

## State Tax Observations

# New York Combined Return Rules Begin to Gain Clarity

By Sandy Weinberg, Principal and Jill Cantor, Manager

In the last 30 years, perhaps the most contentious New York corporate tax issue centered on which entities should be included in a New York combined return. The confusion around the “distortion” test served as a full-time job for practitioners and state and city tax auditors and attorneys. That all changed radically in 2015 with New York State’s corporate tax reform legislation that included the adoption of mandatory unitary combined group reporting.

Under the legislation, combined reporting is required if the taxpayer is engaged in a unitary business and one of three 50% common ownership tests is met. New York City conformed to the State’s legislation during 2015 for years beginning on or after January 1, 2015.

The due date for 2016 New York combined returns (and separate filing corporations) with a calendar year end is April 15, 2017.

### Frequently Asked Questions (FAQs) and Draft Combined Return Regulations

In 2017, the New York State Department of Taxation and Finance (the “Department”) is expected to promulgate final combined filing regulations. The regulations should also address other aspects of the corporate tax reform including discretionary adjustments and the new customer-based sourcing provisions. These regulations were issued in draft in 2016.

Also, in January 2017 the Department updated its Frequently Asked Questions (FAQs) with respect to the combined returns.

### Mandatory Combined Filing - Where Do Things Stand Now?

First, when the regulations are promulgated, they should reflect that a unitary business has “a flow of value as evidenced by functional integration, centralized management and economies of scale.”

Further, in the following situations, a unitary business relationship is presumed when corporations:

- Are engaged in the same general line of business (horizontal integration)
- Are engaged in different steps in a vertically structured enterprise (vertical integration)
- Have a strong centralized management; or
- Are newly formed or, in certain circumstances, newly acquired (a.k.a. “instant unity”).

What about passive holding companies? If a passive holding company and one or more operating companies satisfies the 50% voting power test, the passive holding company is “deemed” to be engaged in a unitary business with the operating company/companies.

Issues have been raised as far as non-U.S. corporations (called “alien” corporations by New York). The proposed regulations make clear that a unitary combined group includes an alien corporation that has effectively connected income regardless of any federal treaty protections.

Can non-unitary companies be included in a combined report? Yes, but with limitations. Specifically, taxpayers are permitted to elect to include all the members of its commonly owned group in a single return, regardless of whether the members establish a unitary relationship. The election must be made on an original timely filed return of the combined group and is irrevocable for seven years. At the end of the seven-year period, the election automatically renews for another seven years unless revoked.

### **Extensions of Time**

With respect to extensions of time, the new FAQs set forth that generally one Form CT-5.3 should be filed for all corporations included in the combined group. However, each corporation being added to an existing group must also file a separate Form CT-5 to extend the first period it is included in the combined group. A separate Form CT-5 must also be filed by a corporation to extend the short period beginning immediately prior to the date it joined the group.

### **Contact Us**

If you have any questions regarding New York State or City's combined return rules, contact Sandy Weinberg at [sweinberg@pkfod.com](mailto:sweinberg@pkfod.com) or Jill Cantor at [jcantor@pkfod.com](mailto:jcantor@pkfod.com).

### **About PKF O'Connor Davies**

PKF O'Connor Davies, LLP is a full-service certified public accounting and advisory firm with a long history of serving clients both domestically and internationally. With roots tracing to 1891, nine offices in New York, New Jersey, Connecticut and Maryland, and more than 600 professionals led by 100 partners, the Firm provides a complete range of accounting, auditing, tax and management advisory services. PKF O'Connor Davies is ranked number 26 on Accounting Today's 2016 "Top 100 Firms" list and is recognized as one of the "Top 10 Fastest-Growing Firms." PKF O'Connor Davies is also recognized as a "Leader in Audit and Accounting" and is ranked among the "Top Firms in the Mid-Atlantic," by Accounting Today. In 2016, PKF O'Connor Davies was named one of the 50 best accounting employers to work for in North America, by Vault. The Firm is the 11th largest accounting firm in the New York Metropolitan area, according to Crain's New York Business.

PKF O'Connor Davies is the lead North American representative in PKF International, a global network of legally independent accounting and advisory firms located in 440 locations, in 150 countries around the world.

Our Firm provides the information in this e-newsletter for general guidance only, and it does not constitute the provision of legal advice, tax advice, accounting services, or professional consulting of any kind.