

ARIZONA CORPORATE TAX RULING

CTR 94-10

This substantive policy statement is advisory only. A substantive policy statement does not include internal procedural documents that only affect the internal procedures of the agency and does not impose additional requirements or penalties on regulated parties or include confidential information or rules made in accordance with the Arizona administrative procedure act. If you believe that this substantive policy statement does impose additional requirements or penalties on regulated parties you may petition the agency under Arizona Revised Statutes § 41-1033 for a review of the statement.

ISSUE:

Which taxpayers may file a consolidated Arizona income tax return and what are the requirements?

APPLICABLE LAW:

Laws 1994, 2nd Reg. Session, Ch. 41 (Senate Bill 1120) provided for the filing of consolidated Arizona income tax returns by corporations.

Arizona Revised Statutes (A.R.S.) § 43-1201.14 exempts insurance companies from Arizona income tax.

DISCUSSION:

Laws 1994, 2nd Reg. Session, Ch. 41 amended A.R.S. § 43-947 to allow corporate taxpayers an election to file consolidated Arizona income tax returns for taxable years beginning from and after December 31, 1993. In order to file an Arizona consolidated return the taxpayer must file a federal consolidated return. The taxpayer must include the same corporations in the Arizona consolidated return as in the federal consolidated return. The election to file on a consolidated basis is binding for all succeeding taxable years, unless the department consents to a change in filing method. The election must be accompanied by the written consent, signed by an officer, of each member of the affiliated group.

Taxpayers may also file retroactively on a consolidated basis by submitting amended returns on or before December 31, 1994, accompanied by properly executed consent forms. Taxpayers who wish to file on a consolidated basis for prior taxable years must file a consolidated Arizona return for the taxable year beginning from and after December 31, 1985, and for all succeeding taxable years.

Overpayments of Arizona tax resulting from retroactive consolidated filing for taxable years 1986 through 1993 are not refunded, but are allowed as a credit against future tax liabilities over a ten year period at a rate of 10 percent of the total credit per year. Overpayments remaining after the tenth year will be applied against the following year's tax liability and any remaining balance will be refunded.

RULING:

This ruling consists of the department's answers to questions which have been raised concerning the election to file consolidated Arizona income tax returns.

1. Which corporate groups are eligible to file a consolidated Arizona income tax return?

An affiliated group of corporations which files a federal consolidated return may elect to file a consolidated Arizona income tax return, subject to the conditions described in this ruling and the statutes.

2. For which taxable years may a taxpayer file Arizona consolidated returns?

Taxpayers may file original returns on a consolidated basis for taxable years beginning from and after December 31, 1993. Taxpayers may also file amended returns on a consolidated basis for all taxable years 1986 through 1993.

3. How does the corporate group elect to file a consolidated return?

For any taxable year beginning from and after December 31, 1993, an affiliated group of corporations may elect to file a consolidated Arizona income tax return by filing a consolidated Arizona tax return on or before the extended due date and attaching completed copies of Arizona Form 122, which is the Arizona consent form. The consent form must be signed by a current officer of each subsidiary in the affiliated group. An affiliated group which has elected to file a consolidated return must file consolidated returns for all succeeding taxable years unless the department consents to a change in filing method.

For taxable years 1986 through 1993, an affiliated group of corporations elects to file consolidated Arizona income tax returns by filing amended Arizona tax returns on a consolidated basis for all taxable years from 1986 through 1993 and attaching completed copies of Arizona Form 122 signed by a current officer of each subsidiary in the affiliated group. All amended returns must be filed after July 17, 1994, and on or before December 31, 1994.

4. If an affiliated group elects to file retroactive consolidated returns for taxable years 1986 through 1993, must consents be filed for each year during the retroactive period?

The consents to consolidated filing are only required for the initial year consolidated filing is elected. Therefore, for those affiliated groups electing consolidated filing for the tax year 1986, or the first year the affiliated group is eligible, a consent is required for the year of election. The consent must be signed by a current officer of each subsidiary included in the affiliated group for that year.

5. If prior to December 31, 1994, a taxpayer realizes that it failed to make a valid election or if it is notified by the department that it failed to make a valid election, may it rectify the defects?

Yes. However, the taxpayer must remedy all defects by December 31, 1994.

6. What will the department do if an affiliated group of taxpayers makes an invalid election to file consolidated returns for taxable years prior to 1994?

The department will notify taxpayers that they did not file a valid election. Taxpayers whose election has been denied will have the right to file a timely appeal to the hearing office. Taxpayers must meet all requirements for filing a valid election by December 31, 1994. Therefore, it is important that any taxpayer making a retroactive election ensure it has met all requirements when filing its amended returns.

7. Must a taxpayer file amended returns for **all** taxable years 1986 through 1993, if it desires to file amended returns on a consolidated basis?

Yes. The law requires consolidated returns be filed for **all** years beginning from and after December 31, 1985, if a taxpayer wishes to make an election for retroactive filing on a consolidated basis. If a taxpayer does not file amended returns on a consolidated basis for all years for which the taxpayer is eligible to file consolidated returns during taxable years 1986 through 1993, the election to file on a consolidated basis retroactively is invalid.

8. If an affiliated group of taxpayers was not in existence, if an affiliated group did not file a federal consolidated return, or if none of the members of the group had nexus in Arizona in 1986 but began filing to Arizona prior to 1993, can the parent of the affiliated group make an election to retroactively file consolidated returns?

Yes. The parent of the affiliated group of corporations may elect retroactive consolidated filing by filing amended consolidated returns commencing with its first year of operation in Arizona in which it also filed federal consolidated returns. If it is subsequently determined that one or more members of the group had taxable nexus within the state prior to the first year of filing and the group filed a federal consolidated return for that taxable year, the retroactive consolidation election will be invalid since all required returns were not filed by December 31, 1994.

To be eligible to retroactively file Arizona consolidated returns, the same affiliated group must have filed federal consolidated returns for the same taxable years. In addition, the affiliated group must have fulfilled all the retroactive filing requirements stated by Laws 1994, 2nd Reg. Session, Ch. 41.

9. May amended consolidated returns be filed for taxable years back to 1986, even if those years are otherwise closed under the statute of limitations?

Yes. However, such returns will also be subject to audit without restriction for four years from the date filed or within the regular statute of limitations, whichever is later. Taxpayers are also not restricted from making any valid adjustment on the amended returns for the same time period.

10. Can a corporation or a group of corporations, that was previously audited by the department and has a closing agreement in effect, elect to file consolidated amended returns for taxable years 1986 through 1993?

A.R.S. § 42-123 provides that closing agreements shall not be annulled, modified, set aside, or disregarded. Therefore, the terms of the closing agreement remain in effect. Unless the amended filings are allowed within the terms of the closing agreement, retroactive consolidated filing for taxable years 1986 through 1993 would not be allowed.

11. Will overpayments resulting from amended returns for taxable years 1986 through 1993 be refunded?

Net overpayments of tax and interest computed until December 31, 1994, from the amended consolidated returns will be allowed as a credit against future Arizona corporate income tax liabilities for taxable years beginning from and after June 30, 1995. The maximum amount of credit that can be used in any taxable year is ten percent of the total credit or the amount of the tax liability, whichever is less. After applying the credit against the tax liabilities for ten consecutive years, the remaining credit, if any, will be applied against the tax liability for the following

year and any balance will be refunded.

12. When an affiliated group that filed retroactive consolidated returns resulting in an overpayment ceases operation, may the group claim an immediate refund since it will have no future liabilities to which credits may be applied?

There are no provisions to allow the refund of overpayments prior to the end of the 10-year period for which credits must be utilized.

13. Will the unused credits earn interest?

No. Interest will be computed through December 31, 1994, on the overpayments from the amended returns. No additional interest will accrue after that date.

14. If some members of a federal consolidated group for taxable years 1986 through 1993 are no longer in existence or ceased to exist during that time period, may the parent still elect to file a consolidated return?

Yes. For the retroactive filing period, the parent may consent to the filing of a consolidated return for any subsidiary which had consented to the filing of a federal consolidated return and which is no longer in existence. In addition, if a parent corporation has an inactive subsidiary which does not have officers, the parent may also sign the consent for such a subsidiary.

15. If a corporation, which was a member of a federal consolidated group for the year of election for any of the taxable years 1986 through 1993, has been sold and is no longer part of the affiliated group, may the parent still elect to file a consolidated return?

Yes. However, the affiliated group must attach a consent to file the consolidated return signed by a current officer of the former subsidiary or another individual authorized by a valid power of attorney to act for that subsidiary in Arizona tax matters for the year of election.

16. Once a group of corporations has elected to file consolidated returns, can they withdraw the election?

No. The election is binding on all succeeding taxable years, unless the department consents to a change in filing method.

17. Since the law goes into effect on July 17, 1994, may those taxpayers whose return for taxable year 1993 will be timely filed with an extension after July 17,

1994, and before December 31, 1994, file their 1993 original returns on a consolidated basis?

Yes. A taxpayer may file its original 1993 return on a consolidated basis if it files on a consolidated basis retroactively for all eligible years by December 31, 1994, and the 1993 return is **timely** filed. The original 1993 consolidated return should be marked "Consolidated Return" at the top of the return.

18. Taxpayers with fiscal years ending from March 31, 1994, through November 30, 1994, may have an original or extended due date for their original tax returns after December 31, 1994. How do these taxpayers elect to file consolidated returns for taxable year 1993 before December 31, 1994, if they desire to file amended consolidated returns retroactively?

On or before December 31, 1994, these taxpayers must file amended returns on a consolidated basis for all taxable years prior to 1993 for which they are eligible to file consolidated returns. The amended returns must include the proper consents for the year of election. These taxpayers must submit a letter stating their intention to report income on a consolidated basis for the 1993 taxable year. The letter must be filed on or before December 31, 1994, and must be signed by an officer of the parent corporation. If 1993 is the first year the taxpayer is eligible and it is electing retroactive consolidated filing, the letter should also include signed consent forms for each subsidiary. The taxpayer may then file an original 1993 return reporting income on a consolidated basis on or before the due date or extended due date of the original return. The return should be marked "Consolidated Return" at the top of the return.

19. Can the credits generated by filing consolidated returns for taxable years 1986 through 1993 be used to reduce the consolidated group's estimated tax payments?

The credits cannot be considered estimated tax payments. However, the required estimated tax payment would be based on the tax liability remaining after application of the available credit for the year.

20. Will the credit generated by filing consolidated returns be applied before or after other credits?

The credit will be applied as a tax payment after other tax credits but before the application of estimated tax payments.

21. If the parent corporation did not previously file in Arizona, should the

consolidated group file under the taxpayer identification number (TIN) of the parent or the subsidiary operating within the state?

The consolidated Arizona tax return should use the name and TIN used on the federal consolidated tax return. When filing amended returns for prior years, it will be necessary to list the name and TIN of previous separate filers on Arizona Form 51D, which must be attached to Form 120X, in order to claim credit for taxes paid on those returns.

22. How is the carryforward of net operating losses computed when members of the affiliated group have losses incurred prior to the consolidation?

See Arizona Corporate Tax Ruling CTR 94-11.

23. How should the capital gains tax be computed if a taxpayer has capital gain income during 1986 or 1987 and is filing an amended return?

The capital gains tax should be computed in accordance with the statute and the retroactive consolidated filing instructions, which provide that the capital gains tax shall be computed at the rate of six and four-tenths percent of net capital gains. The tax should not be computed according to the instructions on the original tax returns for 1986 and 1987 since those instructions erroneously limited the amount of capital gain to an amount equal to net taxable income.

24. How is the fifty dollar minimum tax imposed on the consolidated Arizona return?

The consolidated group is considered one taxpayer and the minimum tax is imposed on the single return rather than each corporation within the group.

25. If taxes were paid by a subsidiary in past years for which filing a consolidated return generates a refund, will the parent or the subsidiary get the refund for those years?

Overpayments of tax generated by a consolidated filing will be applied as a credit against future tax liabilities of the consolidated group. Credits remaining after ten years will be refunded to the consolidated group.

26. Is there a limit to the amount of credit or refund available if a consolidated return is filed for prior taxable years?

There is no limit to the total amount of credit or refund available. However, the

amount of credit which can be utilized in each of the first ten years is limited to the lesser of ten percent of the total credit or the amount of the tax liability for each year.

For example, if a taxpayer has a credit for \$100,000 from filing consolidated returns retroactively for taxable years 1986 through 1993, it may use \$10,000 of the credit or the amount of the tax liability, whichever is less, each year for ten consecutive years beginning with taxable years beginning from and after June 30, 1995. If a tax liability in any taxable year is less than \$10,000, the difference may not be claimed in succeeding taxable years. Any unused credit remaining after ten consecutive years shall be claimed on the Arizona return filed for the next taxable year and, if it exceeds the amount of tax otherwise due, shall be refunded.

27. How will the apportionment formula be calculated for a multistate taxpayer filing a consolidated return?

A single apportionment formula will be calculated using the apportionment factors prescribed in Chapter 11, Article 4 of Title 43. The apportionment formula will be applied against the income of the affiliated group as if it were a single taxpayer. All Arizona property, payroll, and sales of the affiliated corporations will be included in the numerator of the apportionment ratio regardless of whether each of the corporations have or had nexus within the state on a separate basis.

The provisions of Arizona Administrative Code (A.A.C.) rules R15-2-947.A.1 and R15-2-947.B have been superseded by new A.R.S. § 43-947 and are no longer valid.

28. How will the acquisition or sale of a subsidiary affect the consolidated group?

An affiliated group which files a consolidated federal return and which has elected to file a consolidated Arizona return is required to file a consolidated Arizona return for succeeding taxable years. The Arizona affiliated group consists of the same group of corporations that files a consolidated federal return. Newly acquired subsidiaries included in the consolidated federal return are considered to have waived any objection to filing a consolidated Arizona return by their consent to the filing of a consolidated federal return and are included as a part of the Arizona affiliated group.

29. Are insurance companies taxed as part of the consolidated group?

No. Although they may be part of the affiliated group, income or loss of insurance companies exempt under A.R.S. § 43-1201 that are included in the consolidated

Arizona return is excluded from Arizona gross income pursuant to A.R.S. §§ 43-1121 and 43-1122. Property, payroll, and sales of the insurance companies must also be excluded from the numerator and denominator of the apportionment ratio.

30. If an affiliated group of corporations, which was in existence during any of the taxable years 1986 through 1993, has been sold, merged, or otherwise ceased to exist and the parent corporation is no longer in existence, can an election to file amended consolidated returns be made?

If an agent has been authorized to act for the affiliated group pursuant to Treasury Regulation § 1.1502-77(d) and the agent currently retains that authority to act for the affiliated group, the agent may elect, with the proper consents, to file consolidated amended returns. Overpayments would be refunded at the end of the credit period to the lawful successor or assign designated at the time of dissolution.

31. An affiliated group of corporations, consisting of parent Corporation A and subsidiaries, operated in Arizona for taxable years 1986 through 1988. In 1989, this group was acquired by another affiliated group, consisting of parent Corporation B and its subsidiaries, which have operated in Arizona since 1986. Corporation A and its subsidiaries become subsidiaries of Corporation B and are included in Corporation B's federal consolidated filing for taxable years 1989 through 1993. Corporation B, with the consent of its subsidiaries, makes an election to file retroactive amended consolidated returns for 1986 and succeeding taxable years.

Can Corporation A and its former subsidiaries file amended consolidated returns for the taxable years 1986 through 1988?

Yes.

32. Affiliated Group A is electing to file amended consolidated returns for the retroactive period 1986 through 1993. Affiliated Group A sold off subsidiaries B, C, and D at the end of 1990. It retained subsidiaries E, F, and G and continued to file as an affiliated group with those subsidiaries. Corporation B became the parent of Corporations C and D and filed federal consolidated returns for 1991 and succeeding taxable years.

Can the affiliated group consisting of Corporation B and its subsidiaries file amended consolidated returns for the taxable years 1991 through 1993?

Yes.

TAXPAYERS WHO ELECT TO FILE AMENDED RETURNS ON A CONSOLIDATED BASIS FOR PRIOR YEARS MUST FILE AMENDED RETURNS FOR THE ENTIRE RETROACTIVE PERIOD FOR WHICH THEY ARE ELIGIBLE TO FILE CONSOLIDATED RETURNS AND MUST FILE THOSE AMENDED RETURNS ON OR BEFORE DECEMBER 31, 1994. THOSE TAXPAYERS WHO FILE 1993 ORIGINAL RETURNS ON A CONSOLIDATED BASIS MUST FILE THEIR NOTICE OF INTENT TO FILE THE 1993 RETURN ON A CONSOLIDATED BASIS BY DECEMBER 31, 1994, AND MUST FILE THEIR 1993 RETURN BY THE ORIGINAL OR EXTENDED DUE DATE.

FAILURE TO FILE ALL RETURNS BY THE REQUIRED DATE WILL VOID THE ELECTION.

Harold Scott, Director

Explanatory Notice

The purpose of a tax ruling is to provide interpretive guidance to the general public and to department personnel. A tax ruling is intended to encompass issues of law which are not adequately covered in statute, case law or administrative rules. A tax ruling is a position statement which provides interpretation, details or supplementary information concerning the application of the law. **Relevant statute, case law, or administrative rules, as well as a subsequent ruling, may modify or negate any or all of the provisions of any tax ruling.** See GTP 92-1 for more detailed information regarding documents issued by the Department of Revenue.