

CORPORATE FRANCHISE AND INCOME TAX AMENDMENTS

2011 GENERAL SESSION

STATE OF UTAH

Chief Sponsor: J. Stuart Adams

House Sponsor: Todd E. Kiser

LONG TITLE

General Description:

This bill amends provisions related to corporate franchise and income taxes.

Highlighted Provisions:

This bill:

- ▶ amends the definition of "common ownership" for purposes of corporate franchise and income taxes;

- ▶ repeals provisions related to certain distributions by corporations from depletion reserves;

- ▶ addresses the circumstances under which certain receipts, rents, royalties, or sales are considered to be in this state;

- ▶ addresses intercompany transactions for purposes of apportionment of income to the state; and

- ▶ makes technical and conforming changes.

Money Appropriated in this Bill:

None

Other Special Clauses:

This bill has retrospective operation for a taxable year beginning on or after January 1, 2011.

Utah Code Sections Affected:

AMENDS:

59-7-101, as last amended by Laws of Utah 2010, Chapter 198

59-7-108, as repealed and reenacted by Laws of Utah 1993, Chapter 169

30 **59-7-319**, as last amended by Laws of Utah 2008, Chapters 105 and 283

31 **59-7-404.5**, as enacted by Laws of Utah 1994, Chapter 83



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

34 Section 1. Section **59-7-101** is amended to read:

35 **59-7-101. Definitions.**

36 As used in this chapter:

37 (1) "Adjusted income" means unadjusted income as modified by Sections 59-7-105
38 and 59-7-106.

39 (2) (a) "Affiliated group" means one or more chains of corporations that are connected
40 through stock ownership with a common parent corporation that meet the following
41 requirements:

42 (i) at least 80% of the stock of each of the corporations in the group, excluding the
43 common parent corporation, is owned by one or more of the other corporations in the group;
44 and

45 (ii) the common parent directly owns at least 80% of the stock of at least one of the
46 corporations in the group.

47 (b) "Affiliated group" does not include corporations that are qualified to do business
48 but are not otherwise doing business in this state.

49 (c) For purposes of this Subsection (2), "stock" does not include nonvoting stock which
50 is limited and preferred as to dividends.

51 (3) "Apportionable income" means adjusted income less nonbusiness income net of
52 related expenses, to the extent included in adjusted income.

53 (4) "Apportioned income" means apportionable income multiplied by the
54 apportionment fraction as determined in Section 59-7-311.

55 (5) "Business income" is as defined in Section 59-7-302.

56 (6) (a) "Captive real estate investment trust" means a real estate investment trust if:

57 (i) the shares or beneficial interests of the real estate investment trust are not regularly

58 traded on an established securities market; and

59 (ii) more than 50% of the voting power or value of the shares or beneficial interests of
60 the real estate investment trust are directly, indirectly, or constructively:

61 (A) owned by a controlling entity of the real estate investment trust; or

62 (B) controlled by a controlling entity of the real estate investment trust.

63 (b) In accordance with Title 63G, Chapter 3, Utah Administrative Rulemaking Act, the
64 commission may make rules defining "established securities market."

65 (7) (a) "Common ownership" means the direct or indirect control or ownership of more
66 than 50% of the outstanding voting stock of:

67 (i) a parent-subsidary controlled group as defined in Section 1563, Internal Revenue
68 Code, except that 50% shall be substituted for 80%;

69 (ii) a brother-sister controlled group as defined in Section 1563, Internal Revenue
70 Code~~[-, except that 50% shall be substituted for 80%];~~ or

71 (iii) three or more corporations each of which is a member of a group of corporations
72 described in Subsection (2)(a)(i) or (ii), and one of which is:

73 (A) a common parent corporation included in a group of corporations described in
74 Subsection (2)(a)(i); and

75 (B) included in a group of corporations described in Subsection (2)(a)(ii).

76 (b) Ownership of outstanding voting stock shall be determined by Section 1563,
77 Internal Revenue Code.

78 (8) (a) "Controlling entity of a captive real estate investment trust" means an entity
79 that:

80 (i) is treated as an association taxable as a corporation under the Internal Revenue
81 Code;

82 (ii) is not exempt from federal income taxation under Section 501(a), Internal Revenue
83 Code; and

84 (iii) directly, indirectly, or constructively holds more than 50% of:

85 (A) the voting power of a captive real estate investment trust; or

86 (B) the value of the shares or beneficial interests of a captive real estate investment
87 trust.

88 (b) "Controlling entity of a captive real estate investment trust" does not include:

89 (i) a real estate investment trust, except for a captive real estate investment trust;

90 (ii) a qualified real estate investment subsidiary described in Section 856(i), Internal
91 Revenue Code, except for a qualified real estate investment trust subsidiary of a captive real
92 estate investment trust; or

93 (iii) a foreign real estate investment trust.

94 (c) In accordance with Title 63G, Chapter 3, Utah Administrative Rulemaking Act, the
95 commission may make rules defining "established securities market."

96 (9) "Corporate return" or "return" includes a combined report.

97 (10) "Corporation" includes:

98 (a) entities defined as corporations under Sections 7701(a) and 7704, Internal Revenue
99 Code; and

100 (b) other organizations that are taxed as corporations for federal income tax purposes
101 under the Internal Revenue Code.

102 (11) "Dividend" means any distribution, including money or other type of property,
103 made by a corporation to its shareholders out of its earnings or profits accumulated after
104 December 31, 1930.

105 (12) (a) "Doing business" includes any transaction in the course of its business by a
106 domestic corporation, or by a foreign corporation qualified to do or doing intrastate business in
107 this state.

108 (b) Except as provided in Subsection 59-7-102(2), "doing business" includes:

109 (i) the right to do business through incorporation or qualification;

110 (ii) the owning, renting, or leasing of real or personal property within this state; and

111 (iii) the participation in joint ventures, working and operating agreements, the
112 performance of which takes place in this state.

113 (13) "Domestic corporation" means a corporation that is incorporated or organized

114 under the laws of this state.

115 (14) (a) "Farmers' cooperative" means an association, corporation, or other
116 organization that is:

117 (i) (A) an association, corporation, or other organization of:

118 (I) farmers; or

119 (II) fruit growers; or

120 (B) an association, corporation, or other organization that is similar to an association,
121 corporation, or organization described in Subsection (14)(a)(i)(A); and

122 (ii) organized and operated on a cooperative basis to:

123 (A) (I) market the products of members of the cooperative or the products of other
124 producers; and

125 (II) return to the members of the cooperative or other producers the proceeds of sales
126 less necessary marketing expenses on the basis of the quantity of the products of a member or
127 producer or the value of the products of a member or producer; or

128 (B) (I) purchase supplies and equipment for the use of members of the cooperative or
129 other persons; and

130 (II) turn over the supplies and equipment described in Subsection (14)(a)(ii)(B)(I) at
131 actual costs plus necessary expenses to the members of the cooperative or other persons.

132 (b) (i) Subject to Subsection (14)(b)(ii), for purposes of this Subsection (14), the
133 commission by rule, made in accordance with Title 63G, Chapter 3, Utah Administrative
134 Rulemaking Act, shall define:

135 (A) the terms:

136 (I) "member"; and

137 (II) "producer"; and

138 (B) what constitutes an association, corporation, or other organization that is similar to
139 an association, corporation, or organization described in Subsection (14)(a)(i)(A).

140 (ii) The rules made under this Subsection (14)(b) shall be consistent with the filing
141 requirements under federal law for a farmers' cooperative.

142 (15) "Foreign corporation" means a corporation that is not incorporated or organized
143 under the laws of this state.

144 (16) (a) "Foreign operating company" means a corporation if:

145 (i) the corporation is incorporated in the United States;

146 (ii) at least 80% of the corporation's business activity, as determined under Section
147 59-7-401, is conducted outside the United States; and

148 (iii) as calculated in accordance with Part 3, Allocation and Apportionment of Income -
149 Utah UDITPA Provisions, the corporation has:

150 (A) at least \$1,000,000 of payroll located outside the United States; and

151 (B) at least \$2,000,000 of property located outside the United States.

152 (b) "Foreign operating company" does not include a corporation that qualifies for the
153 Puerto Rico and possession tax credit as provided in Section 936, Internal Revenue Code.

154 (17) (a) "Foreign real estate investment trust" means:

155 (i) a business entity organized outside the laws of the United States if:

156 (A) at least 75% of the business entity's total asset value at the close of the business
157 entity's taxable year is represented by:

158 (I) real estate assets, as defined in Section 856(c)(5)(B), Internal Revenue Code;

159 (II) cash or cash equivalents; or

160 (III) one or more securities issued or guaranteed by the United States;

161 (B) the business entity is:

162 (I) not subject to income taxation:

163 (Aa) on amounts distributed to the business entity's beneficial owners; and

164 (Bb) in the jurisdiction in which the business entity is organized; or

165 (II) exempt from income taxation on an entity level in the jurisdiction in which the
166 business entity is organized;

167 (C) the business entity distributes at least 85% of the business entity's taxable income,
168 as computed in the jurisdiction in which the business entity is organized, to the holders of the
169 business entity's:

170 (I) shares or beneficial interests; and
171 (II) on an annual basis;
172 (D) (I) not more than 10% of the following is held directly, indirectly, or constructively
173 by a single person:
174 (Aa) the voting power of the business entity; or
175 (Bb) the value of the shares or beneficial interests of the business entity; or
176 (II) the shares of the business entity are regularly traded on an established securities
177 market; and
178 (E) the business entity is organized in a country that has a tax treaty with the United
179 States; or
180 (ii) a listed Australian property trust.
181 (b) In accordance with Title 63G, Chapter 3, Utah Administrative Rulemaking Act, the
182 commission may make rules defining:
183 (i) "cash or cash equivalents";
184 (ii) "established securities market"; or
185 (iii) "listed Australian property trust."
186 (18) "Income" includes losses.
187 (19) "Internal Revenue Code" means Title 26 of the United States Code as effective
188 during the year in which Utah taxable income is determined.
189 (20) "Nonbusiness income" is as defined in Section 59-7-302.
190 (21) "Real estate investment trust" is as defined in Section 856, Internal Revenue Code.
191 (22) "Related expenses" means:
192 (a) expenses directly attributable to nonbusiness income; and
193 (b) the portion of interest or other expense indirectly attributable to both nonbusiness
194 and business income which bears the same ratio to the aggregate amount of such interest or
195 other expense, determined without regard to this Subsection (22), as the average amount of the
196 asset producing the nonbusiness income bears to the average amount of all assets of the
197 taxpayer within the taxable year.

198 (23) "Safe harbor lease" means a lease that qualified as a safe harbor lease under
199 Section 168, Internal Revenue Code.

200 (24) "S corporation" means an S corporation as defined in Section 1361, Internal
201 Revenue Code.

202 (25) "State of the United States" includes any of the 50 states or the District of
203 Columbia.

204 (26) (a) "Taxable year" means the calendar year or the fiscal year ending during such
205 calendar year upon the basis of which the adjusted income is computed.

206 (b) In the case of a return made for a fractional part of a year under this chapter or
207 under rules prescribed by the commission, "taxable year" includes the period for which such
208 return is made.

209 (27) "Taxpayer" means any corporation subject to the tax imposed by this chapter.

210 (28) "Threshold level of business activity" means business activity in the United States
211 equal to or greater than 20% of the corporation's total business activity as determined under
212 Section 59-7-401.

213 (29) "Unadjusted income" means federal taxable income as determined on a separate
214 return basis before intercompany eliminations as determined by the Internal Revenue Code,
215 before the net operating loss deduction and special deductions for dividends received.

216 (30) (a) "Unitary group" means a group of corporations that:

217 (i) are related through common ownership; and

218 (ii) by a preponderance of the evidence as determined by a court of competent
219 jurisdiction or the commission, are economically interdependent with one another as
220 demonstrated by the following factors:

221 (A) centralized management;

222 (B) functional integration; and

223 (C) economies of scale.

224 (b) "Unitary group" includes a captive real estate investment trust.

225 (c) "Unitary group" does not include an S corporation.

226 (31) "United States" includes the 50 states and the District of Columbia.

227 (32) "Utah net loss" means the current year Utah taxable income before Utah net loss
228 deduction, if determined to be less than zero.

229 (33) "Utah net loss deduction" means the amount of Utah net losses from other taxable
230 years that may be carried back or carried forward to the current taxable year in accordance with
231 Section 59-7-110.

232 (34) (a) "Utah taxable income" means Utah taxable income before net loss deduction
233 less Utah net loss deduction.

234 (b) "Utah taxable income" includes income from tangible or intangible property located
235 or having situs in this state, regardless of whether carried on in intrastate, interstate, or foreign
236 commerce.

237 (35) "Utah taxable income before net loss deduction" means apportioned income plus
238 nonbusiness income allocable to Utah net of related expenses.

239 (36) (a) "Water's edge combined report" means a report combining the income and
240 activities of:

241 (i) all members of a unitary group that are:

242 (A) corporations organized or incorporated in the United States, including those
243 corporations qualifying for the Puerto Rico and Possession Tax Credit as provided in Section
244 936, Internal Revenue Code, in accordance with Subsection (36)(b); and

245 (B) corporations organized or incorporated outside of the United States meeting the
246 threshold level of business activity; and

247 (ii) an affiliated group electing to file a water's edge combined report under Subsection
248 59-7-402(2).

249 (b) There is a rebuttable presumption that a corporation which qualifies for the Puerto
250 Rico and possession tax credit provided in Section 936, Internal Revenue Code, is part of a
251 unitary group.

252 (37) "Worldwide combined report" means the combination of the income and activities
253 of all members of a unitary group irrespective of the country in which the corporations are

254 incorporated or conduct business activity.

255 Section 2. Section **59-7-108** is amended to read:

256 **59-7-108. Distributions by corporations.**

257 (1) (a) For ~~[the purpose]~~ purposes of this chapter, ~~[each]~~ a distribution is made out of
258 earnings or profits to the extent ~~[thereof]~~ of the earnings or profits, and from the most recently
259 accumulated earnings or profits. ~~[Any]~~

260 (b) (i) Subject to Subsection (1)(b)(ii), any earnings or profits accumulated or increase
261 in value of property accrued before January 1, 1931, may be excluded from taxable income
262 after the earnings and profits accumulated after December 31, 1930 have been distributed~~[, but~~
263 ~~any such]~~.

264 (ii) A distribution described in Subsection (1)(b)(i) shall be applied against and reduce
265 the basis of the stock.

266 (2) ~~[F]~~ (a) Subject to Subsection (2)(b), if any distribution [which] that is not in partial
267 or complete liquidation is made by a corporation to its shareholders, is not out of increase in
268 value of property accrued before January 1, 1931, and is not out of earnings or profits, [then]
269 the amount of [such] the distribution shall be applied against and reduce the basis of the stock.

270 (b) If [the] a distribution described in Subsection (2)(a) is in excess of [such] the basis
271 of the stock, the excess shall be treated as a gain from the sale or exchange of property. [The
272 provisions of this subsection also apply to distributions from depletion reserves based on
273 percentage depletion allowed by this chapter.]

274 Section 3. Section **59-7-319** is amended to read:

275 **59-7-319. Circumstances under which a receipt, rent, royalty, or sale is**
276 **considered to be in this state.**

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

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

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

282 (a) a rent in connection with;
283 (i) real property if the real property is in this state; or
284 (ii) tangible personal property if the tangible personal property is in this state;
285 (b) a royalty in connection with real property if the real property is in this state;
286 (c) a sale in connection with real property if the real property is in this state; or
287 (d) other income in connection with real property or tangible personal property if the
288 real property or tangible personal property is in this state.

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

292 (b) In accordance with Title 63G, Chapter 3, Utah Administrative Rulemaking Act, the
293 commission may by rule prescribe the circumstances under which a purchaser of a service
294 receives a greater benefit of the service in this state than in any other state.

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

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

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

303 (5) (a) Notwithstanding Subsections (2) through (4), a sale, other than a sale of tangible
304 personal property, derived, directly or indirectly, from the sale of management, distribution, or
305 administration services to, or on behalf of a regulated investment company, is considered to be
306 in this state:

307 (i) to the extent that shareholders of the regulated investment company are domiciled in
308 the state; and

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

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

313 (i) the taxpayer's total dollar amount of sales of the services; and

314 (ii) a fraction, the numerator of which is the average of the sum of the beginning of the
315 year and the end of year balance of shares owned by the investment company shareholders
316 domiciled in this state and the denominator of which is the average of the sum of the beginning
317 of the year and end of year balance of shares owned by the investment company shareholders.

318 (c) A separate computation shall be made to determine the sales for each investment
319 company.

320 (6) (a) Notwithstanding Subsections (2) through (4) and subject to Subsection (6)(b),
321 the following sales are considered to be in this state to the extent that customers of a securities
322 brokerage business are domiciled in the state:

323 (i) a sale, other than a sale of tangible personal property, derived, directly or indirectly,
324 from the sale of a securities brokerage service by a taxpayer if that taxpayer is primarily
325 engaged in providing a service in this state to a regulated investment company; or

326 (ii) a sale, other than a sale of tangible personal property, derived, directly or indirectly,
327 from the sale of a securities brokerage service by a taxpayer that is an affiliate of a taxpayer
328 that provides a service in this state to a regulated investment company.

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

332 (i) the taxpayer's total dollar amount of sales of securities brokerage services; and

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

336 (7) Whether sales by an airline, other than sales of tangible personal property, are in
337 this state is determined as provided in this section, subject to the calculation required by

338 Subsection 59-7-317(2).

339 Section 4. Section **59-7-404.5** is amended to read:

340 **59-7-404.5. Adjustment to apportionment factors for corporations in a combined**
341 **report -- Sales factor -- Property factor.**

342 For purposes of [the] apportionment [sections] under Part 3 [of this chapter], Allocation
343 and Apportionment of Income - Utah UDITPA Provisions:

344 (1) [~~Corporations~~] corporations filing a combined report under Section 59-7-402 or
345 59-7-403 may not include intercompany sales or other intercompany transactions between the
346 corporations included in the combined report [~~when~~] in determining the sales factor[-]; and

347 [~~(2) Intercompany rents between members of a combined report may not be considered~~
348 ~~in the computation of the property factor.]~~

349 (2) corporations filing a combined report under Section 59-7-402 or 59-7-403 may not
350 include intercompany rents or other intercompany transactions between the corporations
351 included in the combined report in determining the property factor.

352 Section 5. **Retrospective operation.**

353 This bill has retrospective operation for a taxable year beginning on or after January 1,
354 2011.