's $ 90 distribution to P in Year 3 reduced T's $ 10 of

earnings and profits to $ 0, then reduced P's $ 100 basis in T stock to $ 20. Under the matching rule, S takes $ 9 of its gain into account in Year 9 to reflect the difference between P's $ .50 loss taken into account ($ 1.50 sale proceeds minus $ 2 basis) and the $ 8.50 recomputed gain ($ 1.50 sales proceeds minus $ 0 basis plus $ 7 recomputed DISA).

Apportionment. If not excluded pursuant to West Virginia Code §11-24-7(h), the $ 1.50 gross receipts from P's sale of the T stock to Y is included in P's sales factor in Year 9. Both S's $ 9 gain and P's $ .50 loss are treated as current apportionable business income in Year 9.

Example 6: Loss, rather than cash distribution.

(Refer to Treas. Reg. § 1.1502-13(f)(7), example 2(f).)

Facts. The facts are the same as in Example 3, except that T retains the loan proceeds and incurs a $ 90 operating loss in Year 3. The loss results in an earnings and profits deficit of $ 80 for T, but has no effect on P's basis in T's stock. Therefore, no DISA is created. T's $ 5 of earnings in Year 6 reduces its earnings and profits deficit to $ 75, but also has no effect on the stock basis. Because there is no DISA balance to take into account when T becomes a nonmember in Year 9, P's corresponding item and the recomputed item are both $ 0. Consequently, S's entire $ 90 intercompany gain continues to be deferred pending subsequent events.

Example 7: Intercompany reorganization.

(Refer to Treas. Reg. § 1.1502-13(f)(7), example 3.)

Facts. P forms S and B by contributing $ 200 to the capital of each. During Years 1 through 4, S and B each accumulate earnings and profits of $ 50, which is attributable to business income included in the combined reports of S, B and P. On January 1 of Year 5, the fair market value of S's assets and its stock is $ 500, and S merges into B in a tax-free reorganization. Pursuant to the plan of reorganization, P receives new B stock with a; fair market value of $ 350 and $ 150 cash.

Treatment as a distribution under section 301 of the Internal Revenue Code. Under Treasury Regulation section 1.1502-13(f)(3), P is treated as receiving additional B stock with a fair market value of $ 500. Under section 358 of the Internal Revenue Code, P's basis of the additional B stock is $ 200 (P's basis in the relinquished S stock). Immediately after the merger, $ 150 of the stock received is treated as redeemed, and the redemption is treated under section 302(d) of the Internal Revenue Code as a distribution to which section 301 applies. Under section 381(c)(2) of the Internal Revenue Code, B is treated as receiving S's $ 50 of earnings and profits in addition to its own $ 50 of earnings and profits. Therefore, $ 100 of the deemed distribution is treated as a dividend and is eliminated from income for West Virginia tax purposes. The remaining $ 50 of the distribution reduces P's basis in the B stock from $ 400 to $ 350.

Apportionment. The reorganization has no effect on the sales factor. After the reorganization, S's property will be reflected in B's property factor at S's original cost.

13d.7. Obligations of members.

13d.7.a. Unless otherwise provided, this section 13d will follow Treasury Regulation section 1.1502-13(g) relating to the obligations of members.

13d.7.b. Example: The application of this section to obligations of members is illustrated by the following example.

Example: Interest on intercompany debt.

(Refer to Treas. Reg. § 1.1502-13(g)(5), Example 1.)

Facts. On January 1 of Year 1, B borrows $ 100 from S in return for B's note providing for $ 10 of interest annually at the end of each year, and repayment of $ 100 at the end of Year 5. Under their separate entity methods of accounting, B accrues a $ 10 interest deduction annually, and S accrues $ 10 of interest income annually.

Matching rule. Under subdivision **13d.7.a.**, the accrual of interest on B's note is an intercompany transaction. Under the matching rule, S takes its $ 10 of income into account in each of Years 1 through 5 to reflect the $ 10 difference between B's $ 10 of interest expense taken into account and the $ 0 recomputed expense.

Interest offset. Neither S's intercompany interest income nor B's corresponding interest expense are taken into account for purposes of determining the interest offset or foreign investment interest offset under West Virginia Code §11-24-1 *et seq.*

Apportionment. S's interest income is not included in the sales factor in any of Years 1 through 5. The intercompany loan is excluded from S's property factor, even if S is required to include loan balances in its property factor for West Virginia tax purposes.

13d.8. Anti-avoidance rules. If a transaction is engaged in or structured with the principal purpose of avoiding the purposes of this section 13d (including, for example, avoiding treatment as an intercompany transaction, or manipulating the sourcing of income or the occurrence of acceleration events), adjustments may be made to carry out the purposes of this section 13d.

13d.9. Miscellaneous operating rules.

Except as otherwise provided, this section 13d applies the provisions of Treasury Regulation section 1.1502-13(j) relating to miscellaneous operating rules. However, the provisions of subsections (j)(5), (j)(6), and (j)(7) of Treasury Regulation section 1.1502-13 shall not apply for West Virginia tax purposes.

13d.9.a. Subgroups.

13d.9.a.1. If a change occurs in the composition of the combined reporting group, but both S and B either remain members of the same combined reporting group or leave the combined reporting group together and remain unitary with each other, such a change alone will not cause S's intercompany items to be taken into account under the acceleration rule contained in subsection 13d.4.

13d.9.a.2. If the event which causes the combined reporting group to change as described in paragraph **13d.9.a.1.** also causes S's intercompany items to be taken into account in a federal consolidated return, then S may make an irrevocable election to take those intercompany items into account in the same period for West Virginia purposes. The election is made by reporting the income, gain, deduction or loss on a timely filed original tax return. If this election is not made, then S and B must maintain sufficient records to track the intercompany gain or loss which has been taken into account for federal purposes but which remains deferred for state purposes. The election shall be subject to the approval of the Tax Commissioner, and approval or disapproval of such an election is within the sole discretion of the Tax Commissioner.

13d.9.a.3. Examples. The application of subdivision **13d.9.a.** can be illustrated by the following examples.

Example 1: S and B sold.

P is the principal corporation in a combined reporting group in which S and B are members. P sells S and B to Y, an unrelated entity. S and B remain unitary after the sale. The sale of S and B does not cause S's intercompany items to be taken into account under the acceleration rule. Therefore S's intercompany items will remain deferred until subsequent events cause those intercompany items to be taken into account under either the matching rule or the acceleration rule. However, if the sale of S and B caused S's intercompany items to be taken into account in the federal consolidated return, the taxpayer may elect the same treatment under paragraph **13d.9.a.2.** by taking the intercompany items into account on its timely filed original West Virginia return.

13d.9.b. Recognition of income from intercompany transactions occurring prior to entering the state.

13d.9.b.1. Intercompany transactions as defined in subdivision **13d.2.a.** shall include those transactions which occur prior to any member becoming taxable in this State if S and B would have been members of the same combined reporting group had any unitary member been taxable in this State in the year of the transaction.

13d.9.b.2. To the extent that intercompany transactions would have qualified for an election to be treated on a separate entity basis under subdivision **13d.5.b.** but

for the fact that no member of the combined reporting group was a West Virginia taxpayer in the year in which such an election would have been required to be made, a retroactive election under subdivision **13d.5.b.** will be deemed made. The deemed election shall apply to all intercompany transactions described by subdivision **13d.9.b.**

13d.9.b.3. Examples. The application of this section 13d to transactions occurring prior to entering the state can be illustrated by the following examples.

Example 1: Sale outside of group after member enters the state.

Facts. S and B are members of a unitary group which conduct all of their business activity in the U.S. Both are members of a federal consolidated return group. In Year 1, when no member of the group is a West Virginia taxpayer, S sells land with a basis of $ 100 to B for $ 110. S's $ 10 gain is treated as a deferred intercompany item in S and B's consolidated return. The land is used in the unitary business. In Year 2, a member of the unitary group becomes taxable in West Virginia. Prior to the member becoming taxable in this state, no event occurred which would have caused the intercompany item to be taken into account. In Year 3, B sells the land to Y for $ 130.

Matching rule. S's sale of the land to B is an intercompany transaction, and S's $ 10 gain is its intercompany item. S takes its intercompany gain into account in Year 3 to reflect the $ 10 difference between B's corresponding item of $ 20 from the sale to Y, and the recomputed corresponding item of $ 30 ($ 130-$ 100). This is the same result that would have occurred if S and B were unitary divisions of a single corporation and the transaction had been a transfer between divisions prior to the corporation becoming taxable within this state.

Apportionment. The land is included in B's property factor at S's $ 100 original cost basis. In Year 3, the $ 130 gross receipts from B's sale to Y, unless otherwise excluded by West Virginia Code §11-24-7(h), will be included in B's sales factor. S's gain will be treated as current apportionable business income in Year 3.

Example 2. Retroactive election under subdivision **13d.5.b.**

Facts. The facts are the same as in Example 1, except that S and B do not file a consolidated federal return. The Year 1 intercompany transaction between S and B is reported as a $ 10 gain on S's separate return for federal purposes. An election to treat intercompany transactions between S and B on a separate entity basis could have been made if any member of the unitary group was a West Virginia taxpayer in the year of the transaction. Therefore, a retroactive election is deemed made under this subsection in Year 3, which is the year that S's intercompany item would otherwise be taken into account.

Example 3. S leaves the combined reporting group after a member enters the state.

Facts. The facts are the same as in Example 1, except that instead of B selling the land, the stock of S is sold in Year 3 and S becomes a nonmember of the combined reporting group.

Acceleration rule. Once the stock of S is sold, the effect of treating the unitary operations of S and B as divisions of a single corporation cannot be achieved. Therefore, under the acceleration rule of subsection 13d.4, S's $ 10 gain is taken into account in Year 3 immediately before S becomes a nonmember.

Apportionment. The land will be included in B's property factor at S's $ 100 original cost basis until S's intercompany gain is accelerated. Immediately after S's gain is taken into account, the $ 100 value of the land in B's property factor will be increased to reflect B's $ 110 cost. S's intercompany gain will be treated as current apportionable business income in Year 3.

13d.9.c. Partially included water's-edge corporations.

13d.9.c.1. Coordination with West Virginia Code §11-24-13f.

13d.9.c.1.A. If S is a corporation partially included in a water's-edge combined reporting group, and S enters into a transaction with another member of the water's-edge combined reporting group, the transaction is an intercompany transaction if the resulting income, gain, deduction or loss would, but for the provisions of this section 13d, be included as apportionable business income in the water's-edge combined report under West Virginia Code §11-24-13f.

13d.9.c.1.B. Except as provided in subparagraph **13d.9.c.1.C.**, intercompany transactions include transactions where B is a corporation partially included in the combined reporting group immediately after such transaction pursuant to West Virginia Code §11-24-13f(4), but only to the extent that the object of the intercompany transaction gives rise to income, gain, deduction or loss which would be included as apportionable business income in the water's-edge combined report under West Virginia Code §11-24-13f(4).

13d.9.c.1.C. The sale, exchange or other transfer of stock of an affiliated corporation to a corporation partially included in the combined reporting group pursuant to West Virginia Code §11-24-13f(4) will not be treated as an intercompany transaction unless the stock is considered to be a United States real property interest as defined in section 897(c) of the Internal Revenue Code.

13d.9.c.1.D. Where either S or B was partially included in a water's-edge combined reporting group pursuant to West Virginia Code §11-24-13f(4), the intercompany item will be taken into account under the acceleration rule immediately before any income year in which either S or B has no includable income pursuant to West Virginia Code §11-24-13f(4) and is therefore excluded from the water's-edge combined reporting group. If, for any year, the includable income of S or B pursuant to

West Virginia Code §11-24-13f(4) is insubstantial, the Tax Commissioner may permit or require the intercompany item to be taken into account under the acceleration rule immediately before such year.

13d.9.c.1.E. Where B is partially included in a water's-edge combined reporting group pursuant to West Virginia Code §11-24-13f(4), the acceleration rule will apply to take an intercompany item into account to the extent the object of the intercompany transaction ceases to give rise to income, gain, loss, or deductions which would be included as apportionable business income in the water's-edge combined report under West Virginia Code §11-24-7(h). For example, if intangible property gives rise to income includible in the water's-edge combined report under West Virginia Code §11-24-7(h) while held by B, but a disposition of such property results in foreign-source gain or loss under sections 861 through 865 of the Internal Revenue Code which is not included in the water's-edge combined report, then the disposition will trigger application of the acceleration rule to take into account S's intercompany items with respect to such property.

13d.9.c.1.F. Where a sale, exchange or other transfer of stock to a corporation included in the water's-edge combined reporting group pursuant to section West Virginia Code §11-24-13f(a)(4) has been treated as an intercompany transaction under subparagraph **13d.9.c.1.C.**, the acceleration rule will apply to take into account intercompany items arising from that intercompany transaction if the stock ceases to be a United States real property interest as defined in section 897(c) of the Internal Revenue Code.

13d.9.c.2. Coordination with section West Virginia Code §11-24-13f(a)(5) of the Revenue and Taxation Code.

13d.9.c.2.A. Definition. For purposes of this section 13d, the term "partial inclusion ratio" means a fraction not to exceed one, the numerator of which is the "Subpart F income, as defined in section 952 of the Internal Revenue Code " of that corporation for that taxable year and the denominator of which is the "earnings and profits," as defined in Section 964 of the Internal Revenue Code of that corporation for that taxable year. The partial inclusion ratio shall be used for determining the includable amount of income and apportionment factors for a partially included corporation described in West Virginia Code §11-24-13f(a)(5).

13d.9.c.2.B. A transaction between a corporation included in a water's-edge combined reporting group pursuant to West Virginia Code §11-24-13f(a)(5)and another member of the combined reporting group will be an intercompany transaction to the extent of that corporation's partial inclusion ratio for the income year.

13d.9.c.2.C. If both S and B are corporations included in a water's-edge combined reporting group pursuant to West Virginia Code §11-24-13f(a)(5), the partial inclusion ratios of both S and B must be applied to determine the portion of the transaction that will be treated as an intercompany transaction.

13d.9.c.2.D. Where either S or B is included in a water's-edge combined reporting group pursuant to West Virginia Code §11-24-13f(a)(5), the intercompany item will be taken into account under the acceleration rule immediately before the first income year in which the partial inclusion ratio for either S or B is an amount equal to or lower than 50% of its partial inclusion ratio for the year of the intercompany transaction. Regardless of whether the ratio decreases 50% or more below the intercompany transaction year partial inclusion ratio, the acceleration rule will apply to take the intercompany item into account if the partial inclusion ratio is less than 10%.

13d.9.c.2.E. If subparagraph **13d.9.c.2.D.** applies, then, as an alternative to the application of the acceleration rule provided by that subparagraph, the taxpayer may elect to have the acceleration rule apply to take into account only a proportionate share of the intercompany item relative to the amount of the decrease in the partial inclusion ratio. If further decreases in the partial inclusion ratio occur in subsequent years, additional portions of the intercompany item shall be taken into account under the acceleration rule in proportion to such decreases. However, if in any income year the partial inclusion ratio is below 10%, any remaining intercompany items shall be taken into account and the election provided by this subparagraph shall not apply. The election shall be made by reporting the proportionate share of the intercompany item on a timely filed original tax return for the first year in which the partial inclusion ratio decreases 50% or more below the intercompany transaction year partial inclusion ratio. As a condition of this election, the taxpayer must maintain books and records sufficient to identify the amounts of intercompany items, the annual partial inclusion ratios, and the application of this provision to the intercompany items.

13d.9.c.2.F. Where both S and B are included in a water's-edge combined reporting group pursuant to West Virginia Code §11-24-13f(a)(5), and the partial inclusion ratios of both S and B decrease 50% or more below their respective intercompany transaction year partial inclusion ratios, the acceleration methodology of subparagraph **13d.9.c.2.E.** shall be applied in proportion to the greater of either (1) the amount of decrease attributable to S or (2) the amount of decrease attributable to B.

13d.9.c.3. Separate entity election for transactions with partially included entities. See paragraph **13d.5.b.2.** for application of the election to treat transactions on a separate entity basis with respect to transactions with partially included entities.

13d.9.c.4. Examples. The application of this subdivision **13d.9.c.** to partially included entities in a water's-edge combined report is illustrated by the following examples.

Example 1: Intercompany sale of land by an entity included pursuant to West Virginia Code §11-24-13f(a)(4).

Facts. S is a foreign corporation with U.S. branches that are included in a water's-edge combined reporting group pursuant to West Virginia Code §11-24-13f(a)(4). S has

a basis of $ 70 in land which it uses in its U.S. trade or business operations. On January 1 of Year 1, S sells the land to domestic corporation B for $ 100. On July 1 of Year 3, B sells the land to Y for $ 110.

Matching rule. But for the provisions of this section 13d, S's $ 30 gain from the sale to B would be treated as U.S. source income and included in the water's-edge combined report under West Virginia Code §11-24-13f. However, the transaction is an intercompany transaction and S's $ 30 gain is an intercompany item. S takes its intercompany item into account under the matching rule in Year 3 to reflect the $ 30 difference for the year between B's corresponding item of $ 10 and the recomputed corresponding item of $ 40.

Apportionment. To produce the result that would occur if S and B were unitary divisions of a single corporation, the intercompany sale of land will not be reflected in the sales factor in Year 1. In Year 3, unless otherwise excluded, the $ 110 gross receipts from B's sale will be included in B's sales factor. The land is attributable to B after the sale, and it will be reflected in B's property factor at S's $ 70 original cost basis until it is sold outside the water's-edge combined reporting group in Year 3. Both S's $ 30 gain and B's $ 10 gain will be treated as current apportionable business income in Year 3.

Example 2: Intercompany transaction where buyer is an entity included pursuant to West Virginia Code §11-24-13f(a)(4).

Facts. B is a foreign corporation with a U.S. branch which is included in a water's-edge combined reporting group pursuant to West Virginia Code §11-24-13f(a)(4). In Year 1, domestic corporation S incurs expenses of $ 300 to provide engineering services to B in connection with the renovation of B's U.S. facility. B capitalizes the $ 500 fee which it pays to S for the services and computes depreciation on that basis. If S and B were divisions of a single corporation, only the $ 300 in expenses would be capitalized, which would result in smaller depreciation deductions.

Matching Rule. Because the engineering services are attributable to a facility used in the operation of U.S. business activities which give rise to income, gain, deduction or loss included in the combined report under West Virginia Code §11-24-13f, the performance of those services is treated as an intercompany transaction. S has intercompany income of $ 200 ($ 500 receipts less $ 300 expenses). S's intercompany income will be taken into account in subsequent years based upon the difference between B's corresponding depreciation (based on a $ 500 basis) and the depreciation recomputed as though S and B were divisions of a single corporation (based on a $ 300 basis).

Apportionment. As would be the case if the services were performed between unitary divisions of a single corporation, the transaction will not be reflected in the sales factor. If S's expenses with respect to the engineering services include payroll expenses, those expenses would be included in S's payroll factor in Year 1. When the

renovated facility is placed into service in the unitary business, the $ 300 capitalized cost of the engineering services will be included in B's property factor. In each subsequent year, S's intercompany income taken into account and B's corresponding depreciation deduction will be treated as current apportionable business income for that year.

Example 3: Transaction not related to U.S. activities.

Facts. Assume the same facts as in Example 2, except that the engineering services relate to the construction of a plant in Brazil.

Matching rule. Although B is partially included in the water's-edge combined reporting group under West Virginia Code §11-24-13f(a)(4), the engineering services do not relate to an asset which will give rise to income, gain, deduction or loss which will be included in the water's-edge combined report under West Virginia Code §11-24-13f. Therefore, the performance of services is not treated as an intercompany transaction. S's income of $ 500 and expenses of $ 300 are taken into account in Year 1.

Apportionment. Gross receipts of $ 500 are included in S's sales factor.

Example 3a: Transaction allocated between U.S. activities and foreign activities.

Facts. Assume the same facts as in Example 2, except that the engineering services relate to the construction of two plants, one in the U.S. and one in Brazil. S's expenses with respect to the engineering services are allocated 55% to the U.S. activities under the rules in Treasury Regulation section 1.861. Therefore, 55% of the transaction will be treated as an intercompany transaction.

Matching Rule. S has intercompany income of $ 110 ($ 500 receipts less $ 300 expenses, multiplied by 55%). S's intercompany income will be taken into account in subsequent years based upon the difference between B's corresponding depreciation deduction and the depreciation deduction recomputed as though S and B were divisions of a single corporation.

Apportionment. Because 45% of the transaction is not treated as an intercompany transaction, S's $ 90 of non-intercompany income ([$ 500-$ 300] x 45%) will be treated as current apportionable business income in Year 1. Likewise, receipts from engineering services of $ 225 ($ 500 x 45%) will be included in S's sales factor in Year 1. The capitalized cost of the engineering services allocated to the U.S. plant is $ 165 ($ 300 total cost x 55%). When the U.S. plant is placed into service in the unitary business, the $ 165 capitalized cost will be included in B's property factor. In each subsequent year, S's intercompany income taken into account and B's corresponding depreciation deduction will be treated as current apportionable business income for that year.

Example 4: Asset ceases to give rise to U.S. source income.

Facts. Assume the same facts as in Example 2, except that the engineering services relate to the design of specialized equipment which is placed in service in B's U.S. facility by the end of Year 1. On December 31 of Year 4, the equipment is shipped to Germany for use in another plant owned and operated by B.

Matching rule. S has intercompany income of $ 200 (see computations in Example 2), a portion of which is taken into account in Years 2 through 4 to reflect the difference between B's corresponding depreciation deduction and the depreciation recomputed as though S and B were divisions of a single corporation.

Acceleration rule. In Year 4, the equipment ceases to give rise to income, gain, loss or deductions included in the water's-edge combined report under West Virginia Code §11-24-13f. Under the acceleration rule and subparagraph **13d.9.c.1.E.**, S's remaining intercompany income is taken into account in Year 4.

Apportionment. The apportionment results of the transactions in Years 1 through 4 are the same as in Example 2. Because no gross receipts related to the transaction are generated in Year 4, the accelerated income is not reflected in the sales factor.

Example 5. Both Seller and Buyer partially included under West Virginia Code §11-24-13f(a)(4).

S and B are both foreign corporations with U.S. branches that are included in a water's-edge combined reporting group pursuant to West Virginia Code §11-24-13f(a)(4). S sells equipment which it uses in its U.S. trade or business operations to B for a gain. Thereafter, the equipment is used in B's U.S. trade or business operations. Except for the provisions of this section 13d, S's gain from the sale of equipment would be treated as U.S. source income and included in the water's-edge combined report under West Virginia Code §11-24-13f. B's use of the equipment gives rise to income, gain, deduction or loss which will be included in the water's-edge combined report under West Virginia Code §11-24-13f. Therefore, because the requirements of subparagraph **13d.9.c.1.A.** and **13d.9.c.1.B.** are both satisfied, S's sale of the equipment to B is treated as an intercompany transaction and subject to the provisions of this section 13d.

Example 6. Seller excluded from the water's-edge combined reporting group.

Facts. S is a foreign corporation which owns 100% of the stock of affiliated domestic corporations B and RP. RP is a United States Real Property Holding Corporation as defined in section 897(c) of the Internal Revenue Code. In Year 1, S has no income from U.S. activities, and is excluded from the water's-edge combined reporting group of B and RP.

In Year 2, S sells its stock in RP to B for a gain of $ 1,000. Because S's sale of RP is treated as a disposition of a United States real property interest as defined by section 897 of the Internal Revenue Code, S's income and apportionment factors attributable to that sale would, but for the provisions of this section 13d, be included in the water's-

edge combined report in Year 2. Therefore, the transaction is treated as an intercompany transaction. S's intercompany item is its $ 1,000 gain.

In Year 3, S has no income from U.S. activities, and is again excluded from the water's-edge combined reporting group of B and RP.

Acceleration Rule. The effect of treating the operations of S and B as divisions of a single corporation cannot be achieved once S is excluded from the water's-edge combined reporting group. Therefore, under the acceleration rule, S's $ 1,000 intercompany; gain is taken into account in Year 2 (immediately before the income year in which S is excluded from the combined reporting group).

Apportionment. Neither the intercompany sale of RP stock nor the acceleration of the intercompany gain is reflected in the sales factor in Year 2. S's accelerated gain will be treated as current apportionable business income in Year 2.

Example 7: Seller included under West Virginia Code §11-24-13f(a)(5).

Facts. Corporation S is a controlled foreign corporation as defined in section 957 of the Internal Revenue Code, and is included in the water's-edge combined reporting group under West Virginia Code §11-24-13f(a)(5) to the extent of its partial inclusion ratio. In Year 1, S sells land with a basis of $ 500 to domestic corporation B for $ 600. S's partial inclusion ratio for Year 1 is 66%. In Year 5, when S's partial inclusion ratio is 75%, B sells the land to Y for $ 650. At no time in Years 2 through 4 did S's partial inclusion ratio fall to 33% or lower (50% of the Year 1 ratio; see subparagraph **13d.9.c.2.D.**).

Matching rule. $ 66 of S's $ 100 gain is an intercompany item and is deferred ($ 100 x 66%). The remaining $ 34 of S's gain is not included in the water's-edge combined report. In Year 5, B has a corresponding gain of $ 50 ($ 650-$ 600). For purposes of calculating the recomputed gain, S's original cost of $ 500 is increased by the amount of S's $ 34 non-intercompany gain. Therefore, the recomputed gain would be $ 116 ($ 650-$ 534). S's $ 66 intercompany gain is taken into account in the water's-edge combined report in Year 5 to reflect the $ 66 difference between B's $ 50 corresponding gain and the $ 116 recomputed gain.

Apportionment. Gross receipts of $ 396 from S's sale to B are included in the water's-edge combined report ($ 600 x 66%). If S and B were divisions of a single corporation, the transaction would not be reflected in the sales factor. Therefore, the $ 396 intercompany gross receipts shall be eliminated from S's sales factor under paragraph **13d.1.e.1.** For purposes of B's property factor, the land will be reflected at S's cost basis under subparagraph **13d.1.e.2.A.**, adjusted by any gain or loss recognized by S as a result of the non-intercompany portion of the transaction. The net value assigned to the land in B's property factor will be $ 534 ($ 500 cost basis to S + $ 34 non-intercompany gain).

Example 8: Buyer included under West Virginia Code §11-24-13f(a)(5).

Facts. On December 31 of Year 1, domestic corporation S sells land with a basis of $ 500 to corporation B for $ 600. Corporation B is a controlled foreign corporation as defined in section 957 of the Internal Revenue Code, and is included in the water's-edge combined reporting group under West Virginia Code §11-24-13f(a)(5) to the extent of its partial inclusion ratio. B's partial inclusion ratio for Year 1 is 66%. On December 31 of Year 5, when B's partial inclusion ratio is 75%, B sells the land to Y for $ 650. At no time in Years 2 through 4 did B's partial inclusion ratio fall to 33% or lower (50% of the Year 1 ratio).

Matching rule. $ 66 of S's $ 100 gain ($ 100 x 66%) is an intercompany item and is deferred. S's remaining $ 34 gain is taken into account currently in Year 1. In Year 5, B has a corresponding gain of $ 50 ($ 650-$ 600). For purposes of calculating the recomputed gain, S's original cost of $ 500 is increased by the amount of the $ 34 non-intercompany gain taken into account by S. Therefore, the recomputed gain would be $ 116 ($ 650-$ 534). S's $ 66 intercompany gain is taken into account in the water's-edge combined report in Year 5 to reflect the $ 66 difference between B's $ 50 corresponding gain and the $ 116 recomputed gain.

Apportionment. Unless otherwise excluded, S's sales factor in Year 1 will reflect gross receipts of $ 204 from the non-intercompany portion of the sale to B. The remaining $ 396 ($ 600 sales price x 66%) will be eliminated from S's sales factor under paragraph **13d.1.e.1.** The valuation of the land for purposes of B's property factor is S's cost basis adjusted by any gain or loss recognized by S as a result of the non-intercompany portion of the transaction. The net value assigned to the land will be $ 534 ($ 500 cost basis to S + $ 34 non-intercompany gain). The $ 534 valuation will be included in B's property factor to the extent of B's partial inclusion ratio for that year. For example, if B's partial inclusion ratio was 50% in Year 2, the land would be reflected in B's property factor for Year 2 at $ 267 ($ 534 x 50%). In Year 5, unless otherwise excluded, $ 487.50 gross receipts from B's sale of the land to Y will be reflected in B's sales factor ($ 650 sales price to Y x 75% Year 5 partial inclusion ratio).

Example 9: Both Seller and Buyer included under West Virginia Code §11-24-13f(a)(5).

Facts. Assume the same facts as in Example 8, except that S is also a controlled foreign corporation as defined in section 957 of the Internal Revenue Code, and is included in the water's-edge combined reporting group under West Virginia Code §11-24-13f(a)(5) to the extent of its partial inclusion ratio. S's partial inclusion ratio for Year 1 is 80%. On December 31 of Year 5, when S's partial inclusion ratio is 60%, B sells the land to Y for $ 650. At no time in Years 2 through 4 did S's partial inclusion ratio fall to 40% or lower (50% of S's 80% Year 1 ratio).

Matching rule. $ 52.80 of S's $ 100 gain ($ 100 x S's 80% Year 1 ratio x B's 66% Year 1 ratio) is an intercompany item and is deferred. Of S's remaining $ 47.20 non-

intercompany gain, $ 27.20 is currently taken into account in Year 1 ($ 100 total gain x S's 80% Year 1 ratio = $ 80 of total gain includable in water's-edge combined report; less $ 52.80 deferred intercompany portion); $ 20 of non-intercompany gain is not included in the water's-edge combined report. In Year 5, B has a corresponding gain of $ 50 ($ 650-$ 600). For purposes of calculating the recomputed gain, S's original cost of $ 500 is increased by the amount of S's $ 47.20 non-intercompany gain. Therefore, the recomputed gain would be $ 102.80 ($ 650 sales price - $ 547.20 recomputed basis). S's $ 52.80 intercompany gain is taken into account in the water's-edge combined report in Year 5 to reflect the $ 52.80 difference between B's $ 50 corresponding gain and the $ 102.80 recomputed gain.

Apportionment. Gross receipts of $ 480 from S's sale to B ($ 600 x S's 80% Year 1 ratio) are included in the water's-edge combined report. Of that amount, $ 316.80 ($ 480 x B's 66% Year 1 ratio) is attributable to the intercompany transaction and will be eliminated from S's sales factor under paragraph **13d.1.e.1.** Unless otherwise excluded, S's sales factor will continue to reflect the remaining gross receipts of $ 163.20. In Year 5, unless otherwise excluded, $ 487.50 gross receipts from B's sale of the land to Y ($ 650 x B's 75% Year 5 ratio) will be reflected in B's sales factor.

The valuation of the land for purposes of B's property factor is S's cost basis in the land adjusted by any gain or loss recognized by S as a result of the non-intercompany portion of the transaction. The net value assigned to the land will be $ 547.20 ($ 500 cost basis to S + $ 47.20 non-intercompany gain). The $ 547.20 valuation will be included in B's property factor to the extent of B's partial inclusion ratio for that year. For example, if B's partial inclusion ratio was 50% in Year 2, the land would be reflected in B's property factor for Year 2 at $ 273.60 ($ 547.20 x 50%).

Example 10: Intercompany transaction between Seller included under West Virginia Code §11-24-13f(a)(4) and Buyer included under West Virginia Code §11-24-13f(a)(5).

Facts. S is a foreign corporation with a U.S. branch which is included in the water's-edge combined reporting group under West Virginia Code §11-24-13f(a)(4). B is a controlled foreign corporation as defined in section 957 of the Internal Revenue Code, and is included in the water's-edge combined reporting group under West Virginia Code §11-24-13f(a)(5) to the extent of its partial inclusion ratio. In Year 1, S sells land with a basis of $ 800 which it used in its U.S. trade or business activities to B for $ 1,000. B's partial inclusion ratio in Year 1 is 60%. In Year 4, when B's partial inclusion ratio is 65%, B sells the land to Y for $ 1,100. At no time in Years 2 or 3 did B's partial inclusion ratio fall to 30% or lower (50% of B's 60% Year 1 ratio).

Matching rule. Except for the provisions of this section 13d, S's $ 200 gain from the sale to B would be treated as U.S. source income and included in the water's-edge combined report; therefore, the requirements of subparagraph **13d.9.c.1.A.** are satisfied. $ 120 of S's gain ($ 200 total gain x B's 60% partial inclusion ratio) is an intercompany item and is deferred. S's remaining $ 80 non-intercompany gain is taken into account in the water's-edge combined report in Year 1. In Year 4, B has a

corresponding gain of $ 100 ($ 1,100-$ 1,000). For purposes of calculating the recomputed gain, S's original cost of $ 800 is increased by the amount of the $ 80 non-intercompany gain taken into account by S. Therefore, the recomputed gain would be $ 220 ($ 1,100 sales price - $ 880 recomputed basis). S's $ 120 intercompany gain is taken into account in the water's-edge combined report in Year 4 to reflect the $ 120 difference between B's $ 100 corresponding gain and the $ 220 recomputed gain.

Apportionment. Unless otherwise excluded, S's sales factor in Year 1 will reflect gross receipts of $ 400 from the non-intercompany portion of the sale to B. The remaining $ 600 ($ 1,000 sale price x 60%) will be eliminated from S's sales factor under paragraph **13d.1.e.1.** The valuation of the land for purposes of B's property factor is S's cost basis adjusted by any gain or loss recognized by S as a result of the non-intercompany portion of the transaction. The net value assigned to the land will be $ 880 ($ 800 cost basis to S + $ 80 non-intercompany gain). The $ 880 valuation will be included in B's property factor to the extent of B's partial inclusion ratio for that year. For example, if B's partial inclusion ratio was 55% in Year 2, the land would be reflected in B's property factor for Year 2 at $ 484 ($ 880 x 55%). In Year 4, unless otherwise excluded, $ 715 gross receipts from B's sale of the land to Y ($ 1,100 sales price to Y x B's 65% Year 4 partial inclusion ratio) will be reflected in B's sales factor.

Example 11: Depreciable asset sold to buyer partially included under West Virginia Code §11-24-13f(a)(5).

Facts. On January 1 of Year 1, domestic corporation S buys equipment with a 10-year useful life for $ 100 and begins to depreciate it using the straightline method. On January 1 of Year 6, S sells the equipment to B for $ 60. B is a controlled foreign corporation partially included in the combined reporting group under West Virginia Code §11-24-13f(a)(5). B's partial inclusion ratio is 40% in Year 6. B determines that the useful life of the equipment is 5 years from the date it was acquired by B.

Depreciation through Year 5, intercompany gain in Year 6. S claims $ 10 of depreciation for each of Years 1 through 5, and has a $ 50 basis at the time of the sale to B. Thus, S has a $ 10 gain from its $ 60 sale to B in Year 6. $ 4 of S's gain is an intercompany gain ($ 10 gain x B's 40% partial inclusion ratio) and is deferred. S's remaining $ 6 non-intercompany gain is taken into account currently in Year 6.

Matching rule. In each of Years 6 through 10, B's corresponding item is its $ 12 depreciation deduction ($ 60 basis / 5-year life). If S and B were divisions of a single corporation, the recomputed depreciation deduction would be the $ 10 annual depreciation for Years 6 through 10 based on S's $ 100 basis, plus an additional $ 1.20 of depreciation attributable to the $ 6 increase in basis resulting from S's non-intercompany gain ($ 6 non-intercompany gain / 5-year remaining life). Thus, in each of Years 6 through 10, S will take $ .80 of its intercompany gain into account to reflect the difference between B's $ 12 corresponding depreciation and the $ 11.20 recomputed depreciation.

Apportionment. Unless otherwise excluded, S's sales factor in Year 6 will reflect gross receipts of $ 36 from the non-intercompany portion of the sale to B. The remaining $ 24 ($ 60 x B's 40% partial inclusion ratio) will be eliminated from S's sales factor under paragraph **13d.1.e.1.** The valuation of the equipment for purposes of B's property factor is S's cost basis of $ 100. (Because S's $ 10 total gain from the sale to B does not exceed the depreciation already deducted by S with respect to the equipment, the basis is not adjusted by the non-intercompany gain. If the total gain had exceeded the amount of depreciation already deducted by S, then the valuation of the property in B's property factor would be increased by the 60% non-intercompany portion of the excess gain.) The $ 100 valuation will be included in B's property factor in each year to the extent of B's partial inclusion ratio for that year. For example, the equipment would be reflected in B's property factor in Year 6 at $ 60 ($ 100 x 60%). In each of Years 6 through 10, S's $ .80 intercompany gain will be treated as current apportionable business income. B's $ 12 depreciation deduction will be included in combined report business income in each year to the extent of B's partial inclusion ratio for that year. For example, $ 7.20 of B's depreciation deduction would be included in combined report business income in Year 6 ($ 12 depreciation deduction x 60% partial inclusion ratio).

Example 12: Decreasing partial inclusion ratio.

Facts. Assume the same facts as in Example 8, except that B does not sell the land to Y in Year 5. In Year 6, B's partial inclusion ratio is 25%, a 62% decrease from B's Year 1 ratio of 66% (41% difference between 66% Year 1 ratio and 25% Year 6 ratio, divided by 66% Year 1 ratio, equals 62%).

Acceleration rule. Under subparagraph **13d.9.c.2.D.**, the acceleration rule will apply to take S's intercompany gain of $ 66 into account in Year 5 (immediately before the income year in which B's partial inclusion ratio falls below the 50% threshold).

Example 13: Election made under subparagraph **13d.9.c.2.E.**

Facts. Assume the same facts as in Example 12, except that the taxpayer elects under subparagraph **13d.9.c.2.E.** to have the acceleration rule apply to take into account only a proportionate share of the intercompany item. B's partial inclusion ratio is 33% in Year 7, 16% in Year 8, and 8% in Year 9.

Acceleration rule. In Year 6, $ 40.92 of S's intercompany gain would be taken into account ($ 66 intercompany gain multiplied by the 62% proportionate decrease between B's 66% Year 1 ratio and B's 25% Year 6 ratio). B's partial inclusion ratio rose in Year 7; but the Year 8 partial inclusion ratio represented a new low point. At 16%, the Year 8 partial inclusion ratio was 76% below the Year 1 ratio of 66% (50% difference between 66% Year 1 ratio and 16% Year 8 ratio, divided by 66% Year 1 ratio, equals 76%). Accordingly, $ 9.24 of S's intercompany gain would be taken into account in Year 8 ($ 66 intercompany gain x 14% incremental difference between 76% decrease and the 62% decrease that was previously recognized). In Year 9, B's partial inclusion ratio fell

below the 10% floor, so S's remaining intercompany gain of $ 15.84 is taken into account.

13d.9.d. Earnings and profits. The timing provisions of this section 13d apply to the calculation of West Virginia earnings and profits. Therefore, the West Virginia earnings and profits of S will not reflect S's intercompany items until those items are taken into account under this section 13d.

13d.9.e. Foreign country operations. To the extent that foreign country operations are included in the combined report, and the corporations engaging in those operations are not required to report intercompany transactions under a similar deferral method for federal income tax purposes or any other purposes, then intercompany transactions involving those foreign operations may be reported using the method used for consolidated financial reporting purposes if that method reasonably reflects income and approximates the result that would be obtained from use of the provisions of this section 13d. However, adjustments may be permitted or required for any transaction or series of transactions for which the financial reporting method does not produce a result which reasonably approximates the results that would have been obtained under this section 13d.

13d.9.f. If the taxpayer fails to disclose its DISA balance on its annual tax return, the Tax Commissioner may, in the Tax Commissioner's discretion, require the amounts in the undisclosed DISA accounts to be taken into account in part or in whole in any year of such failure.

13d.9.g. Recordkeeping. Intercompany and corresponding items shall be reflected on permanent books and records (including work papers).

13d.10. Effective date. This section 13d applies to intercompany transactions occurring on or after January 1, 2009.

§110-24-13e. Election To File A Group Return; Designation Of Surety.

13e.1. *General.* -- Every taxpayer subject to the West Virginia corporation net income tax is required to file its own tax return, including taxpayers that are members of a combined reporting group. Taxpayers subject to the West Virginia corporation net income tax that are members of a combined reporting group are required to attach a combined report to their annual tax returns. Members of a combined reporting group may annually elect to designate one taxpayer member of the combined group to file a single return in the form and manner prescribed by the Tax Department, in lieu of filing their own respective returns, without changing the respective liability of the group members. The group member taxpayer designated to file the single return must consents to act as surety with respect to the tax liability of all other taxpayers properly included in the combined report and must agree to act as agent on behalf of those taxpayers for the year of the election for tax matters relating to the combined report for that year. All combined group members required to file in West Virginia must be

included in the group tax return filed pursuant to this section and W. Va. Code § 11-24-13e.

13e.1.a. *Combined report.* -- "Combined report" refers to the schedules that are required to be filed by W. Va. Code § 11-24-13a, which are attached to the West Virginia Form 120 of a taxpayer member of the combined reporting group, which reports the taxpayer member's income from sources within this State under the combined reporting method and other information required by law.

13e.1.b. *Combined reporting group.* -- "Combined reporting group" refers to those corporations and entities with business income that are permitted or required to be included in a particular combined report under W. Va. Code § 11-24-13a. A combined reporting group includes those partnerships and limited liability companies treated as partnerships for federal income tax purposes whose incomes are required to be included in a combined report.

13e.1.c. *Group return.* -- "Group return" means a single composite tax return filed under W. Va. Code § 11-24-13e on behalf of members of a combined reporting group, and includes, but is not limited to annual returns and quarterly and other periodic returns, declarations of estimated tax and the forms for making installment payments of estimated tax. The group return reflects the aggregate total tax of the tax liabilities of all of the Taxpayer members, calculated on the basis of the separate tax liability of each such Taxpayer member.

13e.1.d. *Key corporation or key member.* -- "Key corporation" or "key member" means the taxpayer member which files a group return described under this section on behalf of the taxpayer members of the combined reporting group as agent and surety for the taxpayer members of the combined reporting group pursuant to West Virginia Code §11-24-13e.

13e.1.e. *Taxpayer member.* -- "Taxpayer member" means a corporation or entity which is required to file a tax return under West Virginia Code §11-24-1 *et seq.* in this State, and which is a member of a combined reporting group.

13e.1.f. The term "corporation" as used in this section means and includes any entity required to file a tax return under article 11-24-1, *et seq.* of the West Virginia Code, and any entity whose income, expenses, capital or activities are required to be included on or as a part of a combined report under article 11-23-1 *et seq* or article 11-24-1, *et seq.* of the West Virginia Code.

13e.2. *Requirements.*

13e.2.a. In order to be eligible to make the election provided under this section, the electing key corporation must meet the definition of a "key corporation" as defined in this section in addition to meeting the following requirements, by either being:

13e.2.a.1. The parent corporation of the combined reporting group as defined in subparagraph 8.7.a.1.A. of these rules, or

13e.2.a.2. If the parent corporation of the combined reporting group is not a taxpayer member, the taxpayer member with the largest West Virginia property factor numerator, and

13e.2.a.3. The key corporation's powers, rights and privileges must not be forfeited or suspended by the West Virginia Secretary of State and it must not have a petition with the United States Bankruptcy Court pending on the last day of the taxable year.

13e.2.b. If the entity that would have otherwise been designated as the key corporation under this section is disqualified due to the parent corporation not being a taxpayer member, or due to rights and privileges having been forfeited or suspended by the West Virginia Secretary of State, or due to a pending bankruptcy petition, then the Members of the combined reporting group may not elect to designate one taxpayer member of the combined group to file a single return under West Virginia Code §11-24-13e.

13e.3. *Manner for making the election.* -- An election to file a group return is made by the key corporation by the filing of an Election to File Unitary Taxpayers' Group Return, filed in conjunction with its West Virginia Form 120, which sets forth such information as the Tax Commissioner may prescribe. This election must be made with an original, timely filed return, determined by including any authorized extensions for filing the return.

13e.4. *Consequences of making an election.*

13e.4.a. The election is binding on all the taxpayer members of the combined group and the key corporation for all matters for the taxable year of the election.

13e.4.b. *The key corporation shall file the group return.* -- The group return satisfies the requirement for filing a West Virginia form 120 by each taxpayer member listed on the key corporation's Election to File Unitary Taxpayers' Group Return, filed in conjunction with its West Virginia Form 120, listing of members included in the group return.

13e.4.b.1. A combined group member having income or gain not required to be reported on the combined return, and having no income that is required to be reported on the combined return, need not be included in the group return, but may either file a separate return or may be included on the group return, and, if so included shall report income or gain not required to be reported on the combined return in the group return. A combined group member having income that is required to be reported on the combined return, shall be included in the group return, and the group return shall report both income that is required to be reported on the combined return for that

combined group member and any income or gain not required to be reported on the combined return for that combined group member shall also be reported on the group return.

13e.4.b.2. By signing the West Virginia Form 120, an officer of the key corporation is attesting that he or she has the legal authority to bind the key corporation to all of its duties.

13e.4.b.3. Failure of a taxpayer member, properly included in a group return, to file its own return shall be deemed to be an acknowledgement that the officer of the key corporation possesses the authority to fulfill the taxpayer member's return filing obligation.

13e.4.b.4. A taxpayer member asserting that it is not properly included in a group return must independently satisfy its obligation to file a return.

13e.4.c. The key corporation is a surety for each taxpayer member properly included in a group return, for payments owed under the West Virginia corporation net income tax law for the tax year for which the election applies.

13e.4.d. The key corporation is an agent for each taxpayer member.

13e.4.e. Extensions for filing tax returns or waivers to extend the statute of limitations for issuing notices of assessments shall be executed by the key corporation and shall be effective for all taxpayer members properly included in a group return, for the tax year for which the election applies.

13e.4.f. All Tax Department notices, assessments, legal documents and administrative documents relating to or regarding the business franchise tax or corporation net income tax liability of a taxpayer member properly included in a group return, may be sent to the key corporation and additional amounts due with respect to any taxpayer member properly included in a group return, may be assessed and billed to the key corporation, which shall be liable for payment of such amounts. The key member may file a petition for reassessment on behalf of a taxpayer member properly included in a group return, in response to a notice of assessment. The key member may also file claims for refund or credit and petitions for refund or credit on behalf of the a taxpayer member properly included in a group return. Any refund or credit due to a taxpayer member properly included in a group return may be paid or credited to the key corporation. Any levy, any notice of a lien, or any other proceeding to collect the amount of any assessment, after an assessment has become final, shall name the corporation or entity from which such collection is to be made. A taxpayer member properly included in a group return from which collection is to be made and the key corporation, as surety and agent of the taxpayer, shall be jointly and severally liable for any amount due.

13e.4.g. If some or all of the corporations included in the election to file a group

return are subsequently determined not to be members of the combined reporting group of the key corporation, then the key corporation and the electing taxpayer members shall be deemed to agree that any subsequent adjustment for any and all members included in the original group return may still be billed to or paid by the key corporation in the case of assessments and refunded to the key corporation in the case of overpayments.

13e.5. *Duration of election to file group return.* -- The election to file a group return for all matters for the taxable year of the election will remain in effect until 30 days following the receipt by the Tax Commissioner of a written notice of termination of the election by any of the taxpayer members. The taxpayer member that is terminating the election must also notify the previously designated key corporation that the election is being terminated. The termination will only be applied prospectively. If the key corporation is terminating the election, it must notify all of the taxpayer members that were included in the group return election. If an employee, agent or representative of the Tax Commissioner is conducting an examination of a combined group return at the time when any of the taxpayer members or a key corporation sends a written notice of termination to the Tax Commissioner, the terminating taxpayer member or terminating key corporation must provide the employee, agent or representative of the Tax Commissioner that is conducting the examination with a copy of the written notification of termination of the election.

13e.6. *Failure or inability of key corporation to perform its duties.* -- If the key corporation does not fulfill its obligation to pay any tax liability or to act on behalf of the taxpayer members, or if its powers, rights and privileges are forfeited or suspended at any time with respect to a tax year, each taxpayer member may be independently assessed or billed for its own tax liability for that tax year. In that event, each taxpayer member will be credited with taxes previously paid in accordance with the taxpayer member's tax liability as indicated in the return data as filed. In the event that the liabilities of the taxpayer members cannot be derived from the return data as filed, the individual liabilities of the each of the respective members may be determined by the Tax Commissioner from data obtained during audit or supplied by the taxpayer members, using the best available information. If insufficient information is available to determine individual liabilities, the Tax Commissioner, may, in the discretion of the Tax Commissioner, credit taxes paid in a manner that is reasonable under the circumstances.

13e.7. *Curing an invalid election.*

13e.7.1. In the event that a taxpayer fails to satisfy one or more of the conditions of this section, the Tax Commissioner may, at the request of the taxpayer and at the Commissioner's discretion, treat the W. Va. Code § 11-24-13e election to designate one taxpayer member of the combined group to file a single return, as being valid.

13e.7.2. In lieu of disallowing a W. Va. Code § 11-24-13e election to designate one taxpayer member of the combined group to file a single return, the Tax

Commissioner may, at the Commissioner's discretion, allow the taxpayer members to designate another taxpayer member in substitution for the key corporation originally designated in the election.

13e.8. *Appointment of designated agent for purposes of resolving disputes over membership in a combined group.* -- If the Tax Commissioner determines that one or more corporations which did not join in the filing of a group return are members of a combined group, or that one or more corporations which did join in the filing of a group return are not members of the combined group which filed the return, then, for purposes of resolving disputes over the membership of the combined group and any separate company item of any such corporation:

13e.8.1. *Notification of deficiency or assessment to corporation which has ceased to be a member of the combined group.* -- If a corporation that made the election to file or was required to join in the filing of a group return has ceased to be a member of the combined group, and if such corporation files written notice of such cessation with the Tax Commissioner, then the Commissioner upon request of such corporation must furnish the corporation with a copy of any notice of deficiency or notice of assessment in respect of the tax for a group return year for which it was a member of the combined group and information regarding any notice and demand for payment of such deficiency. The written notice of cessation should be mailed to the address stated in the instructions to the West Virginia corporation net income tax return. The filing of the written notification and request by a corporation shall not have the effect of limiting the scope of the agency of the key member provided for in this section with respect to those tax years during which the corporation was a member of the combined group for which a group return was filed, and a failure by the Tax Commissioner to comply with such written request shall not have the effect of limiting the liability of such corporation.

13e.8.2. If no group return was filed, the corporations may appoint a member of the combined group as the designated agent solely for purposes of contesting the Tax Commissioner's determination. The Commissioner may accept a written representation made by any member of the combined group that it has been appointed the designated agent. The appointment of a designated agent under this provision shall not be construed as a concession by either the corporations or the Tax Commissioner regarding the proper composition of the combined group. The designated agent appointed under this provision shall have all rights and responsibilities of a key corporation under this section, including the responsibility to file a group return for all tax periods beginning on or after the appointment of the key member. The designated agent appointed under this subsection. must meet the qualifications of a key member as provided in these rules, and must continue to act as designated agent for the combined group under the provisions this section for all tax periods beginning on or after the appointment of the key member, until the appointment of the key member is lawfully revoked.

13e.8.3. If a group return was filed, the key member which filed the return shall represent all corporations which joined in the filing of the group return and all

corporations which the Tax Commissioner asserts are members of the combined group, except that the Commissioner may allow any corporation which the Commissioner asserts should be added to or eliminated from the combined group included in the return to represent itself after receipt of a written request from such corporation. And in such case, any such corporation shall be bound by any action taken by the designated agent (including, for example, extensions of the statute of limitations, settlements, stipulations or concessions of fact) before the request of such corporation to represent itself has been accepted by the Tax Commissioner.

13e.9. *Liability for combined tax, additions to tax, penalty and interest.*

13e.9.1. *Joint and several liability of members of a combined group.* -- The taxpayer members who elected to file a group return shall be jointly and severally liable for the combined tax, addition to tax, penalty and interest computed in accordance with the West Virginia Tax Procedure and Administration Act codified in article ten, chapter eleven of the West Virginia Code.

13e.9.2. *Effect of intercompany agreements.* -- No agreement entered into by one or more members of a combined group with any other member of such group or with any other person shall in any case have the effect of reducing the liability prescribed under this Section, or these rules or West Virginia Code §11-24-1 *et seq.*

13e.9.3. *Additions to tax, penalties and interest.* -- If additions to tax, penalties or interest are imposed under the West Virginia Tax Procedure and Administration Act, with respect to a group return year, the amount shall be based on the combined tax liability or deficiency for the common taxable year.

13e.9.3.a. For purposes of applying the addition to tax for failure to file a return:

13e.9.3.a.1. A corporation which erroneously fails to join in the filing of a group return, but which timely files a separate West Virginia corporation net income tax return or joins in the timely filing of a group return for another combined group, shall not be subject to any addition to tax for failure to timely file the return. In determining whether the separate or group return is timely filed, the separate taxable year of the corporation or the common taxable year of the taxpayer members included in the group return such corporation erroneously joined shall be used, rather than the common taxable year of the group with which the corporation should have filed. Provided that the Tax Commissioner may at the discretion of the Tax Commissioner, disallow the group return under which the Taxpayer should have filed, but failed to file, and require all group members to each file separately. The Tax Commissioner may at the discretion of the Tax Commissioner, disallow the group return under which the Taxpayer filed, in circumstances where the Taxpayer erroneously filed under the group return of a different combined group, and require all group members of the group under which the Taxpayer erroneously filed to each file separately. Also the Tax Commissioner may at the discretion of the Tax Commissioner disallow both group returns and require

separate filings for each member of both such groups.

13e.9.3.a.2. A corporation which erroneously fails to join in the filing of a group return, and which fails, without reasonable cause, to timely file a separate West Virginia corporation net income tax return or to join in the timely filing of a group return for another combined group, shall be subject to additions to tax for failure to timely file a return computed on the amount of tax shown (or required to be shown) due on the group return for its proper combined group. Because it is the duty of the key member, acting on behalf of the combined group, to include the corporation in the group return, the members of the combined groups shall be jointly and severally liable for the amount of the addition to tax.

13e.9.3.a.3.A corporation which erroneously joins in the timely filing of a group return shall not be subject to additions to tax for failure to file a return, but Depending on the facts and circumstances of the case, may be subject to applicable sanctions for failure to pay tax, late filing, tax evasion, fraud or other applicable administrative or criminal sanctions.

13e.9.3.b. For purposes of applying the addition to tax for failure to timely pay tax:

13e.9.3.b.1. In a case where a corporation or entity erroneously fails to join in the filing of a group return for a common taxable year, neither that corporation or entity nor the combined group shall be subject to any failure-to-pay addition to tax under the West Virginia Tax Procedure and Administration Act if timely payment is made of the tax shown on a separate return filed by such corporation or on a group return in which it erroneously joins in filing for each taxable year ending with or within such common taxable year. Unless there is reasonable cause for the failure of such corporation or entity to join in the filing of the group return, such corporation or entity and the combined group may be jointly and severally liable for the addition to tax for failure to pay any additional amount which would have been shown on the group return had such corporation or entity been included. Depending on the facts and circumstances of the case the Taxpayer may be subject other applicable administrative or criminal sanctions.

13e.9.3.b.2. A corporation or entity which erroneously fails to join in the filing of a group return for a common taxable year or which joins in the filing of a group return, for the taxable year ending with or within such common taxable year, and which also fails to timely pay the tax shown on the return, shall be subject to additions to tax under the West Virginia Tax Procedure and Administration Act only for failure to pay the tax shown on the return it actually files or joins in filing. Unless there is reasonable cause for the failure of such corporation or entity to join in the filing of the group return, such corporation and the combined group may be jointly and severally liable for an addition to tax under the West Virginia Tax Procedure and Administration Act for failure to pay any additional amount which would have been shown on the group return had such corporation been included. Depending on the facts and circumstances of the case,

the Taxpayer may be subject other applicable administrative or criminal sanctions.

13e.9.3.b.3. If a corporation erroneously joins in the filing of a group return, neither such corporation nor the combined group shall be subject to the addition to tax under the West Virginia Tax Procedure and Administration Act for failure to pay any tax required to be shown on a separate company return and the combined group shall not be subject to addition to tax under the Act for failure to pay any increase in tax resulting from the exclusion of such corporation from the combined group if the tax timely paid with the original group return exceeds the total tax required to be shown on the correct returns. Depending on the facts and circumstances of the case, the Taxpayer may be subject other applicable administrative or criminal sanctions.

13e.9.3.c. For purposes of applying the addition to tax for negligence imposed by the West Virginia Tax Procedure and Administration Act or the addition to tax for fraud imposed by that Act, in any case in which a corporation erroneously joins or fails to join in the filing of a group return, the addition may be imposed on any deficiency resulting from such error, without taking into account any overpayment which may have resulted from the error.

Example. Corporations A, and B meet all the requirements of a unitary business combined group. Corporations A and B cannot be included in the same unitary business group as their non-unitary affiliate Corporation C. On a separate-return basis, Corporation A has a West Virginia net loss of $500, Corporation B has West Virginia net income of $300 and Corporation C has West Virginia net income of $700. Corporations A and C file a group return reporting combined West Virginia net income of $200, while Corporation B files a separate return reporting West Virginia net income of $300. On audit, the Tax Commissioner corrects the liabilities by combining Corporations A and B, which eliminates Corporation B's separate return income and entitles them to a refund of the taxes paid by Corporation B, and by determining a separate return deficiency for Corporation C. If the combination of Corporations B and C on the original return was due to negligence or an intent to defraud, Corporation C will be subject to the applicable addition to tax on its entire deficiency without regard to the overpayment made by Corporation B.

13e.9.4. *Interest.* – If interest is imposed under the West Virginia Tax Procedure and Administration Act, with respect to a group return year, the amount shall be based on the separate tax liability, deficiency underpayment or overpayment of the group return members for the common taxable year.

13e.9.5. *Combined amended returns.*

13e.9.5.a. If an election to file a group return is in effect for a taxable year and that election is subsequently revoked for that year because the group is not a unitary business, the key member may not file a group amended return. If a group files what it believes to be a correct group return and it is later determined that the group is not engaged in a unitary business, the key member shall not file a group amended return.

Instead, in either instance, the key member and each corporation which joined in the filing of the group return shall file a separate amended return. In computing the tax due on any such amended return, the filer shall take into account all payments, credits and other amounts (including refunds) actually paid by, or to, the filer, or applied by, or for, the filer under the erroneously filed group return.

13e.9.6. *Ineligible member.* -- If a change in liability relates to the removal from the group return of a member that was not eligible to be included in the group return, or of a taxpayer which could not be required to be a part of the group (e.g., a corporation which was not engaged in a unitary business with the combined group members), the key member shall file a group amended return and the ineligible taxpayer member shall file a separate amended return.

13e.9.7. If a corporation erroneously fails to join in the filing of a group return, the key member shall file an amended group 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 group return.

13e.10. *Application.* -- This section applies to taxable years beginning after December 31, 2008.

§110-24-13g. Treatment Of Certain Charitable Expenses.

13g.1. When a charitable expense is incurred by a member of a combined group, the threshold question is whether the charitable contribution was paid from nonbusiness income, from business income that is unitary group business income, or from business income that is not unitary group business income. If the contribution was of property other than money, the question becomes whether the property was an asset that generated nonbusiness income, unitary group business income, or other business income from a separate line of business. In the event the property generated no income, the preceding sentence shall be applied as if the property generated income. Only when the charitable expense, or any part thereof, was not paid from nonbusiness income or from business income that is not unitary business income, may the expense, or the portion thereof, not paid from nonbusiness income, or from business income that is not unitary group business income, be applied against unitary group business income as provided in subsection 13g.2. of this section.

13g.2. When the charitable expense incurred by a member of a combined group was paid from unitary group business income then, to the extent allowable as a deduction pursuant to IRC § 170, it shall be subtracted first from the business income of the combined group, subject to the income limitations of IRC § 170 applied to the entire business income of the group and any remaining amount shall then be treated as a nonbusiness expense allocable to the member that incurred the expense, subject to the income limitations of IRC § 170 applied to the nonbusiness income of that specific member. If nonbusiness income is less than the nonbusiness charitable expenses, the

difference may be carried forward. Any charitable deduction disallowed under the foregoing rule, but allowed as a carryover deduction in a subsequent year, shall be treated as originally incurred in the subsequent year by the same member and the rules of this section shall apply in the subsequent year in determining the allowable deduction in that year.

13g.3. This section shall apply to contributions made during a taxable year beginning after December 31, 2008.

§§110-24-14 through 19. Reserved for future use.

§ 110-24-20. Report of Change In Federal Taxable Income.

20.1. *General rule.* –

20.1.a. If the amount of a taxpayer's federal taxable income reported on its federal income tax return for any taxable year is changed or corrected by the United States Internal Revenue Service or other competent authority, or as the result of a renegotiation of a contract or subcontract with the United States, the taxpayer shall file an amended West Virginia return to report such change or correction in federal taxable income within the time specified in West Virginia Code § 11-24-20, after the final determination of such change, correction or renegotiation, or as otherwise required by the tax commissioner, and shall concede the accuracy of such determination or state wherein it is erroneous, except as otherwise provided in this section.

20.1.b. Any taxpayer filing an amended federal income tax return shall also file an amended corporate net income tax return within the time specified in West Virginia Code § 11-24-20, and shall give such information as the Tax Commissioner may require.

20.2. *Amended combined report.* -- When the taxpayer files an amended return as provided in this section, and the taxpayer is a member of a combined group engaged in unitary business activity in this State, the taxpayer shall file with the amended return an amended combined report for the combined group.

20.3. *Amended group return.* -- The general rule provided in subsection 20.1 of this section applies when the taxpayer files its annual return on a separate company basis. For a taxable year beginning after December 31, 2009, a taxpayer engaged in unitary business activity in this State that must file an amended return as provided in West Virginia Code § 11-24-20 and in this section, which filed under a group return as provided in W. Va. Code § 11-24-13e for the tax year at issue, may not file a separate amended return. Instead, the key member which filed the group return which included the Taxpayer as one of the group filers, shall file an amended group corporation net income tax return for the tax year at issue. The key member shall attach to the amended group return an amended combined report for the combined group engaged in unitary business activity in this State.

§§110-24-21 through 25. Reserved for future use.

§110-24-26. Priority Of Tax In Distributions Of Property And Estates.

26.1. In the distribution, voluntary or compulsory, in receivership, bankruptcy or otherwise, of the property or estate of any person, all taxes due and unpaid under W. Va. Code §§11-24-1, *et seq.* shall be paid from the first money available for distribution in priority to all claims and liens except taxes and debts due the United States which under federal law are given priority over the debts and liens created by W. Va. Code §11-24-1 et seq. Any person charged with the administration or distribution of any such property or estate who shall violate the provisions of this section shall be personally liable for any taxes accrued and unpaid under W. Va. Code §§11-24-1, *et seq.* which are chargeable against the person whose property or estate is in administration or distribution.

26.2. There is a priority for all unpaid corporation net income tax in distributions of the property or estate of any person, and the tax must be paid from the first money available for distribution in priority to all other claims and liens, except taxes and debts due the United States.

26.2.a. The distribution of property subject to federal tax liens is subject to the priority of such liens provided in the Internal Revenue Code.

26.2.b. The distribution of property in federal bankruptcy proceedings is subject to the priorities of debts and liens provided in the United States Bankruptcy Code (11 U.S.C. '101 *et seq.*).

26.2.c. This priority applies to the amount of tax, interest, additions to tax, and penalties.

26.3. The priority applies to all distributions of the property or estate of any person. A "distribution" of property of an estate is the sale or transfer of the property, or the disbursement of money resulting from the sale or transfer of the property or estate of any person. Distributions include, but are not limited to, the transfer of property or disbursement of proceeds of sales of property by any executor, administrator, receiver, trustee, fiduciary, special commissioner, or any public officer under judicial process; and distributions in any proceedings such as bulk sale, liquidation sale, estate sale, assignment for the benefit of creditors, interpleader action, and administrative or judicial proceeding for the dissolution of a partnership or corporation.

26.4. The priority does not apply to transactions that do not constitute distributions of property. These transactions include the sale or transfer of property in the ordinary course of the business of the owner of the property; sales or transfers of any property by the owner or for consideration payable to the owner by the purchaser or transferee.

26.5. This priority applies to the distribution of all property, including but not limited to real property or any interest therein; tangible personal property, including fixtures, equipment, machinery, furniture and vehicles; intangible property, including accounts receivable, contract rights, bank accounts, stocks, bonds; and the proceeds from the sale or liquidation of any such property.

26.6. This priority requires payment of the tax from the first money that is available for distribution to lienors, creditors, beneficiaries, or any other person, after payment of costs, commissions, fees and any other expenses incurred in the preservation, storage, liquidation, or transportation of the property or estate.

26.7. The debt or claim for taxes has priority over all claims and liens, except debts due the United States.

26.7.a. Claims subject to this priority include any debt or obligation, liquidated or unliquidated, that does not constitute a lien upon the property or estate.

26.7.b. Liens subject to this priority include any charge or encumbrance on the property or estate for payment of any claim, debt or obligation, such as a deed of trust, judgment lien, security interest, vendors lien, execution lien, tax lien, mechanics lien, landlords lien and municipal lien.

26.7.c. The priority of the corporation net income tax debt in such distributions is not determined by the presence or absence of a perfected notice of tax lien, by the presence or absence of a perfected lien securing any competing claim or debt, or by the order in which any such competing liens were perfected.

§110-24-27. "Safety Zones" Bar Imposition Of Additions To Tax For Underpayment Of Estimated Tax.

27.1. In General. - Additions to tax will not be imposed for any underpayment of any installment of estimated tax if, on or before the date prescribed for payment of the installment (determined with regard to any authorized extension of time for payment), the total amount of all payments of estimated tax made equals or exceeds the least of the amounts due under "Safety zones" set forth in this section.

27.1.a. Safety zone 27.1.a.. - The amount of tax due with the annual return is five hundred dollars ($500) or less.

27.1.b. Safety zone 27.1.b.- The amount of tax due with the annual return is ten percent (10%) or less of the tax liability for the taxable year.

27.1.c. Safety zone. – For tax years beginning on or after January 1, 2010 -- The amount of tax which would be due if computed based on the facts and law applicable to the West Virginia corporate net income tax return for the preceding year, but using current year rates, exemptions and credits. This safety zone avoids additions to tax if

the total payments of estimated tax already made by the installment date are at least equal to an amount which would have been required on that installment date if the estimated tax was determined based on the facts shown on the previous year's return and the previous year's law, but using current year rates, exemptions and credits. In this safety zone, the following rules apply:

27.1.c.1. Nonrecurring items of income and deductions are not to be excluded.

27.1.c.2. An entity that did not file a West Virginia corporate net income tax return for the preceding tax year cannot use this safety zone.

27.1.d. Application of safety zones to short tax years. – For purposes of this subsection 27.1 and subsection 27.2, additions to tax for an underpayment of estimated tax are equally applicable to short tax years where a declaration of estimated tax is required to be filed. In computing the safety zones for short taxable years, the estimated tax (whether based on that shown on the previous year's return, based on the previous year's facts, or based on annualized current income) is reduced by multiplying the estimated tax for a full year by the percentage which the number of months in the short tax year bears to twelve (12).

27.1.e. For purposes of this subsection 27.1 and subsection 27.2, if the tax rates for the current year have changed from those in effect for the preceding year, the estimated tax must be computed using current rates.

27.1.f. Safety zone requirements. - For purposes of this subsection 27.1 and subsection 27.2, safety zone requirements must be satisfied on each installment date to avoid the imposition of additions to tax on an underpayment of estimated tax as of the installment date. For purposes of this rule, it is presumed that a taxpayer's West Virginia taxable income is received in equal installments throughout the taxable year. The taxpayer bears the burden of proof to establish that the West Virginia taxable income was received during the taxable year in some other manner.

27.2 Transition period safety zones. The combined reporting requirements of West Virginia Code §11-24-1 *et seq.* apply for tax years beginning on and after January 1, 2009. Safety zones set forth in this subsection 27.2 apply only with relation to estimated payments made for the first tax year beginning on or after January 1, 2009.

27.2.a. For purposes of safety zones set forth in this subsection 27.2, the terms "previous tax year" or "previous year" mean the tax year immediately preceding the first tax year beginning on or after January 1, 2009.

27.2.a.1. Additions to tax will not be imposed for any underpayment of any installment of estimated tax if, on or before the date prescribed for payment of the installment (determined with regard to any authorized extension of time for payment),

the total amount of all payments of estimated tax made equals or exceeds the least of the amounts due under "Transition period safety zones" set forth in this subsection 27.2.

27.2.b. Transition period safety zone 27.2.b – This safety zone applies for a Taxpayer who filed separately for the tax year immediately preceding the first tax year beginning on or after January 1, 2009, but not on a combined reporting basis. This safety zone is available only for the first tax year beginning on or after January 1, 2009.

27.2.b.1. For any entity who filed separately for the tax year immediately preceding the first tax year beginning on or after January 1, 2009:

27.2.b.2. If the previous tax year was a full 12 month tax year and

27.2.b.3. If the amount of tax shown for the previous year has not been adjusted, redetermined or the subject of an assessment or other challenge by the Tax Commissioner, and

27.2.b.4. If total payments of estimated tax made by each installment date for the first tax year beginning on or after January 1, 2009 are at least equal to the amount which would have been required on that installment date if the estimated tax was the amount of tax shown on the previous year's West Virginia corporate net income tax return, then this safety zone applies, except that:

27.2.b.5. If the annual return for the preceding year is not filed on or before the due date, including extensions of time to file, of the annual return for the preceding year, then the declaration of estimated tax for the current tax year cannot be based on last year's tax, and this safety zone does not apply.

27.2.b.6. If the preceding taxable year was a short year, estimated tax for the current year will be computed on an annualized basis. For purposes of this safety zone, the pro forma amount of tax that would have been shown on the preceding tax year's West Virginia corporate net income tax return, on a recomputed separate filing basis, shall be computed on an annualized basis. The requirements of paragraphs 27.2.b.3. through 27.2.b.5 must be met for the short year in order for this safety zone to apply. The annual of tax payable for the current year and the estimated tax for the current year will not be reduced because the previous year was a short year.

27.2.c. Transition period safety zone 27.2.c – This safety zone applies for a Taxpayer who filed as part of a consolidated filing unit, composite filing unit or group filing unit other than a combined reporting or unitary group for the tax year immediately preceding the tax year beginning on or after January 1, 2009. This safety zone is available only for the first tax year beginning on or after January 1, 2009.

27.2.c.1. For any entity that filed corporate net income tax as a component member of a consolidated, composite or group filing unit other than a combined or unitary filing group:

27.2.c.2. If the previous tax year was a full 12 month tax year, and

27.2.c.3. If the previous year amount of tax shown has not been adjusted, or redetermined or the subject of an assessment or other challenge by the Tax Commissioner, and

27.2.c.4. If total payments of estimated tax made by each installment date are at least equal to the amount which would have been required on that installment date if the estimated tax was determined based on the pro forma amount of tax that would have been shown on the pro forma previous year's West Virginia corporate net income tax return, determined on a recomputed separate filing basis for the Taxpayer but not on a combined reporting basis, then this safety zone applies, except that:

27.2.c.5. If the annual return for the preceding year is not filed on or before the due date, including extensions of time to file, of the annual return for the preceding year, then the declaration of estimated tax for the current tax year cannot be based on last year's tax, and this safety zone does not apply.

27.2.c.6. If the preceding taxable year was a short year, estimated tax for the current year will be computed on an annualized basis. For purposes of this safety zone, the pro forma amount of tax that would have been shown on the preceding tax year's West Virginia corporate net income tax return, on a recomputed separate filing basis but not on a combined reporting basis, shall be computed on an annualized basis. The requirements of paragraphs 27.2.c.3 through 27.2.c.5 must be met for the short year in order for this safety zone to apply. The annual of tax payable for the current year and the estimated tax for the current year will not be reduced because the previous year was a short year.

27.2.d. Transition period safety zone 27.2.d -- This safety zone applies for a Taxpayer who filed a separate tax return, but as a component member of a unitary, or combined reporting group for the tax year immediately preceding the first tax year beginning on or after January 1, 2009. This safety zone is available only for estimated payments made for the first tax year beginning on or after January 1, 2009.

27.2.d.1. This safety zone applies with relation to taxpayers that filed a separate tax return, but as a component member of a unitary, or combined reporting group, for the tax year immediately preceding the tax year beginning on or after January 1, 2009.

27.2.d.2. For any entity that filed corporate net income tax as a component member of a unitary, composite or group filing unit:

27.2.d.3. If the previous tax year was a full 12 month tax year and

27.2.d.4. The amount of tax shown for the previous year has not been adjusted, redetermined or the subject of an assessment or other challenge by the Tax Commissioner, and

27.2.d.5. If the unitary or combined reporting group remains the same for the first tax year beginning on or after January 1, 2009 as the previous tax year, and

27.2.d.6. If total payments of estimated tax made by each installment date are at least equal to the amount which would have been required on that installment date if the estimated tax was computed based on the amount of tax shown on the previous year's West Virginia corporate net income tax return, then this safety zone applies, except that:

27.2.d.7. If the annual return for the preceding year is not filed on or before the due date, including extensions of time to file, of the annual return for the preceding year, then the declaration of estimated tax for the current tax year cannot be based on last year's tax, and this safety zone does not apply.

27.2.d.8. If the preceding taxable year was a short year, estimated tax for the current year will be computed on an annualized basis. The requirements of paragraphs 27.2.d.4. through 27.2.d.7 must be met for the short year in order for this safety zone to apply. The annual tax payable for the current year and the estimated tax for the current year will not be reduced because the previous year was a short year.

27.2.e. Transition period safety zone 27.2.e -- This safety zone applies for a Taxpayer who filed as a component member of a composite tax return or group tax return, and as a component member of a unitary, or combined reporting group for the tax year immediately preceding the first tax year beginning on or after January 1, 2009 and who will likewise file as a component member of a composite tax return or group tax return, and as a component member of a unitary, or combined reporting group for the first tax year beginning on or after January 1, 2009. This safety zone is available only for estimated payments made for the first tax year beginning on or after January 1, 2009.

27.2.e.1. This safety zone applies with relation to Taxpayers that did not file a separate return in the previous year, and who instead filed as a component member of a composite tax return or group tax return filing unit, and as a component member of a unitary, or combined reporting group for the tax year immediately preceding the tax year beginning on or after January 1, 2009.

27.2.e.2. For any entity that filed corporate net income tax as a component member of a composite tax return or group tax return, and as a component member of a unitary, or combined reporting group filing unit for the tax year immediately preceding the tax year beginning on or after January 1, 2009:

27.2.e.3. If the previous tax year was a full 12 month tax year and

27.2.e.4. The amount of tax shown for the previous year has not been adjusted, redetermined or the subject of an assessment or other challenge by the Tax Commissioner, and

27.2.e.5. If the unitary or combined reporting group remains the same for the first tax year beginning on or after January 1, 2009 as the previous tax year, and

27.2.e.6 If the component membership of the composite tax return or group tax return remains the same for the first tax year beginning on or after January 1, 2009 as the previous tax year, and

27.2.e.7. If total payments of estimated tax made by each installment date are at least equal to the amount which would have been required on that installment date if the estimated tax was computed based on the amount of tax shown on the previous year's West Virginia corporate net income tax return, then this safety zone applies, except that:

27.2.e.8. If the annual return for the preceding year is not filed on or before the due date, including extensions of time to file, of the annual return for the preceding year, then the declaration of estimated tax for the current tax year cannot be based on last year's tax, and this safety zone does not apply.

27.2.e.9. If the preceding taxable year was a short year, estimated tax for the current year will be computed on an annualized basis. The requirements of paragraphs 27.2.e.4. through 27.2.d.8 must be met for the short year in order for this safety zone to apply. The annual tax payable for the current year and the estimated tax for the current year will not be reduced because the previous year was a short year.

27.2.f. Transition period safety zone 27.2.f. – This safety zone applies for a Taxpayer who filed as a component member of a composite tax return or group tax return, and as a component member of a unitary, or combined reporting group for the tax year immediately preceding the first tax year beginning on or after January 1, 2009, and who will file separately as a component member of a unitary, or combined reporting group for the first tax year beginning on or after January 1, 2009. This safety zone is available only for estimated payments made for the first tax year beginning on or after January 1, 2009.

27.2.f.1. This safety zone applies with relation to Taxpayers who filed as a component member of a composite tax return or group tax return filing unit, and as a component member of a unitary, or combined reporting group for the tax year immediately preceding the tax year beginning on or after January 1, 2009, and who will file separately as a component member of a unitary, or combined reporting group for the first tax year beginning on or after January 1, 2009..

27.2.f.2. For any entity that filed corporate net income tax as a component member of a composite tax return or group tax return, and as a component member of a unitary, or combined reporting group filing unit, and who will file separately as a component member of a unitary, or combined reporting group for the first tax year beginning on or after January 1, 2009:

27.2.f.3. If the previous tax year was a full 12 month tax year and

27.2.f.4. The amount of tax shown for the previous year has not been adjusted, redetermined or the subject of an assessment or other challenge by the Tax Commissioner, and

27.2.e.5. If the unitary or combined reporting group remains the same for the first tax year beginning on or after January 1, 2009 as the previous tax year, and

27.2.f.6. If total payments of estimated tax made by each installment date are at least equal to the amount which would have been required on that installment date if the estimated tax was determined based on the pro forma amount of tax that would have been shown on the pro forma previous year's West Virginia corporate net income tax return, determined on a recomputed separate filing basis for the Taxpayer and on a combined reporting basis, then this safety zone applies, except that:

27.2.f.7. If the annual return for the preceding year is not filed on or before the due date, including extensions of time to file, of the annual return for the preceding year, then the declaration of estimated tax for the current tax year cannot be based on last year's tax, and this safety zone does not apply.

27.2.f.8. If the preceding taxable year was a short year, estimated tax for the current year will be computed on an annualized basis. The requirements of paragraphs 27.2.f.4. through 27.2.f.7. must be met for the short year in order for this safety zone to apply. The annual tax payable for the current year and the estimated tax for the current year will not be reduced because the previous year was a short year.

APPENDIX B

FISCAL NOTE FOR PROPOSED RULES

Rule Title: Corporation Net Income Tax (110 CSR 24)

Type of Rule: __X__ Legislative ____ Interpretive ____ Procedural

Agency: State Tax Department

Address: 1001 Lee Street

Charleston, WV 25301

Phone Number: (304) 558-5330 Email: _____

Fiscal Note Summary

Summarize in a clear and concise manner what impact this measure will have on costs and revenues of state government.

The rule, as written, updates definitions used in the Corporation Net Income Tax Act and provides information on the procedures for taxpayers to file a combined return.

Fiscal Note Detail

Show over-all effect in Item 1 and 2 and, in Item 3, give an explanation of Breakdown by fiscal year, including long-range effect.

FISCAL YEAR			
Effect of Proposal	Current Increase/Decrease (use "-")	Next Increase/Decrease (use "-")	Fiscal Year (Upon Full Implementation)
1. Estimated Total Cost	$0	$90,000	$50,000
Personal Services	$0	$50,000	$50,000
Current Expenses	$0	$10,000	$0
Repairs & Alterations	$0	$0	$0
Assets	$0	$30,000	$0
Other	$0	$0	$0
2. Estimated Total Revenues	$0	$28,000,000	$24,000,000

Rule Title: Corporation Net Income Tax (110 CSR 24)

3. **Explanation of above estimates (including long-range effect):**
Please include any increase or decrease in fees in your estimated total revenues:

Based upon the experience of other states that have implemented "combined reporting," it is expected that tax revenue for the General Revenue Fund will increase by $24 million to $28 million per year. Additional administrative costs to the State Tax Department would be roughly $90,000 in the first year and roughly $50,000 per year each year thereafter. The additional costs would provide for the hiring of two additional auditors to assist in the review of the complicated tax returns expected as taxpayers file on a "combined" basis.

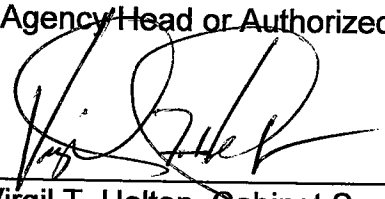
MEMORANDUM

Please identify any areas of vagueness, technical defects, reasons the proposed rule **would not** have a fiscal impact, and/or any special issues **not** captured elsewhere on this form.

The rule, as written, updates definitions used in the Corporation Net Income Tax Act and provides information on the procedures for taxpayers to file a combined return.

Date: _____

Signature of Agency Head or Authorized Representative:



Virgil T. Helton, Cabinet Secretary
West Virginia Department of Revenue