Representative John Dougall proposes the following substitute bill:

APPORTIONMENT OF BUSINESS INCOME AND DEDUCTION OF NET LOSSES BY AN ACQUIRED CORPORATION

2008 GENERAL SESSION

STATE OF UTAH

Chief Sponsor: Wayne L. Niederhauser

House Sponsor: John Dougall

LONG TITLE

General Description:

This bill amends the Corporate Franchise and Income Taxes chapter and the Individual Income Tax Act relating to the apportionment of business income and the calculation of a net loss deduction by an acquired corporation.

Highlighted Provisions:

This bill:

- addresses the calculation of a net loss deduction by an acquired corporation;
- for purposes of apportionment of business income, addresses the circumstances under which certain receipts, rents, royalties, or sales are considered to be in this state;
- addresses the apportionment of business income for purposes of the individual income tax; and
- makes technical changes.

Monies Appropriated in this Bill:

None

Other Special Clauses:

This bill provides an effective date.

Utah Code Sections Affected:

AMENDS:

59-7-110, as last amended by Laws of Utah 1994, Chapter 83

59-7-319, as last amended by Laws of Utah 1992, Chapter 165

59-10-118, as last amended by Laws of Utah 1995, Chapter 311

Be it enacted by the Legislature of the state of Utah:

Section 1. Section **59-7-110** is amended to read:

59-7-110. Utah net losses -- Carryforwards and carrybacks.

(1) The amount of Utah net loss which shall be carried back or forward to offset income of another taxable year shall be determined as provided in this section.

(2) (a) A Utah net loss from a taxable year beginning before January 1, 1994, shall be carried back three taxable years preceding the taxable year of the loss and any remaining loss shall be carried forward five taxable years following the taxable year of the loss, subject to the limitations of this section.

(b) A Utah net loss from a taxable year beginning on or after January 1, 1994, may be carried back three taxable years preceding the taxable year of the loss and carried forward 15 taxable years following the taxable year of the loss, subject to the limitations of this section. If an election is made to forego the federal net operating loss carryback, the Utah net loss is not eligible to be carried back unless an election is made for state purposes.

(3) The Utah net loss shall be carried to the earliest eligible year for which the Utah taxable income before net loss deduction, minus Utah net losses from previous years which were applied or required to be applied to offset income, is not less than zero.

(4) (a) Except as provided in Subsection (4)(a)(iii), the amount of Utah net loss which shall be carried to the year identified in Subsection (3) shall be the lesser of:

(i) the remaining Utah net loss after deduction of any amounts of such loss which were carried to previous years; or

(ii) the remaining Utah taxable income before net loss deduction of the year identified in Subsection (3) after deduction of Utah net losses from previous years which were carried or required to be carried to such year; and

(iii) in any event, the amount carried back from a taxable year beginning on or after January 1, 1994, may not exceed $1,000,000 in Utah taxable income for each corporate return filed in a taxable year; any losses in excess of $1,000,000 may be carried forward; and

(b) any remaining Utah net loss shall be available to be carried to one or more taxable years in accordance with this section.

(5) (a) Corporations acquiring the assets or stock of another corporation may not deduct any net loss incurred by the acquired corporation prior to the date of acquisition. This subsection does not apply if the only change in the corporation is that of the state of incorporation.

(b) An acquired corporation may deduct its net losses incurred before the date of acquisition against its separate income as calculated under Subsection (6) if the acquired corporation has continued to carry on a trade or business substantially the same as that conducted before such acquisition.

(6) For purposes of Subsection (5)(b), the amount of net loss an acquired corporation that is acquired by a unitary group may deduct is calculated by:

(a) subject to Subsection (6)(e), calculating the sum of:

(i) an amount determined by dividing the average value of the acquired corporation's real and tangible personal property owned or rented and used in this state during the taxable year by the average value of all of the unitary group's real and tangible personal property owned or rented and used during the taxable year;

(ii) an amount determined by dividing the total amount paid in this state during the taxable year by the acquired corporation for compensation by the total compensation paid everywhere by the unitary group during the taxable year; and

(iii) an amount determined by:

(A) dividing the total sales of the acquired corporation in this state during the taxable year by the total sales of the unitary group everywhere during the taxable year; and

(B) if the unitary group elects to apportion business income to this state using the method described in Subsection 59-7-311(2)(b), multiplying the amount calculated under Subsection (6)(a)(iii)(A) by two;

(b) dividing the amount calculated under Subsection (6)(a) by the denominator of the fraction for the unitary group to apportion business income to this state using the same election for calculating that denominator that the unitary group uses:

(i) for that taxable year; and

(ii) in accordance with Section 59-7-311;

(c) multiplying the amount calculated under Subsection (6)(b) by the business income of the unitary group for the taxable year that is subject to apportionment under Section 59-7-311; and

(d) calculating the sum of:

(i) the amount calculated under Subsection (6)(c); and

(ii) the following amounts allocable to the acquired corporation for the taxable year:

(A) nonbusiness income allocable to this state; or

(B) nonbusiness loss allocable to this state.

(e) The amounts calculated under Subsection (6)(a) shall be derived in the same manner as those amounts are derived for purposes of apportioning the unitary group's business income before deducting the net loss, including a modification made in accordance with Section 59-7-320.

Section 2. Section **59-7-319** is amended to read:

59-7-319. Receipt, rent, royalty, or sale in connection with other than tangible personal property -- When considered to be in this state.

[~~(1) Sales, other than sales of tangible personal property, are in this state if:~~]

[~~(a) the income-producing activity is performed in this state; or~~]

[~~(b) 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.~~]

(1) (a) Subject to Subsection (1)(b), as used in this section, "regulated investment company" is as defined in Section 851(a), Internal Revenue Code, in effect for the taxable year.

(b) "Regulated investment company" includes a trustee or sponsor of an employee benefit plan that has an account in a regulated investment company.

(2) The following are considered to be in this state:

(a) a rent in connection with real property if the real property is in this state;

(b) a royalty in connection with real property if the real property is in this state;

(c) a sale in connection with real property if the real property is in this state; or

(d) other income in connection with real property if the real property is in this state.

(3) (a) Subject to Subsection (3)(b), a receipt from the performance of a service is considered to be in this state if the purchaser of the service receives a greater benefit of the service in this state than in any other state.

(b) In accordance with Title 63, Chapter 46a, Utah Administrative Rulemaking Act, the commission may by rule prescribe the circumstances under which a purchaser of a service receives a greater benefit of the service in this state than in any other state.

(4) (a) Subject to Subsection (4)(b), a receipt in connection with intangible property is considered to be in this state if the intangible property is used in this state.

(b) If the intangible property described in Subsection (4)(a) is used in this state and outside this state, a receipt in connection with the intangible property shall be apportioned to this state in accordance with Subsection (4)(c).

(c) For purposes of Subsection (4)(b), for a taxable year the percentage of a receipt in connection with intangible property that is considered to be in this state is the percentage of the use of the intangible property that occurs in this state during the taxable year.

[~~(2)~~] (5) (a) Notwithstanding [~~Subsection (1), sales, other than sales~~] Subsections (2) through (4), a sale, other than a sale of tangible personal property, derived, directly or indirectly, from the sale of management, distribution, or administration services to, or on behalf of a regulated investment company, [~~as defined in Section 851(a) of the Internal Revenue Code of 1986, including trustees or sponsors of employee benefit plans which have accounts in a regulated investment company, shall be assigned to~~] is considered to be in this state:

(i) to the extent that shareholders of the regulated investment company are domiciled in the state [~~as follows: (a) by multiplying~~]; and

(ii) as provided in this Subsection (5).

(b) For purposes of Subsection (5)(a), the amount of a sale, other than a sale of tangible personal property, that is considered to be in this state is calculated by determining the product of:

(i) the taxpayer's total dollar amount of sales of [~~such~~] the services [~~by~~]; and

(ii) a fraction, the numerator of which is the average of the sum of the beginning of the year and the end of year balance of shares owned by the investment company shareholders domiciled in this state[~~;~~] and the denominator of which is the average of the sum of the beginning of the year and end of year balance of shares owned by the investment company shareholders.

[~~(b)~~] (c) A separate computation shall be made to determine the sales for each investment company.

[~~(3)~~] (6) (a) Notwithstanding [~~Subsection (1)~~] Subsections (2) through (4) and subject to Subsection (6)(b), the following sales [~~shall be assigned to the~~] are considered to be in this state to the extent that customers of a securities brokerage business are domiciled in the state:

(i) [~~sales, other than sales~~] a sale, other than a sale of tangible personal property, derived, directly or indirectly, from the sale of a securities brokerage [~~services~~] service by a taxpayer [~~which in this state is~~] if that taxpayer is primarily engaged in providing [~~services~~] a service in this state to a regulated investment company [~~as described in Subsection (2)~~]; or

(ii) [~~sales, other than sales~~] a sale, other than a sale of tangible personal property, derived, directly or indirectly, from the sale of a securities brokerage [~~services~~] service by a taxpayer [~~which~~] that is an affiliate of a taxpayer [~~which, in this state,~~] that provides [~~services~~] a service in this state to a regulated investment company [~~as described in Subsection (2)~~].

[~~(b) This assignment of sales shall be determined as follows: by multiplying~~]

(b) For purposes of Subsection (6)(a), the amount of a sale, other than a sale of tangible personal property, that is considered to be in this state is calculated by determining the product of:

(i) the taxpayer's total dollar amount of sales of securities brokerage services [~~by~~]; and

(ii) a fraction, the numerator of which is the receipts from securities brokerage services from customers of the taxpayer domiciled in this state, and the denominator of which is the receipts from securities brokerage services from all customers of the taxpayer.

Section 3. Section **59-10-118** is amended to read:

59-10-118. Division of income for tax purposes.

(1) As used in this section [~~unless the context otherwise requires~~]:

(a) "Business income" means income arising from transactions and activity in the regular course of [~~the~~] a taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, management, and disposition of the property constitutes integral parts of the taxpayer's regular trade or business operations.

(b) "Commercial domicile" means the principal place from which the trade or business of [~~the~~] a taxpayer is directed or managed.

[~~(c) "Compensation" means wages, salaries, commissions, and any other form of remuneration paid to employee for personal services.~~]

[~~(d)~~] (c) "Nonbusiness income" means all income other than business income.

[~~(e)~~] (d) "Sales" means all gross receipts of [~~the~~] a taxpayer not allocated under Subsections (3) through (7).

[~~(f)~~] (e) "State" means any state of the United States, the District of Columbia, the commonwealth of Puerto Rico, [~~and~~] or any possession of the United States.

(2) [~~Any~~] A taxpayer having business income [~~which~~] that is taxable both within and without this state, shall allocate and apportion [~~his~~] the taxpayer's net income as provided in this section.

(3) Rents and royalties from real or tangible personal property, capital gains, interest, dividends, or patent or copyright royalties, to the extent that they constitute nonbusiness income, shall be allocated as provided in Subsections (4) through (7).

(4) (a) Net rents and royalties from real property located in this state are allocable to this state.

(b) Net rents and royalties from tangible personal property are allocable to this state:

(i) if and to the extent that the property is utilized in this state; or

(ii) in their entirety if the taxpayer's commercial domicile is in this state and the taxpayer is not organized under the laws of or taxable in the state in which the property is utilized.

(c) 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.

(5) (a) Capital gains and losses from sales of real property located in this state are allocable to this state.

(b) Capital gains and losses from sales of tangible personal property are allocable to this state if:

(i) the property [~~had~~] has a situs in this state at the time of the sale; or

(ii) the taxpayer's commercial domicile is in this state and the taxpayer is not taxable in the state in which the property had a situs.

(c) Capital gains and losses from sales of intangible personal property are allocable to this state if the taxpayer's commercial domicile is in this state.

(6) Interest and dividends are allocable to this state if the taxpayer's commercial domicile is in this state.

(7) (a) Patent and copyright royalties are allocable to this state:

(i) if and to the extent that the patent or copyright is utilized by the payer in this state; or

(ii) if and to the extent that the patent or copyright is utilized by the payer in a state in which the taxpayer is not taxable and the taxpayer's commercial domicile is in this state.

(b) A patent is utilized in a state to the extent that it is employed in production, fabrication, manufacturing, or other processing in the state or to the extent that a patented product is produced in the state. If the basis of receipts from patent royalties does not permit allocation to states or if the accounting procedures do not reflect states of utilization, the patent is utilized in the state in which the taxpayer's commercial domicile is located.

(8) All business income shall be apportioned to this state [~~by multiplying the income by a fraction, the numerator of which is the property factor plus the payroll factor plus the sales factor, and the denominator of which is three~~] using the same methods, procedures, and requirements of Sections 59-7-311 through 59-7-320.

[~~(9) 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 in this state during the tax period and the denominator of which is the average value of all the taxpayer's real and tangible personal property owned or rented and used during the tax period.~~]

[~~(10) Property owned by the taxpayer is valued at its original cost. Property rented by the taxpayer is valued at eight times the net annual rental rate. Net annual rental rate is the annual rental rate paid by the taxpayer less any annual rental rate received by the taxpayer from subrentals.~~]

[~~(11) The average value of property shall be determined by averaging the values at the beginning and ending of the tax period but the commission may require the averaging of monthly values during the tax period, if reasonably required to reflect properly the average value of the taxpayer's property.~~]

[~~(12) The payroll factor is a fraction, the numerator of which is the total amount paid in this state during the tax period by the taxpayer for compensation, and the denominator of which is the total compensation paid everywhere during the tax period.~~]

[~~(13) Compensation is paid in this state if:~~]

[~~(a) the individual's service is performed entirely within the state; or~~]

[~~(b) the individual's service is performed both within and without the state, but the service performed without the state is incidental to the individual's service within the state; or~~]

[~~(c) some of the service is performed in the state and:~~]

[~~(i) the base of operations or, if there is no base of operations, the place from which the service is directed or controlled is in the state; or~~]

[~~(ii) 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 individual's residence is in this state.~~]

[~~(14) The sales factor is a fraction, the numerator of which is the total sales of the taxpayer in this state during the tax period, and the denominator of which is the total sales of the taxpayer everywhere during the tax period.~~]

[~~(15) Sales of tangible personal property are in this state if the property is delivered or shipped to a purchaser within this state regardless of the f.o.b. point or other conditions of the sale.~~]

[~~(16) Sales, other than sales of tangible personal property, are in this state if:~~]

[~~(a) the income-producing activity is performed in this state; or~~]

[~~(b) 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.~~]

[~~(17) If the allocation and apportionment provisions of this chapter do not fairly represent the extent of the taxpayer's business activity in this state, the taxpayer may petition for or the commission may require, in respect of all or any part of the taxpayer's business~~

~~activity, if reasonable:~~]

[~~(a) separate accounting;~~]

[~~(b) the exclusion of any one or more of the factors;~~]

[~~(c) the inclusion of one or more additional factors which will fairly represent the taxpayer's business activity in this state; or~~]

[~~(d) the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.~~]

Section 4. **Effective date.**

(1) Except as provided in Subsection (2), this bill takes effect for taxable years beginning on or after January 1, 2009.

(2) The amendments to Section 59-7-110 have retrospective operation for taxable years beginning on or after January 1, 2008.

Fiscal Note

S.B. 136 1st Sub. (Green) - Apportionment of Business Income and Deduction of Net Losses by an Acquired Corporation

2008 General Session

State of Utah

State Impact

Due to the net loss an acquired corporation may deduct against tax liability, enactment of this bill is likely to lead to a loss in revenue to the Uniform School Fund. The magnitude of the loss to the Uniform School Fund is unknown.

Individual, Business and/or Local Impact

Individuals or businesses in Utah that perform certain financial services out-of-state are likely to benefit, whereas individuals or businesses that reside elsewhere but perform certain financial services consumed in Utah are likely to see some increase in individual tax liability. In addition, the bill addresses the amount of net loss an acquired corporation may deduct against tax liability. Individuals and businesses involved in acquisitions may benefit.