Reed Smith Teleseminar Series

Combined Reporting in New York

Practical Advice to Handle Audit Issues

December 13, 2011

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The business of relationships.

Overview

- New York State Combination Law
  - ✓ NY Tax Law Sec. 211
  - ✓ Amended effective January 1, 2007
- New York City Combination Law
  - ✓ NYC Admin. Code Sec. 11-605
  - ✓ Conformity, amended effective January 1, 2009

Combination
Tax Years Before
January 1, 2007 (NY)
January 1, 2009 (NYC)

Requirements

- Ownership
  - ✓ 80%
- Unitary Business
  - ✓ *British Land*
- Distortion
  - ✓ SIT = presumption of distortion
  - ✓ *Hallmark* – had SIT but rebutted presumption. Held: no combination
  - ✓ *Kellwood* – Most recent decision
  - ✓ Burden of proof

Rebutting Presumption of Distortion

- Step 1: Merit tax respect

(a.k.a. economic substance doctrine or sham transaction analysis)

- ✓ Objective Substance
  - Reasonable opportunity for economic profit exclusive of tax benefits
- ✓ Subjective Purpose
  - Standard: Transaction entered into for valid, non-tax, business purpose(s)

- Step 2: Arm's Length
  - ✓ 482 analysis (battle of experts)

Combination
Tax Years Beginning
On or After
January 1, 2007 (NY)
January 1, 2009 (NYC)

Requirements

- Ownership – No change
- Unitary – Regulatory requirement
  - ✓ Constitutional
- SIT – TSB-M-08(2)C (3/3/08)
  - ✓ Substantial incorporate receipts
  - ✓ Substantial intercorporate expenditures
  - ✓ Substantial intercorporate asset transfers
  - ✓ 10-step analysis

Discretionary Authority

- NY Tax Law Sec. 211.4(a)(4) provides:

  Except as provided in the first undesignated paragraph of this paragraph, no combined report covering any corporation shall be required unless the commissioner deems such a report necessary, because of inter-company transactions or some agreement, understanding, arrangement or transaction referred to in subdivision five of this section, in order properly to reflect the tax liability under this article.

Impact

	Old Law	New Law
SIT & no distortion	**No Combination** ▪Rebut presumption ▪Discretionary Auth	**Combination** ▪De facto distortion
SIT & actual distortion	**Combination**	**Combination** ▪De facto distortion
No SIT & no distortion	**No Combination** ▪No presumption ▪Discretionary Auth	**No Combination** ▪Discretionary Auth
No SIT & actual distortion	**Combination** ▪No presumption ▪Discretionary Auth	**Combination** ▪Discretionary Auth

Audit Issues

Discretionary Authority

- No SIT, distortion, combination
  - ✓ *InterAudi Bank*
  - ✓ *Heidelberg Eastern*
- SIT, distortion, combination
  - ✓ *Campbell Sales*
  - ✓ *Sherwin-Williams*
  - ✓ *Kellwood*
- SIT, no distortion, no combination
  - ✓ *Kellwood*
  - ✓ *Hallmark*
  - ✓ *Silver King Broadcasting*

Discretionary Authority Cont.

- Impact of old combination cases on new law
  - ✓ *InterAudi Bank*
  - ✓ *Hallmark*
  - ✓ *Kellwood*
- Other discretionary relief
  - ✓ Apportionment
  - ✓ Tax base
  - ✓ N.Y. Tax Law Sec. 211.5

Discretionary Authority

- NY Tax Law Sec. 211.5 provides:

  In case it shall appear to the tax commission that any agreement, understanding or arrangement exists between the taxpayer and any other corporation or any person or firm, whereby the activity, business, income or capital of the taxpayer within the state is improperly or inaccurately reflected, the tax commission is authorized and empowered, in its discretion and in such manner as it may determine, to **adjust items of income, deductions and capital, and to eliminate assets in computing any allocation percentage provided only that any income directly traceable thereto be also excluded from entire net income**, minimum taxable income or pre-nineteen hundred ninety minimum taxable income, so as equitably to determine tax.

Decombination

- *Panavision*
- Add back v. combination
  - ✓ Priority
  - ✓ Add back in SIT analysis
- Recent Audit Activity

Other Issues

- Procedure
  - ✓ *American Banknote*
  - ✓ *Autotote*
- Apportionment
  - ✓ *Disney*
  - ✓ Other business receipts

Other Issues

- Tax Base
  - ✓ *Bausch & Lomb*
  - ✓ *Bankers Trust* – beneficial ownership
- Subsidiary Capital Base
  - ✓ Reduction of base
  - ✓ Elected formulary method
- Investment Income
  - ✓ Unconstitutional – USSCT in *MeadWestvaco*?
  - ✓ Net operating loss allocation

Conclusion

- Refund opportunities
  - ✓ Assessment of requirements and tax impact
- Audit risk
  - ✓ Reserves
- Ongoing audit
  - ✓ Settlement v. Appeal

Authorities

- NY Tax Law Sec. 211
- NYC Admin. Code Sec. 11-605
- *Campbell Sales Company v. NY State Tax Commission*, 505 N.Y.S.2d 54 (N.Y. 1986).
- *Matter of Autotote Limted*, Division of Tax Appeals, Tax Appeals Tribunal,, DTA No. TSB-D-90(4)C (1990).
- *Matter of British Land (Maryland), Inc.* Division of Tax Appeals, Tax Appeals Tribunal,, DTA No. 806894 (1992), *rev'd on other grounds*, *British Land (Maryland), Inc. v. Tax App. Trib.*, 647 N.E.2d 1280 (N.Y. 1995).
- *Matter of Heidelberg Easter, Inc.,* Division of Tax Appeals, ALJ, DTA No. 806890 & 807829 (1993).
- *Matter of British Land (Maryland), Inc. v. Tax Appeals Tribunal*, 623 N.Y.S.2d 772 (N.Y. 1995).
- *Matter of Silver King Broadcasting of N.J.,* Division of Tax Appeals, Tax Appeals Tribunal,, DTA No. 812589 (1996).
- *Matter of Sherwin-Williams v. Tax Appeals Trib.*, 12 A.D.3d 112 (N.Y. App. Div. 2004), *lv. Denied* 4 N.Y.3d 709 (N.Y. 2005).

Authorities

- *Matter of Panavision, Inc.*, Division of Tax Appeals, Tax Appeals Tribunal,, DTA No. 816660 (2002).
- *Hallmark Marketing Corporation*, Division of Tax Appeals, ALJ, DTA No. 819956 (2007).
- Matter of Bausch & Lomb, Division of Tax Appeals, Tax Appeals Tribunal,, DTA No. 819883 (2007).
- TSB-M-08(2)C (3/3/08)
- *Matter of Disney Enterprises, Inc. v. Tax Appeal Tribunal*, 859 N.Y.S2d 87 (N.Y. 2008)
- *MeadWestvaco Corp. v. Ill. Dep't of Revenue*, 553 U.S. 16 (2008).
- *Matter of Bankers Trust Corp.*, NYC Tax Appeals Tribunal, TAT (E)04-36(BT) (4/8/10).
- *Matter of American Banknote Corporation*, NYC Tax Appeals Tribunal, TAT (E)03-31(GC), TAT (E)03-32(GC), TAT (E)03-33(GC) (2010)
- *Interaudi Bank (USA)*, Division of Tax Appeals, Tax Appeals Tribunal, DTA No. 821659 (2011).
- *Matter of Kellwood Company*, DTA No. 820915, Division of Tax Appeals, TAT (9/22/11).

Questions or Comments

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