

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of

██████████ ██████████ ██████████

Petitioner.

DOCKET NO. 1-802-638-336

DECISION

██████████ ██████████ ██████████ ██████████ (Petitioner)¹ protested the Notice of Deficiency Determination (Notice) dated October 6, 2023, issued by the Income Tax Audit Bureau (Bureau). Petitioner disagreed with the Bureau's adjustments to Idaho net operating loss (NOL). The Idaho State Tax Commission (Tax Commission) reviewed the matter and for the reasons stated below modifies the Notice.

BACKGROUND

Petitioner acquired ██████████ ██████████ (██████████) in June 2013, but did not include ██████████ in their combined Idaho return upon the acquisition. Petitioner's explanation for that is because no integration happened before and/or after the acquisition². ██████████ reported an Idaho NOL on its final return for the period beginning January 1, 2013, ending June 28, 2013. For the short period after the acquisition, beginning June 29, 2013, ending December 31, 2013, ██████████ filed its own Idaho return and reported the second Idaho NOL. ██████████ continued to separately file its own Idaho returns until filing another final return, reporting the third Idaho NOL for tax year 2016. Tax year 2017 was the first year that Petitioner included ██████████ in their combined Idaho return, utilizing ██████████ Idaho NOLs. Petitioner carried the unused Idaho NOLs to tax year 2018 and onward. The Bureau disallowed Petitioner's use

¹ Petitioner is currently called ██████████ ██████████ ██████████ ██████████ ██████████ ██████████ ██████████ ██████████ changed its name to ██████████ ██████████ ██████████ in 2017.

² Petitioner argued that there was no instant unity upon acquisition.

of [REDACTED] Idaho NOLs in their 2019 through 2021 Idaho returns due to [REDACTED] “incorrect filing from 2013-2016” and issued a Notice.

Petitioner protested the Notice, disagreeing with the Bureau’s disallowance of [REDACTED] Idaho NOLs utilized in their 2019 through 2021 combined Idaho returns. Petitioner argued that [REDACTED] separately filed Idaho returns³ are correct as no instant unity occurred upon acquisition. Petitioner mentioned in the protest that Idaho requires a taxpayer to calculate Idaho NOLs by entity, and a combined return does not disregard each entity’s identity⁴. Petitioner argued that [REDACTED] Idaho NOLs survived the acquisition and therefore, they should be able to carry the Idaho NOLs over to tax year 2017 onward. 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 March 27, 2025. During the hearing, Appeals requested Petitioner provide additional information to enable a review and analysis of the unitary issue. Petitioner provided the information requested by Appeals. The Tax Commission, having reviewed the file, hereby issues its final decision.

ISSUES

The issues on appeal are whether [REDACTED] became a unitary member of Petitioner upon acquisition, and whether Petitioner can utilize [REDACTED] Idaho NOLs in their 2019 through 2021 Idaho returns.

³ For tax years 2013 through 2016.

⁴ Idaho Income Tax Administrative Rule IDAPA 35.01.01.365

LAW AND ANALYSIS

Unitary

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)

Idaho Income Tax Administrative Rules IDAPA 35.01.01.(Idaho Rule) 340 through 344, outline the principles for determining the existence of a unitary group. Idaho Rule 340 explains the concept of a unitary business as “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 Idaho Rule 341 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)

Idaho Rule 342 provides descriptions of functional integration, centralization of management, and economies of scales. Idaho Rule 343 describes the same type of business as being one of the

indicators of unity, and Idaho Rule 344 says that, to be unitary, corporations must be part of a controlled group which is defined by common ownership.

In the present case, Petitioner explained in the protest that, after the acquisition, the original founder of [REDACTED] remained as the Chief Executive Officer and managed the day-to-day operations. For tax years 2013 through 2016, [REDACTED] had its own Enterprise Resource Planning (ERP) system and accounting team as it's a stand-alone Core Business Unit. [REDACTED] had separate headquarters and office locations from the other [REDACTED] [REDACTED] [REDACTED] businesses. [REDACTED] administrative functions gradually started integrating after the acquisition but not entirely until tax year 2017 when Petitioner acquired the remaining shares of [REDACTED]. Petitioner argued that, although Petitioner acquired more than 50% of the shares of [REDACTED] in June 2013, they did not have controlling power over [REDACTED]. Petitioner's response to the Bureau's unitary questionnaire indicated that there were some connections between [REDACTED] and Petitioner. However, none of them are definitive evidence that there were significant flows of value between them. To investigate the unitary issue further, Appeals requested additional information, including, but not limited to, partial copies of the consolidated returns Petitioner filed with the Internal Revenue Service for tax years 2013 through 2016, the detailed "to/from" analysis of the eliminations taken for federal purposes, the job description of the common officer for all consolidated entities, and a clarification of the timing of when [REDACTED] became a part of Petitioner's 401(k) plan.

In response to Appeals' request, Petitioner provided a partial copy of their consolidated returns and analysis of intercompany transactions, which shows that there were some intercompany transactions, i.e., royalty income, interest expense, management service fee, between [REDACTED] and Petitioner. Petitioner explained during the hearing that the intercompany transaction involving royalty income was because one of Petitioner's subsidiaries used [REDACTED] trademarks in manufacturing

products. [REDACTED] received royalty income since all their trademarks, copyrights, and domain names remained with [REDACTED] even after the acquisition⁵. In the process of consolidation for federal purposes, Petitioner eliminated the royalty income [REDACTED] received from another consolidated subsidiary of Petitioner. Petitioner also eliminated interest expense and explained that it is due to a daily cash sweep⁶ they do as the foreign parent required all of its affiliates follow its cash pooling policy. Petitioner further explained that, although they swept [REDACTED] cash at the end of each business day, [REDACTED] maintained daily cash management for itself. As for the management service fee eliminated as an intercompany transaction, there was an officer, the Treasurer, who was commonly involved in all consolidated subsidiaries⁷. Petitioner explained that the Treasurer oversaw financial affairs and record-keeping, such as meeting minutes, and had custody of all funds, securities and corporate documents. As for the 401(k) plan, Petitioner clarified that they brought [REDACTED] into their 401(k) plan on January 1, 2019.

All explanations and documentations Petitioner provided to Appeals are consistent with Petitioner's position that [REDACTED] was not a unitary member. However, in their response to the unitary questionnaire, Petitioner indicated that they voluntarily filed income tax returns on a combined basis, including [REDACTED] for California, Florida, Illinois, Massachusetts, Maine, New Hampshire, Oregon, Texas, and Utah. To review consistency in reporting⁸, Appeals requested Petitioner explain their rationale for [REDACTED] separately filing Idaho returns while it was combined with Petitioner for other

⁵ The Agreement and Plan of Merger, dated May 12, 2021, among [REDACTED] and [REDACTED] the original owner of [REDACTED]. There is no other agreement (e.g., shared service agreement, burn-out/buy-out agreement, etc.) going along with the Agreement and Plan of Merger.

⁶ The concept of a cash sweep is that excess cash in a borrower's account is converted into a debt payment at the end of each business day.

⁷ Petitioner's federal Form 1125-E shows that the Treasurer was the only officer who was commonly involved in all consolidated entities.

⁸ "State to state consistency", Idaho Income Tax Administrative Rule IDAPA 35.01.01. 375.02.

states. Petitioner explained that the inclusion of [REDACTED] was to avoid their compliance burden, not because they asserted [REDACTED] as a unitary member.

The Tax Commission found some flows of value, but they are not significant enough to prove that [REDACTED] was a unitary member of Petitioner. Therefore, the Tax Commission finds [REDACTED] separately filed Idaho returns are correct. The Tax Commission further reviews whether [REDACTED] correctly calculated its Idaho NOLs for tax years 2013 through 2016, and whether Petitioner's application of [REDACTED] Idaho NOLs to tax years 2017 through 2021 are correct.

Idaho NOLs

For tax years 2013 through 2016

Idaho Income Tax Administrative Rule IDAPA 35.01.01.201.03.c., states,

Adjustments may be made even though the year is closed due to the statute of limitations, but will not result in any tax due or refund for the closed taxable years.

The Tax Commission reviews three separate Idaho NOLs generated from different tax years during tax years 2013 through 2016.

Short period from January 1, 2013, to June 28, 2013 (June 2013 Idaho NOL)

The June 2013 Idaho NOL is based on the final return [REDACTED] filed upon the acquisition by Petitioner. The Tax Commission reviewed [REDACTED] final return and determined that [REDACTED] correctly reported the June 2013 Idaho NOL. [REDACTED] is entitled to the June 2013 Idaho NOL and its carryover if any exists after utilizing the Idaho NOL in years with absorption income. Therefore, the Tax Commission modifies the Notice and allows Petitioner to utilize the June 2013 Idaho NOL and any carryover going into tax years 2019 through 2021.

Short period from June 29, 2013, through December 31, 2013 (December 2013 Idaho NOL)

The December 2013 Idaho NOL is based on the short period return [REDACTED] separately filed. As previously determined in this decision, [REDACTED] was not a unitary member of Petitioner for the

short period ending December 31, 2013. During administrative review, Petitioner provided a partial copy of their consolidated return and details of gross receipts, calculating federal taxable income/loss by company (by-company details). The Tax Commission reviewed the by-company details, showing a federal loss for [REDACTED] and verified that [REDACTED] Idaho return started with the federal loss before the deduction of charitable contribution. The Tax Commission verified that, after Idaho additions and subtractions allowed under Idaho Code section 63-3022, the Idaho NOL [REDACTED] reported on its separately filed Idaho return is correct. [REDACTED] is entitled to the December 2013 Idaho NOL and any carryover that exists after utilizing the Idaho NOL in years with absorption income. Therefore, the Tax Commission modifies the Notice and allows Petitioner to utilize the December 2013 Idaho NOL and any carryover going into tax years 2019 through 2021.

Calendar year from January 1, 2016, through December 31, 2016 (2016 Idaho NOL)

[REDACTED] reported an Idaho NOL for tax year 2016 based on the federal loss separately calculated for them. The Tax Commission reviewed the by-company details, reporting a federal loss for [REDACTED] and verified that [REDACTED] Idaho return started with the federal loss deduction before charitable contribution. The Tax Commission verified that, after Idaho additions and subtractions set forth in Idaho Code section 63-3022, the Idaho NOL [REDACTED] reported on its separately filed Idaho return is correct. [REDACTED] is entitled to the 2016 Idaho NOL and any carryover that exists after utilizing the Idaho NOL in years with absorption income. Therefore, the Tax Commission modifies the Notice and allows Petitioner to utilize the 2016 Idaho NOL and any carryover going into tax years 2019 through 2021.

For tax years 2017 through 2021

Idaho Code section 63-3027(t)(1) states in pertinent part:

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...

Idaho Income Tax Administrative Rule IDAPA 35.01.01.200., provides calculation of Idaho

NOL for unitary taxpayers:

01. Unitary Taxpayers. Each corporation included in a unitary group must determine its respective share of the Idaho apportioned net operating loss incurred by the unitary group for the taxable year. A corporation's share of the net operating loss is computed using its Idaho apportionment factor for the year of the loss...

Idaho Income Tax Administrative Rule IDAPA 35.01.01.365., clarifies Idaho NOL carryback and carryforward:

03. Net Operating Loss. The Idaho net operating loss carryover or carryback for each included corporation is limited to its share of the combined net operating loss apportioned to Idaho for each taxable year.

In the present case, the Idaho NOLs, previously identified in this decision, should be carried forward and utilized in the years where there was income to absorb the Idaho NOLs. The Tax Commission reviewed Petitioner's Idaho combined return for tax year 2017 and found that they reported \$1,645,771 of [REDACTED] net income apportioned to Idaho (absorption income). However, Petitioner utilized only \$182,270 of [REDACTED] Idaho NOLs, instead of utilizing it up to the \$1,645,771 absorption income. For tax year 2018, Petitioner also had \$664,017 of [REDACTED] net income apportioned to Idaho but did not utilize Idaho NOLs at all. To correctly calculate the Idaho NOL carryover going into tax years 2019 onward, the Tax Commission adjusts application of Idaho NOLs.



The Tax Commission's calculation shows that Petitioner utilized all of [REDACTED] Idaho NOLs in tax year 2020, and there is no Idaho NOL carryover into tax year 2021. Therefore, the Tax Commission modifies the Notice to adjust [REDACTED] Idaho NOL application as shown above.

CONCLUSION

The Tax Commission found that [REDACTED] separately filed Idaho returns for tax years 2013 through 2016 were correct, and [REDACTED] is entitled to Idaho NOLs generated prior to tax year 2017. The Tax Commission reviewed Petitioner's application of [REDACTED] Idaho NOLs for tax years 2017 and 2018 to correctly calculate the Idaho NOLs going into tax years 2019 onward, and found an adjustment is necessary since Petitioner did not utilize [REDACTED] Idaho NOLs based on [REDACTED]

absorption income amount. Therefore, the Tax Commission modifies the Notice to correctly apply [REDACTED] Idaho NOLs for tax years 2019 through 2021.

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. As for the penalties⁹ the Bureau added, the Tax Commission found the addition of the penalties appropriate and in accordance with Idaho Code section 63-3046.

THEREFORE, the Notice of Deficiency Determination dated October 6, 2023, and directed to Petitioner is AFFIRMED as MODIFIED by this decision.

<u>YEAR</u>	<u>TAX/(REFUND)</u>	<u>PENALTY</u>	<u>INTEREST</u>	<u>TOTAL</u>
2019	\$(16,443)	\$0	\$(3,436)	\$(19,879)
2020	(17,621)	0	(3,196)	(20,817)
2021	47,434	7,115	6,211	60,760
			TOTAL DUE	<u>\$20,064</u>

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

⁹ The Bureau added a five percent (5%) negligence penalty and a ten percent (10%) substantial understatement penalty.

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.


