

**BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO**

In the Matter of the Protest of

██████████ ██████████ ██████████ ██████████

Petitioner.

DOCKET NO. 0-058-188-800

DECISION

██████████ ██████████ ██████████ ██████████ formerly called ██████████ ██████████ ██████████ ██████████  
(Petitioner)<sup>1</sup> protested the Notice of Deficiency Determination (Notice) dated March 27, 2024,  
issued by the Income Tax Audit Bureau (Bureau). Petitioner disagreed with the Bureau's  
disallowance of nonbusiness income for tax year 2019. The Idaho State Tax Commission (Tax  
Commission) reviewed the matter and for the reasons stated below modifies the Notice.

**BACKGROUND**

Petitioner is a subsidiary of ██████████ ██████████ ██████████ ██████████ formerly called ██████████ ██████████  
██████████ ██████████ ██████████ ██████████ ██████████ ██████████ the parent, included Petitioner in its  
consolidated return for federal purposes. For Idaho purposes, Petitioner is the entity who filed an  
Idaho return to include the parent and other affiliates in the calculation of their apportionable  
income and apportionment factor. The parent provided products and services through its affiliates  
under three business segments:<sup>2</sup> ██████████,<sup>3</sup> ██████████,<sup>4</sup> and ██████████<sup>5</sup> The parent sold  
██████████ in 2019, and Petitioner reported the gain from the sale of ██████████ (██████████ gain)<sup>6</sup> as

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<sup>1</sup> Petitioner filed its Idaho return for tax year 2019, including ██████████ ██████████ ██████████ ██████████ the parent and its affiliates.  
The parent was formerly called ██████████ ██████████ ██████████ ██████████

<sup>2</sup> A segment is a distinct part of a company's operations, often identified by specific products, services, or geographic  
locations. Petitioner called their business segment a line of business (LOB) and vice versa.

<sup>3</sup> ██████████ manages various loyalty programs and offers marketing services.

<sup>4</sup> ██████████ provides advertising services through digital means.

<sup>5</sup> ██████████ issues private label and co-branded credit cards.

<sup>6</sup> The gain from sale of ██████████ was generated by the sale of all the capital stock, shares and other equity interests of  
██████████ ██████████ (EIN ██████████-██████████ ██████████ ██████████ ██████████ (EIN ██████████-██████████ and ██████████ ██████████

nonbusiness income on their Idaho return. The Bureau determined that the [REDACTED] gain is apportionable business income; therefore, they disallowed Petitioner's subtraction of nonbusiness income and issued a Notice.<sup>7</sup>

Petitioner protested the Notice, disagreeing with the Bureau's disallowance of nonbusiness income. Petitioner argued in the protest that they appropriately allocated the [REDACTED] gain as required by Idaho law, and explained that, to determine whether the income is business income or nonbusiness income, a taxpayer must meet either the transactional test or the functional test.<sup>8</sup> Petitioner explained that they acquired [REDACTED] through various investments since 2004 and did not sell any of them until they sold [REDACTED] in 2019. Petitioner argued that the [REDACTED] gain does not satisfy the transactional test because "One disposition over a 15-year period is not regular business activity." Petitioner argued that the [REDACTED] gain does not satisfy the functional test because acquisition, management, or disposition of the [REDACTED] entities was not an integral or necessary part of Petitioner's business. The Bureau acknowledged Petitioner's protest and sent the matter to the Tax Commission's Appeals Unit (Appeals) for administrative review.

Appeals reviewed the case and sent Petitioner a letter explaining the options available for redetermining a Notice. Petitioner responded and requested an informal hearing, which was held on February 5, 2025. At the conclusion of the hearing, Appeals requested Petitioner provide additional information<sup>9</sup> to enable a review and analysis of the nonbusiness income issue. Appeals

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[REDACTED] Federal Form 8949 of the parent's Schedule D lists goodwill, publisher networks, customer contracts, tradename, etc., as long-term assets held by the parent.

<sup>7</sup> The Bureau also adjusted Petitioner's state and local income taxes, dividend received deduction, and foreign dividend exclusion. Since Petitioner did not protest these issues, the Tax Commission will not address them any further.

<sup>8</sup> Idaho Code section 63-3027(a)(1).

<sup>9</sup> The requested information includes business description, organizational chart, lists of directors and officers, lists of clients for each business segment, "to/from" details of intercompany transactions, transfer pricing memo, apportionment factor details, nexus questionnaires, reconciliation of nonbusiness income reported on Petitioner's Idaho return and the capital gain reported on their consolidated return, etc. Although Appeals requested the board meeting minutes, Petitioner did not provide this information.

granted a 60-day extension per Petitioner's request, and they provided the requested information within the extended period. The Tax Commission, having reviewed the file, hereby issues its final decision.

## **ISSUE**

The issue on appeal is whether the [REDACTED] gain is nonbusiness income or apportionable business income. The Tax Commission reviews the [REDACTED] gain to determine whether it meets the transactional test or the functional test.<sup>10</sup> If the [REDACTED] gain meets either of these tests and is determined to be business income, the Tax Commission must then review whether the gross receipts from the sale of [REDACTED] gain are properly reflected in Petitioner's apportionment factor, specifically the sales factor.

## **LAW AND ANALYSIS**

### **Business income**

Idaho Code section 63-3027(a)(1) states,

"Business income" means income arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income from the acquisition, management, or disposition of tangible and intangible property when such acquisition, management, or disposition constitutes integral or necessary parts of the taxpayer's trade or business operations. Gains or losses and dividend and interest income from stock and securities of any foreign or domestic corporation shall be presumed to be income from intangible property, the acquisition, management, or disposition of which constitutes an integral part of the taxpayer's trade or business; such presumption may only be overcome by clear and convincing evidence to the contrary.

Idaho Code section 63-3027(a)(1) provides two separate definitions for "business income".

The first definition is the transactional test, and the second definition is the functional test. The Tax Commission must review whether the [REDACTED] gain qualifies as "business income" as defined

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<sup>10</sup> The functional test consists of two parts, the operational or passive investment test, and the unitary business test.

in Idaho Code section 63-3027(a)(1) under either (1) the transactional test or (2) the functional test.

#### Transactional test

The transactional test provides that business income is "income arising from transactions and activity in the regular course of the taxpayer's trade or business."<sup>11</sup> However, Idaho Income Tax Administrative Rule IDAPA 35.01.01.332.03., states in part that the transaction or activity "need not be one that frequently occurs in the trade or business." It is reasonable to conclude that transactions are made "in the regular course of a trade or business" where they "are customary in the kind of trade or business being conducted or are within the scope of what that kind of trade or business does."<sup>12</sup> In addition, "Income may be business income even though the actual transaction or activity that gives rise to the income does not occur in Idaho."<sup>13</sup> In the *Noell* case,<sup>14</sup> the district court examined two cases, one in Illinois and the other in Indiana, in reaching its decision wherein the respective appellate courts concluded that the gain arising from a holding company's sale of a subsidiary can qualify as business income if the holding company regularly engages in the buying and selling of subsidiaries; however, a one-time sale does not qualify. *Compare E.I DuPont De Nemours & Co. v. Indiana Dep 't of State Revenue*, 79 N.E.3d 1016, 1023 (Ind. T.C. 2017), with *PPG Indus., Inc. v. Dep 't of Revenue*, 765 N.E.2d 34, 45 (Ill. App. 2002). Importantly, the Illinois and Indiana statutes at issue in these cases utilize similar language to the Uniform Division of Income for Tax Purposes Act<sup>15</sup> and the Idaho statute to define business income, including the term

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<sup>11</sup> Idaho Code section 63-3027(a)(1).

<sup>12</sup> IDAPA 35.01.01.332.03.

<sup>13</sup> IDAPA 35.01.01.332.02.

<sup>14</sup> *Noell Industries, Inc. v. Idaho State Tax Commission*, 167 Idaho 367, 470 P3d 1176 (2020).

<sup>15</sup> The Uniform Division of Income for Tax Purposes Act (UDITPA) provides a uniform method for dividing income between states for tax purposes, thereby assuring that a taxpayer is not taxed more than once on its net income.

"regular" to describe the trade and business operations that qualify as "business income" under the transactional test.<sup>16</sup>

In this case, Petitioner explained in their protest that they acquired [REDACTED] through various investments from 2004 through 2019 and did not regularly engage in the trade or business of buying and selling entities. Petitioner, as a single entity, probably did not. However, the parent and its affiliates regularly engaged in the business of buying entities. The Tax Commission reviewed the parent's Form 10-K filed with the U.S. Securities and Exchange Commission and found that the parent acquired several businesses to develop and establish [REDACTED] business. [REDACTED] is a segment,<sup>17</sup> providing [REDACTED] services through multiple entities ultimately owned by the parent. Starting in 2004,<sup>18</sup> the parent acquired [REDACTED] a provider of integrated direct marketing solutions, and in 2005, [REDACTED] now known as [REDACTED]. In 2006, [REDACTED] acquired [REDACTED],<sup>19</sup> a provider of [REDACTED] services, from [REDACTED] Inc. In 2011, the parent acquired [REDACTED] a provider of [REDACTED] services, to be a part of [REDACTED]. In 2012, [REDACTED] acquired [REDACTED] and [REDACTED] collectively [REDACTED] and [REDACTED].<sup>20</sup> In 2014, the parent

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<sup>16</sup> Idaho Code section 63-3027(a)(1); *E.I. DuPont De Nemours & Co.*, 79 N.E.3d at 1022 (quoting Indiana Code section 6-3-1-20 (2001)); *PPG Indus., Inc.*, 765 N.E.2d at 42 (quoting 35 ILL. COMP. STAT. 5/1501(a)(1) (1994)).

<sup>17</sup> A segment is a distinct part of a company's operations, often identified by specific products, services, or geographic locations. Petitioner called their business segment a line of business (LOB) vice versa.

<sup>18</sup> In addition to the entities related to [REDACTED] the parent's Network Services business acquired [REDACTED] and the parent's Utility Services business acquired [REDACTED] in 2008. In 2012, the parent acquired [REDACTED] private label credit card portfolio. In 2014, the parent acquired 60% ownership in [REDACTED] a [REDACTED]-based company. In 2015, [REDACTED] acquired all the stock in [REDACTED] and [REDACTED]. In 2017, the parent acquired part of [REDACTED] business (i.e., credit card receivables and the associated accounts and assumed a portion of an existing customer care operation, including a facility sublease agreement and approximately 250 employees). In 2019, the parent acquired part of [REDACTED] business (i.e., certain assets as well as the assembled workforce and related office lease agreements).

<sup>19</sup> [REDACTED] was a division of [REDACTED].

<sup>20</sup> [REDACTED] focuses on retail marketing.

acquired [REDACTED] [REDACTED]<sup>21</sup> and folded it into [REDACTED]. Through these acquisitions, the parent intended to enhance “[REDACTED] core capabilities, strengthen its competitive advantage, expand [REDACTED] into new industry verticals and add a talented team of marketing professionals.”<sup>22</sup> The acquisition of [REDACTED] “added important capabilities to [REDACTED] digital messaging platform.”<sup>23</sup> and enhanced its functionality. The parent’s Form 10-K further explains, “[REDACTED] data also enriched the Company’s existing offline and online data set, allowing for more effective targeted marketing programs. The goodwill recognized was attributable to expected synergies and the assembled workforce.” The parent and/or its affiliates did not sell any of the businesses acquired since 2004 until they sold [REDACTED] in 2019. Therefore, Petitioner argued in the protest, “One disposition over a 15-year period is not regular business activity.” IDAPA 35.01.01.332.03., states in part, “For a transaction or activity to be in the regular course of the taxpayer’s trade or business, the transaction or activity need not be one that frequently occurs in the trade or business.”<sup>24</sup> The Tax Commission found that the acquisitions of businesses occurred regularly during the period prior to the sale of [REDACTED]. These acquisitions increased [REDACTED] ability to generate operating earnings<sup>25</sup> from transactions and activity in the regular course of [REDACTED] businesses, which contributed to the sale price of [REDACTED] in 2019. The Tax Commission makes no ruling on the transactional test at this time.

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<sup>21</sup> [REDACTED] [REDACTED] was formerly known as [REDACTED] [REDACTED].

<sup>22</sup> The parent’s Form 10-K for tax year 2014.

<sup>23</sup> [REDACTED] digital messaging platform is called [REDACTED] [REDACTED].

<sup>24</sup> IDAPA 35.01.01.332.03

<sup>25</sup> Earnings before interest, taxes, depreciation, and amortization (EBITDA) is a measure of business’s ability to generate operating earnings. It focuses on a company’s core business performance by excluding non-operating expenses like interest and taxes and non-cash expenses like depreciation and amortization. This provides a clearer picture of how well a company is performing financially from its core operations before accounting for these specific factors.

<sup>26</sup> Adjusted EBITDA, reported under “segment information” on the parent’s Form 10-K: In 2018, [REDACTED] generated \$2 billion revenues, which resulted in \$475.1 million of adjusted EBITDA. The sale price to [REDACTED] [REDACTED] was \$4.4 billion, approximately 10 times [REDACTED] 2018 adjusted EBITDA.

## Functional test

The functional test provides that business income is “income for the acquisition, management, or disposition of tangible property when such acquisition, management or disposition constitute integral or necessary parts of the taxpayer's trade or business operations.”

To meet the functional test, the Idaho Supreme Court explained in the *Noell* case,<sup>27</sup>

Rule 333.08 of Idaho's Income Tax Administrative Rules provides two methods for meeting the functional test: "business income" can be established either by (a) finding that the intangible interest serves an operational function-rather than a passive investment-as "an integral, functional, or operative component to the taxpayer's trade or business operations," or (b) by meeting the unitary-business test. IDAPA 35.01.01.333.08. Even though these methods would appear to be independent of each other, the U.S. Supreme Court has rejected the notion that the operational-function test and unitary-business test are separate principles. *MeadWestvaco Corp. ex rel. Mead Corp. v. Illinois Dep 't of Rev.*, 553 U.S. 16, 29-32 (2008). Therefore, **we must apply both tests.** (emphasis added)

The Tax Commission now reviews whether the [REDACTED] gain met (a) operational or passive investment test, and (b) unitary business test with regard to the functional test.

## ***Operational or passive investment test***

IDAPA 35.01.01.333.05., provides,

Under the functional test, income from intangible property is business income when the intangible property serves an operational function as opposed to solely an investment function. The relevant inquiry focuses on whether the property is or was held in furtherance of the taxpayer's trade or business, that is, on the objective characteristics of the intangible property's use or acquisition and its relation to the taxpayer and the taxpayer's activities. The functional test is not satisfied where the holding of the property is limited to solely an investment function as is the case where the holding of the property is limited to mere financial betterment of the taxpayer in general.

Petitioner argued in their protest that they acted as a holding company for [REDACTED] and held investments in [REDACTED] for mere financial betterment. However, the parent's Form 10-K describes

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<sup>27</sup> *Noell Industries, Inc. v. Idaho State Tax Commission*, 167 Idaho 367, 470 P3d 1176 (2020).

██████ as one of their primary business segments and provided marketing services, offered complete marketing solutions by using data, analytics, creativity, and technology. Through the acquisition of multiple businesses, the parent and its affiliates developed ██████ services, including strategic consulting, customer database technologies, omnichannel marketing, loyalty management, and digital agency services. On behalf of the parent's clients, ██████ developed marketing programs via their digital media practice,<sup>28</sup> ██████,<sup>29</sup> for individual consumers who need to create highly targeted offers and personalized communications.<sup>30</sup> ██████ distributed campaigns through various channels like direct mail, email, mobile, and social media, serving over 1,800 clients across industries such as finance, insurance, media, automotive, retail, travel, healthcare, and telecommunications. The consolidated income statement, provided in the parent's 10-K, shows that ██████ revenue represented 29% and 27%, respectively, of total revenue for tax years 2017 and 2018, the years prior to the sale. The parent provided ██████ digital marketing services through its affiliates, i.e., ██████ ██████ ██████ ██████,<sup>31</sup> ██████ ██████ ██████ ██████, ██████,<sup>32</sup> and ██████ ██████ ██████ ██████.<sup>33</sup> The parent ultimately owned, and sold the capital stock, shares and other equity interests of these affiliates, who provided the ██████ services. The parent's federal Form 8949 of Schedule D reported the ██████ gain as a long-term capital gain from the

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<sup>28</sup> Digital media practice refers to the skills, strategies, and approaches used to create and manage digital content and communications. Digital media practice encompasses all aspects of creating, distributing, and interacting with digital content, which includes software, data, and other forms of digital media. It is not limited to just one of these elements; rather, they are all interconnected and crucial for the field.

<sup>29</sup> ██████ is currently known as ██████ ██████ ██████ ██████ (██████ the marketing platform, originally developed by ██████ ██████. In 2014, after ██████ ██████ changed its name to ██████ ██████ the parent acquired ██████ ██████.

<sup>30</sup> ██████ provides digital-marketing services to help their clients create advertising with target messages across devices, e.g., phones, computers, tablets, etc.

<sup>31</sup> ██████ ██████ ██████ (EIN ██████-██████-██████)

<sup>32</sup> ██████ ██████ ██████ (EIN ██████-██████-██████) is a domestic disregarded entity of Petitioner.

<sup>33</sup> ██████ ██████ ██████ is a foreign disregarded entity of the parent.



sale of goodwill, publisher networks, customer contracts, tradename, etc.<sup>34</sup> The Tax Commission found that the parent ultimately owned [REDACTED] intangible properties and engaged in [REDACTED] business operations as it was an integral part of their business prior to the sale of [REDACTED] IDAPA 35.01.01.333.03., provides in part, “Property that was an integral part of the trade or business is not considered converted to investment purposes merely because it is placed for sale.” The sale of [REDACTED] was not for investment purposes as [REDACTED] was an integral part of their business. Therefore, the Tax Commission found that the [REDACTED] gain met the operational function test under the functional test.

### ***Unitary business test***

Idaho Code section 63-3027(t) states in part,

...the income of two (2) or more corporations, wherever incorporated, the voting stock of which is more than fifty percent (50%) owned directly or indirectly by a common owner or owners, when necessary to accurately reflect income, shall be... apportioned **as if the group of corporations were a single corporation**, in which event:

(1) The Idaho taxable income of any corporation subject to taxation in this state shall be determined by use of a combined report which includes the income, determined under paragraph (2) of this subsection, of all corporations which are members of a unitary business, ... apportioned using apportionment factors for all corporations included in the combined report and methods set out in this section. The use of a combined report does not disregard the separate corporate identities of the members of the unitary group. Each corporation which is transacting business in this state is responsible for its apportioned share of the combined business income..., minus its net operating loss carryover or carryback. (emphasis added)

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<sup>34</sup> Federal Form 8949 Sales and Other Dispositions of Capital Assets, Part II, 1. Description of property: [REDACTED] [REDACTED] [REDACTED] [REDACTED] [REDACTED] [REDACTED] [REDACTED] and [REDACTED] [REDACTED] Date acquired for these intangible assets varies, and most of them were acquired on December 10, 2014, some are acquired on November 30, 2012, and one of the tradenames was acquired on May 31, 2021. The acquisition date on [REDACTED] [REDACTED] is shown as “various”.

IDAPA 35.01.01.340 through 344, outlines the principles for determining the existence of a unitary group. IDAPA 35.01.01.340 explains the concept of a unitary business as a “single economic enterprise that is made up either of separate parts of a single business entity or of a commonly controlled group of business entities that are sufficiently interdependent, integrated and interrelated through their activities...” and IDAPA 35.01.01.341.02., further explains,

A unitary business is characterized by significant flows of value evidenced by factors such as those described in *Mobil Oil Corp. v. Vermont*, 445 U.S. 425 (1980): **functional integration, centralization of management, and economies of scale.** These factors provide evidence of whether the business activities operate as an integrated whole or exhibit substantial mutual interdependence. Facts suggesting the presence of the factors mentioned above should be analyzed in combination for their cumulative effect and not in isolation. A particular business operation may be suggestive of one (1) or more of the factors mentioned above. (emphasis added)

IDAPA 35.01.01.342 provides descriptions of functional integration, centralization of management, and economies of scales. IDAPA 35.01.01.343 describes the same type of business as being one of the indicators of unity, and IDAPA 35.01.01.344 states that, to be unitary, corporations must be part of a controlled group which is defined by common ownership.

In the protest, Petitioner explained, [REDACTED] shared certain officers with the other business segments; however, these officers were high-level executives who were not involved in the day-to-day management of [REDACTED] business. Petitioner also explained that various subsidiaries held by the parent shared certain corporate administrative elements, including tax, legal, accounts payment, payroll and human resources. However, Petitioner argued that these shared services are similar to the findings in the *Noell* case wherein the Court pointed out that the utilization of these shared services did not alone result in the income being deemed as business income.

The Bureau explained in the Notice that Petitioner included [REDACTED] income in the calculation of their apportionable income and apportionment factor for the years prior to the sale of [REDACTED] and therefore [REDACTED] is a unitary member of Petitioner for tax year 2019. However, the

Bureau did not provide any other rationale for their findings or their analysis that led to their unitary determination. The inclusion of [REDACTED] income in the prior years' apportionable income and apportionment factor may be an indication of a unitary relationship in the prior years; however, it does not mean that significant flows of value existed for the current year. Without analyzing all the factors, it is not possible to determine whether a unitary relationship existed for the year under review. Therefore, the Tax Commission reviews all the factors: functional integration, centralization of management, and economies of scale, to determine whether a unitary relationship existed among Petitioner, the parent and its affiliates, including the entities who were sold at net gain.

Functional integration

IDAPA 35.01.01.342.01., states in part,

Functional integration includes, but is not limited to, transfers or pooling with respect to the unitary business's products or services, technical information, marketing information, distribution systems, purchasing, and intangibles such as patents, trademarks, service marks, copyrights, trade secrets, know-how, formulas, and processes...The following is a list of examples of business operation that can support the finding of functional integration...

- a. Sales, exchanges, or transfers (collectively "sales") of products, services, or intangibles between business activities provide evidence of functional integration... For example, sales among business entities that are part of a vertically integrated unitary business are indicative of functional integration.
- c. Transfer or Pooling of Technical Information or Intellectual Property. Transfers or pooling of technical information or intellectual property, such as patents, copyrights, trademarks and service marks, trade secrets, processes or formulas, know-how, research, or development, provide evidence of functional integration when the matter transferred is significant to the businesses' operations.

Petitioner states in their protest, “The core functions of each line of business<sup>[35]</sup> were significantly different and independent of each other. [REDACTED] generated income from interest and other financial transactions. [REDACTED] earned revenue through its digital advertising and direct mail channels. While there was overlap in some customers, the majority of operating elements of [REDACTED] and [REDACTED] were independent of each other. The strategy of each line of business was separate and distinct.” Petitioner also stated in the protest, “[REDACTED] was never integrated into or with the other LOBs<sup>[36]</sup> held by [REDACTED] [REDACTED] it remained a separate business that largely operated autonomously. From the perspective of [REDACTED] [REDACTED] and similar to the facts in the *Noell* case, [REDACTED] was acquired for investment purposes. Marketing companies traditionally have a higher PE ratio<sup>[37]</sup> compared to that of the other LOBs held by [REDACTED] [REDACTED]. The Company's investors reaped benefits driven by [REDACTED] [REDACTED] diversified holdings. As the diversified holdings strategy became more complicated, and the investor gains from the strategy began to dwindle, the Company decided to sell its investment in [REDACTED].

As previously mentioned in this decision, in 2014, the parent acquired [REDACTED] [REDACTED] ([REDACTED] who specialized in digital marketing, and folded it into [REDACTED] [REDACTED] was an offline marketer before the acquisition of [REDACTED] and the acquisition of [REDACTED] helped [REDACTED] grow their digital marketing capabilities based on the technologies and networks already established by [REDACTED]. Based on the foundation established by [REDACTED] [REDACTED] grew its digital marketing business through several entities directly and indirectly owned by the parent, and

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<sup>35</sup> Line of businesses (LOBs), or business segments.

<sup>36</sup> Line of businesses (LOBs), or business segments.

<sup>37</sup> PE ratio stands for Price to Earnings ratio. PE ratio is a valuation metric of stocks and measures a company's current share price relative to its per-share earnings. It's often used as a tool to assess whether a stock is undervalued or overvalued, especially when comparing to other companies in the same industry.



implement strategies that assist our clients in acquiring, retaining and managing valuable repeat customers. **Our credit card programs capture transaction data that we analyze to better understand consumer behavior and use to increase the effectiveness of our clients' marketing activities.** We use multi-channel marketing communication tools, including in-store, web, permission-based email, mobile messaging and direct mail to reach our clients' customers. (emphasis added)

Petitioner's protest explained that [REDACTED] provided funding and receivables management services, in addition to accepting customer deposits. [REDACTED] performed call center activities, including account processing, customer services, payment application and collections, and operates a call center in Idaho. Through [REDACTED] the integrated marketing services, the parent and its affiliates designed and implemented marketing strategies for [REDACTED] clients, and [REDACTED] captured its clients' customer data to increase the effectiveness of their marketing activities. [REDACTED] provided marketing services in coalition with [REDACTED] and these transactions were consistently reflected in Petitioner's details of their inter-segment transactions regarding marketing and data processing. These inter-segment transactions represent the existence of vertical integration between the [REDACTED] and [REDACTED] segments. Therefore, the Tax Commission found functional integrations exist among Petitioner, the parent and its affiliates, including the entities who were sold at net gain.

#### Centralization of management

IDAPA 35.01.01.342.02, states in part,

Centralization of management exists when directors, officers, or other management employees jointly participate in the management decisions that affect the respective business activities and that may also operate to the benefit of the entire economic enterprise. Centralization of management can exist whether the centralization is effected from a parent entity to a subsidiary entity, from a subsidiary entity to a parent entity, from one (1) subsidiary entity to another, from one (1) division within a single business entity to another division within a business entity, or from any combination of the foregoing...

The Court has found that centralization of management and control exists where "high

officials of appellant gave directions to subsidiaries for compliance with the parent's standard of professionalism, profitability, and ethical practices.” *Container Corp.*, 463 U.S. at 177. Also, the Court found centralization of management to exist when there was considerable interplay between the parent and the subsidiary in the area of corporate expansion. *Id.* at 179. Additionally, centralization of management exists when the parent company's officers provided general guidance and technical assistance. *Id.* In *Exxon Corp.*, 447 U.S. at 224, a unitary business exists where the integrated business benefited "from an umbrella of centralized management and controlled interaction." For centralization of management and control to exist, it must be present and occurring and not just legally permissible or the potential to exercise. *ASARCO Inc. v. Idaho State Tax Commission*, 458 U.S. 307,323 (1982 S.Ct.).

In the present case, Petitioner provided Appeals with a list of directors and officers for Petitioner, the parent, and [REDACTED] [REDACTED] [REDACTED] [REDACTED]. Most of the directors and officers of [REDACTED] [REDACTED] [REDACTED],<sup>47</sup> and Petitioner were the same as the directors and officers of the parent. IDAPA 35.01.01.342.02., provides in part, “Common offers are more likely to provide evidence of centralization of management...”, and that is because officers, such as the Chief Executive Officer, Chief Operating Officer, Chief Financial Officer, etc., are responsible for implementing the board’s decisions and managing the day-to-day operation of the company. Based on Petitioner’s lists of officers, the Tax Commission found that there was centralization of management among Petitioner, the parent, and its affiliates, including the entities who were sold at net gain.

### Economies of scale

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<sup>47</sup> [REDACTED] [REDACTED] [REDACTED] [REDACTED] directly owned [REDACTED] [REDACTED] [REDACTED] [REDACTED] [REDACTED]

IDAPA 35.01.01.342.03, states in part,

Economies of scale refers to a relation among and between business activities resulting in a significant decrease in the average per unit cost of operational or administrative functions due to the increase in operational size. Economies of scale may exist from the inherent cost savings that arise from the presence of functional integration or centralization of management...

Economies of scale exist where there is a sharing of resources among members of the unitary group. *Container Corp.*, 463 U.S. at 178. As previously mentioned under “Centralization of management” in this decision, the parent, [REDACTED],<sup>48</sup> and Petitioner shared most of their directors and officers. By doing so, Petitioner received the benefit of the services provided by the directors and officers who were members of the parent. Additionally, as mentioned under “Functional integration” in this decision, [REDACTED] and [REDACTED] had inter-segment transactions, which were eliminated in the parent’s consolidated return as these segments consisted of the affiliates directly and indirectly owned by the parent. Therefore, the Tax Commission found that there were economies of scale among Petitioner, the parent and its affiliates, including the entities who were sold at net gain.

The Tax Commission finds that the gain from the sale of [REDACTED] met all requirements of the functional test, consisting of the operational test and the unitary business test. However, before reaching a final determination regarding whether there was a unitary relationship among Petitioner, the parent, and its affiliates, including the entities who were sold at net gain, the Tax Commission will review Petitioner’s 2019 Idaho return regarding their filing method: water’s-edge.

### **Water’s-edge election**

Idaho Code section 63-3027D(a), states in pertinent part,

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<sup>48</sup> [REDACTED] directly owned [REDACTED]



A qualified taxpayer and its affiliates shall be presumed to be a part of a unitary business and all income of that business shall be presumed to be apportionable business income **if a valid water's-edge election has been made**, ... (emphasis added)

As part of their 2018 original Idaho return, Petitioner submitted a valid water's-edge election, Idaho Form 14,<sup>49</sup> with a list of their unitary members, including the parent and its affiliates related to all business segments, i.e., [REDACTED] [REDACTED] and [REDACTED] and the disregarded entities<sup>50</sup> directly and indirectly owned by the parent. A valid Idaho water's-edge election is permanent unless a taxpayer files a written request with the Tax Commission for a change in its filing method at least thirty (30) days prior to the due date for filing the tax return.<sup>51</sup> Additionally, a taxpayer must receive written approval from the Tax Commission for a change of filing method. There is no record that Petitioner requested, and the Tax Commission approved a change in filing method after they filed their 2018 return with a valid election. Petitioner filed their 2019 Idaho return on a water's edge basis, just as they did on their 2018 Idaho return, listing the same unitary members.

The Tax Commission found that there was a unitary relationship between Petitioner, the parent, and all other affiliates directly and indirectly owned by the parent. Therefore, the [REDACTED] gain is apportionable business income, and the Tax Commission upholds the Bureau's

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<sup>49</sup> Idaho Form 14 Idaho Water's-edge Election and Consent Form.

<sup>50</sup> Petitioner's list of unitary members also include disregarded entities, [REDACTED]

[REDACTED] and [REDACTED]

<sup>51</sup> IDAPA 35.01.01.643.03. Due Date for Filing the Written Petition. The written petition requesting the change of reporting method must be filed with the Tax Commission at least thirty (30) days prior to the due date for filing the tax return.

disallowance of Petitioner's nonbusiness income treatment in the calculation of the apportionable income. While the Bureau appropriately included the [REDACTED] gain as business income in the calculation of Petitioner's apportionable income, they did not clearly explain in the Notice whether they adjusted the apportionment factor, specifically, the sales factor<sup>52</sup> to include gross receipts from the sale of [REDACTED]. Therefore, the Tax Commission reviews Petitioner's sales factor to see whether the Bureau included gross receipts from the sale of [REDACTED].

### **Apportionment factor**

#### Sales factor

IDAPA 35.01.01.525.01., states,

**In General.** Sales means all gross receipts of a taxpayer not allocated as nonbusiness income. The sales factor for each trade or business of the taxpayer includes all gross receipts derived by the taxpayer from transactions and activity in the regular course of that trade or business.

#### ***Sales denominator***

IDAPA 35.01.01.530, states in part that "The denominator of the sales factor includes the total gross receipts derived by the taxpayer from transactions and activity in the regular course of its trade or business, ..."

In response to Appeals' request, Petitioner confirmed that their sales denominator did not include gross receipts from the sale of [REDACTED] and they provided details of their sales denominator calculation. The Tax Commission reviewed Petitioner's sales denominator details, i.e., their summary and reconciliation, federal Form 1120, Schedule D, and Form 4797, and verified that their sales denominator calculation is consistent with their nonbusiness income position.

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<sup>52</sup> The sales factor represents the portion of apportionable income that is attributable to a taxpayer's sales.

In the Notice, the Bureau did not adjust the sales denominator to include the gross receipts from the sale of [REDACTED] despite their determination that the [REDACTED] gain is an apportionable business income. As previously mentioned, the Tax Commission finds that the [REDACTED] gain is apportionable business income. The Tax Commission now must determine what amount of the gross receipts from the sale of [REDACTED] must be included in the sales denominator.

The Tax Commission requested, and Petitioner provided the Securities Purchase Agreement (purchase agreement) between the parent and the purchaser of [REDACTED],<sup>53</sup> dated April 12, 2019. The purchase agreement stated that the sales price<sup>54</sup> of [REDACTED] was \$4,400,000,000,<sup>55</sup> but this may not be the same as the gross receipts<sup>56</sup> from the sale. However, in this case, since the purchase agreement does not describe any closing adjustments, the sales price can be substituted for gross receipts. Therefore, the Tax Commission modifies the sales denominator to include \$4,400,000,000 of the sale price as the gross receipts from the sale of [REDACTED] in the sales denominator.

### ***Sales numerator***

IDAPA 35.01.01.535., states in part, “The numerator of the sales factor includes gross receipts attributable to Idaho and derived by the taxpayer from transactions and activity in the regular course of its trade or business...” IDAPA 35.01.01.570.01., provides the sales factor for the gross receipts from intangibles, and states in part, “... gross receipts from the sale of an ownership interest in another entity are included in the sales factor numerator based on the

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<sup>53</sup> The purchaser of [REDACTED] is [REDACTED] [REDACTED] [REDACTED] and its affiliates.

<sup>54</sup> A sale price means the total amount charged for a specific item.

<sup>55</sup> The purchase agreement defines that purchase price means the “pre-adjustment cash amount”, plus the “closing adjustment”, if any. The purchase agreement provides that the pre-adjustment cash amount is “\$4,400,000,000 in cash” but does not provide any details of the closing adjustment or if any existed.

<sup>56</sup> A gross receipt or gross proceed means the total amount of money received from a sale or transactions without any deductions for expenses, taxes, or fees.

proportion of the entity's operational assets located in Idaho. The amount included is determined by multiplying the gross receipts received by the percentage of the entity's total real and tangible personal property located in Idaho at the time of the sale." The Tax Commission reviewed the details of Petitioner's property factors of [REDACTED] [REDACTED] [REDACTED] [REDACTED] [REDACTED] [REDACTED] [REDACTED] and [REDACTED] [REDACTED] [REDACTED] [REDACTED] and found that none of these entities had real and tangible personal property in Idaho<sup>57</sup> at the time of the sale. Therefore, none of the gross receipt from the sale of [REDACTED] should be apportioned to Idaho. The Tax Commission accepts the sales numerator as reported by Petitioner.

### CONCLUSION

The Tax Commission found that the [REDACTED] gain was business income. Therefore, the [REDACTED] gain must be included in the calculation of Petitioner's apportionable income and apportionment factor. The Tax Commission reviewed the Notice and found that the Bureau properly included the [REDACTED] gain in their apportionable income calculation. However, the Tax Commission found that the Bureau did not adjust Petitioner's apportionment factor for the sales denominator to include the gross receipts from the sale of [REDACTED]. Therefore, the Tax Commission modifies the Notice, specifically for the sales denominator to include the gross receipts based on the security purchase agreement.

The Bureau added interest to Petitioner's Idaho tax. The Tax Commission reviewed the addition and found it appropriate. The Tax Commission updated interest based on Idaho Code section 63-3045. The Bureau added a ten percent (10%) penalty for substantial understatement,

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<sup>57</sup> [REDACTED] [REDACTED] [REDACTED] [REDACTED] a disregarded entity of Petitioner, had Idaho payroll but no Idaho property.

and the Tax Commission found the addition of the penalty appropriate and in accordance with Idaho Code section 63-3046.

THEREFORE, the Notice of Deficiency Determination dated March 27, 2024, and directed to Petitioner is AFFIRMED as MODIFIED by this decision.

<u>YEAR</u>	<u>TAX</u>	<u>PENALTY</u>	<u>INTEREST</u>	<u>TOTAL</u>
2019	\$1,465,226	\$146,523	\$236,363	\$1,848,112

DEMAND for immediate payment of the foregoing amount is hereby made and given.

An explanation of Petitioner's right to appeal this decision is enclosed.

DATED this \_\_\_\_\_ day of \_\_\_\_\_ 2025.

IDAHO STATE TAX COMMISSION

## CERTIFICATE OF SERVICE

I hereby certify that on this \_\_\_\_\_ day of \_\_\_\_\_, 2025,  
a copy of the within and foregoing DECISION was served by sending the same by United States  
mail, postage prepaid, in an envelope addressed to:



Receipt No.

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