



**State of California
Franchise Tax Board**

1996 Guidelines for Corporations Filing A Combined Report

Table of Contents

	Page
Introduction	3
Important Tax Law Changes	3
The Unitary Method.	3
The Use of a Combined Report.	4
Consolidated Return Distinguished.	5
Corporations Having Different Accounting Periods.	5
Part-Year Members.	5
Adjustments for Intercompany Transactions	6
Unitary Partnerships	6
Net Operating Losses	7
Alternative Minimum Tax.	8
Election to File a Group Return.	8
Exceptions — Where Group Return is Not Allowed	8
Example of Combined Report and Schedules	8
Schedule 1 — Combined Income Subject to Apportionment.	10,11
Schedule 2 — Computations to Place Corp D Income and Apportionment Factors on a Calendar Year Basis	12
Schedule 3 — Calculation of Combined Interest Offset.	13
Schedule 4 — Combined Apportionment Formula and Entity Income Assignment	14-18
Schedule 5 — Combined Alternative Minimum Tax	19-21
How to get California Tax Information	23,24

Other Publications

Other publications prepared by the Franchise Tax Board include:

- Form 100, California Corporation Tax Booklet
- Form 100-WE, Water's-Edge Booklet
- FTB Pub. 1038, Guide for Corporations Dissolving, Surrendering (Withdrawing) or Merging
- FTB Pub. 1050, Application and Interpretation of Public Law 86-272
- FTB Pub. 1060, Guide for Corporations Starting Business in California
- FTB Pub. 3817, Electronic Funds Transfer Program Information Guide

These publications may be obtained by writing to:

**TAX FORMS REQUEST UNIT
FRANCHISE TAX BOARD
PO BOX 307
RANCHO CORDOVA CA 95741-0307**

Or by calling:

From within the United States 1-800-852-5711
From outside the United States (not toll free). 1-916-845-6500

Or by downloading from the Internet:

<http://www.ftb.ca.gov>

Corporations Filing a Combined Report

Introduction

This publication sets forth the concepts of the unitary method of taxation and its application by the State of California to corporations subject to either the franchise tax or income tax. It includes instructions for preparing a combined report, because a corporation is required to use it in computing its California tax liability when the corporate activities are part of a unitary business conducted by itself and related corporations. A combined report is not equivalent to a consolidated return for federal purposes.

This publication does not address water's-edge statutes under which corporate taxpayers may elect to exclude from the combined report some or all of the income and apportionment factors of certain foreign affiliates in the unitary group. For more information about the water's-edge election, get Form 100-WE, Water's-Edge Contract. Questions regarding water's-edge elections may be addressed to:

FRANCHISE TAX BOARD
PO BOX 1779
RANCHO CORDOVA CA 95741-1779

Important Information

Twenty-five Percent Foreign Owned U.S. Corporations and Foreign Corporations That Are California Taxpayers

If you were required to file federal Form(s) 5472, Information Return of a Foreign Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business, with your federal return, and you are a California taxpayer, you must attach a copy(s) to your California return. The penalty for failing to include federal Form(s) 5472 as required is \$10,000 per form.

Note: Form 5472 is required to be filed timely even if the tax return cannot be filed timely.

Electronic Funds Transfer (EFT)

Corporations that meet certain requirements must remit all of their payments through an EFT rather than by paper checks. Corporations that remit an estimated tax payment or extension payment in excess of \$20,000 or that have a total tax liability in excess of \$80,000 in any income year beginning on or after January 1, 1995, must pay through an EFT. The FTB will notify corporations that are subject to this requirement. Those that wish to participate on a voluntary basis may do so. For more information, call the EFT Unit at 1-916-845-4025 and request FTB Pub. 3817, Electronic Funds Transfer Program Information Guide.

Important Tax Law Changes

Charitable Contributions

For income years beginning on or after January 1, 1996, the amount of allowable charitable contributions deduction is increased from 5% of California net income to 10% of California net income. Corporations will now be able to carry over excess contributions for 5 years.

Corporations/Water's-Edge

For income years beginning on or after January 1, 1996, California allows water's-edge taxpayers a flat 75% deduction for dividends

received for foreign affiliates of domestic-based multinational corporations. California did not make a change to the existing law regarding the 100% dividend deduction for foreign construction projects.

For income years beginning on or after January 1, 1997, there is a 25% interest offset provided with respect to foreign source dividends.

Enhanced Oil Recovery Credit

For income years beginning on or after January 1, 1996, California allows a credit equal to one-third of the federal credit of the cost for enhanced oil recovery projects (also known as tertiary injectants) incurred by small, independent oil producers.

Convention and Trade Show Activities

For income years beginning on or after January 1, 1996, corporations that are not incorporated under the laws of California and whose sole activities in California during an income year are engaging in convention and trade show activities may no longer be subject to the \$800 minimum franchise tax. To qualify, such corporations must engage in only convention and trade show activities for seven or fewer days during an income year, and earn gross income reportable to this state from such activities of \$10,000 or less. Qualified corporations must still report California gross income and pay the corporate income tax.

For this purpose, convention and trade show activities are defined by reference to IRC Section 513(d)(3)(A), and corporations engaged in convention and trade show activities for a portion of a day will be considered to have engaged in such activities for an entire day. The determination of gross income reportable to California is made by including gross income reportable to this state for each member of a commonly controlled group.

Tax Law Changes for Coming Tax Years

New AMT and Tax Rate for 1997

For income years beginning on or after January 1, 1997, the following changes have been made to AMT and tax rates: C corporation tax rate is 8.84%, bank and financial tax rate is 10.84% and the AMT rate is 6.65%. The S corporation's tax rate remains at 1.5%.

Currently, corporations are required to pay 95% of the current year's tax in four installments to avoid a penalty. For income years beginning on or after January 1, 1998 and before January 1, 1999 that amount increases to 98% and for income years beginning on or after January 1, 1999 the amount increases to 100% of the current year's tax.

In addition, for income years beginning on or after January 1, 1997, California conforms to the federal annualization methods. For more information, get Form 100ES, Corporation Estimated Tax.

Net Operating Loss

For income years beginning in 1997, the definition of "new business" will be expanded to include certain biopharmaceutical companies.

Nonconformity to Federal S Corporation Changes

At the time this booklet was printed, California did not conform to the changes made to federal S Corporation statutes by H.R. 3448, Small Business Job Protection Act.

The Unitary Method

Corporations deriving income from sources both within and outside California are required to measure their tax liability by income derived from or attributable to sources within California. To determine the portion of total income that may reasonably be attributable to this state, California utilizes the unitary business principle. This concept has been validated by income and franchise tax cases for more than 70 years.

Under the unitary method as applied by California, all of the elements comprising a single trade or business are viewed as a whole or unit, hence the term "unitary." The business income from all activities of a unitary business is combined into a single report, whether such activities are conducted by divisions of a single corporation or by members of a commonly controlled group of corporations. For most businesses the combined business income is apportioned to California by a formula derived from the Uniform Division of Income for Tax Purposes Act (UDITPA, R&TC Sections 25120-25139). The elements required in a combined report are discussed in detail beginning on page 5.

Development of the Unitary Method

The theory underlying the unitary business principle has its roots in property tax law, where the issue of apportionment arose during the 1870s in the context of railroad taxation. (*State Railroad Tax Cases*, (1876) 92 U.S. 575) A broader application later evolved as the states adopted the practice of measuring taxes by income. As early as 1920, the United States Supreme Court approved the use of a formula to apportion the income of a single corporation among several states in the case of *Underwood Typewriter Co. v. Chamberlain*, (1920) 254 U.S. 113.

California's use of formula apportionment dates to 1929 and the enactment of the original Franchise Tax Act. The use of the unitary method to combine the income from unitary divisions of a single corporation was validated by the California Supreme Court in *Butler Bros. v. McColgan* (1941), 17 Cal.2d.664. In *Edison California Stores v. McColgan*, (1947) 30 Cal.2d.472, the California Supreme Court extended the unitary business concept to allow apportionment of combined income of a common business activity conducted by a multi-corporate group.

While R&TC Section 25101 provides the general authority for use of the unitary business concept, no statutes have ever been adopted to define precisely the scope of application of the unitary principle. Instead, the law has evolved through a series of judicial decisions. For example:

- In *Superior Oil Co. v. Franchise Tax Board*, (1963), 60 Cal.2d 406, the California Supreme Court held that once it is determined that a business with income from

sources within and outside the state is unitary, formula apportionment MUST be utilized.

- The United States Supreme Court found California's application of the unitary business principle to multiple corporations to be constitutional in *Container Corporation v. Franchise Tax Board*, (1983) 463 U.S. 159, aff'g 117 Cal. App.3d 988 (1981).
- Application of the unitary method is required whether the unitary business is carried on over state or international boundaries. Application of the unitary method to worldwide activities of a single corporation was first sanctioned by the United States Supreme Court in *Bass, Ratcliff & Gretton Ltd. v. State Tax Commission*, (1924) 266 U.S. 271. More recent decisions upholding the application of the unitary method to worldwide activities of multiple corporations are *Container Corporation v. Franchise Tax Board*, discussed above; *Barclays Bank Internat., LTD v. Franchise Tax Board*, (1994) 129 L. Ed 2d. 244 aff'd 2 Cal. 4th 708, (1992); and *Colgate-Palmolive v. FTB*, (1994) 129 L. Ed 2d. 244.

Tests for Determining Unity

Both *Butler Bros.* and *Edison California Stores*, discussed above, set forth tests to be used in determining whether the activities of several divisions or corporations should be considered unitary. In *Butler Bros.*, the court held that a "unitary business" exists where there is: (1) unity of ownership; (2) unity of operation as evidenced by central divisions for functions such as purchasing, advertising, accounting and management; and (3) unity of use in its centralized executive force and centralized system of operations. In *Edison California Stores*, the court held that if the operation of the portion of the business done within the state is dependent upon or contributes to the operation of the business outside the state, the operations are unitary; otherwise, if there is no such dependency, the business within the state may be considered to be separate.

The three unities test and the contribution or dependency test, have been applied by the California courts in a variety of cases. (See, e.g., *Superior Oil Co. v. Franchise Tax Board* (1963) 60 Cal.2d 406, 411-412; *Honolulu Oil Corp. v. Franchise Tax Board* (1963) 60 Cal.2d 417, 423-424; *John Deere Plow Co. v. Franchise Tax Board* (1951) 38 Cal.2d 214, 221-222; *Container Corporation of America v. Franchise Tax Board* (1981) 117 Cal.App.3d 988, 994-1001, aff'd at 463 U.S. 159, (1983); *Chase Brass & Copper Co. v. Franchise Tax Board* (1970) 10 Cal.App.3d 496, 501-502.)

The United States Supreme Court has also referred to a unitary business as one that exhibits "contributions to income resulting from functional integration, centralization of management and economies of scale." (*Mobil Oil Corp. v. Comm'r of Taxes of Vt.* (1980) 445 U.S. 425, 438; *F. W. Woolworth Co. v. Taxation and Revenue Dep't of the State of N.M.* (1982) 458 U.S. 354, 366, *Allied Signal v. Director, Taxation Division* (1992), 119 L.Ed. 533.) That court further noted that, "[t]he prerequisite to a constitutionally acceptable finding of a unitary business is a flow of value, not a flow of goods." (*Container Corp. of America v. Franchise Tax Board* (1983) 463 U.S. 159, 178.) The Supreme Court has stated

that for commonly controlled activities to be non-unitary, they must be part of "unrelated business activity which constitutes a 'discrete business enterprise.'" (*Mobil Oil Corp.*, supra, 445 U.S. at 439-440.)

18 Cal. Code Reg. Section 25120 provides additional rules and examples regarding what constitutes a unitary business. The regulation (1) recognizes that a single taxpayer may have more than one "trade or business"; and (2) sets forth three factors, the presence of any one of which creates a "strong presumption" that the activities of the taxpayer constitute a single trade or business. 18 Cal. Code Reg. Section 25120 provides in pertinent part:

(b) Two or More Businesses of a Single Taxpayer. A taxpayer may have more than one "trade or business." In such cases, it is necessary to determine the business income attributable to each separate trade or business. The income of each business is then apportioned by an apportionment formula which takes into consideration the instate and out of state factors which relate to the trade or business the income of which is being apportioned.

* * *

The determination of whether the activities of the taxpayer constitute a single trade or business or more than one trade or business will turn on the facts in each case. In general, the activities of the taxpayer will be considered a single business if there is evidence to indicate that the segments under consideration are integrated with, dependent upon or contribute to each other and the operations of the taxpayer as a whole. The following factors are considered to be good indicia of a single trade or business, and the presence of any of these factors creates a strong presumption that the activities of the taxpayer constitute a single trade or business:

- (1) Same type of business. This factor applies when all of a taxpayer's activities are in the same general line, such as in the operation of a chain of retail grocery stores.
- (2) Steps in a vertical process. An example of this factor would be a taxpayer which explores for and mines copper ores; concentrates, and smelts and refines the copper ores; and fabricates the refined copper into consumer products.
- (3) Strong centralized management. A taxpayer that might otherwise be considered as engaged in more than one trade or business is properly considered as engaged in one trade or business when there is a strong central management, coupled with the existence of centralized departments for such functions as financing, advertising, research, or purchasing.

For recent court decisions that discuss strong centralized management and the application of the unitary concept to diverse businesses, see *Mole-Richardson Co. v. Franchise Tax Board* (1990) 220 Cal.App.3d 889, 894; *Tenneco West, Inc. v. Franchise Tax Board* (1991) 234 Cal.App.3d 1510; and *Dental Insurance Consultants, Inc. v. Franchise Tax Board* (1991) 1 Cal.App.4th 343.

As noted above, the activities of a single corporation or group of commonly owned corporations do not always constitute a single unitary business. If a taxpayer has two or more trades or businesses that are not unitary with one another, separate combined report computations must be made to compute business income and apportionment factors for each trade or business, and to apportion to California the business income of each.

California law classifies income as either "business" or "nonbusiness." Business income is income arising from transactions and activity in the regular course of the taxpayer's trade or business. Business income includes income from tangible and intangible property if the acquisition, management and disposition of the property constitute integral parts of the taxpayer's regular trade or business operations. Business income is assigned through formula apportionment (R&TC Section 25120(a)). Nonbusiness income is all other income (R&TC Section 25120(d)), and is generally allocated to a particular jurisdiction (R&TC Sections 25123-25127). Regulations under R&TC Section 25120 also provide guidance for distinguishing between business and nonbusiness income. For further discussion and examples of business and nonbusiness income, refer to the instructions for Schedule R, Apportionment and Allocation of Income.

Unity of Ownership

A corporation may file a combined report with other members of a unitary group only if the corporations are members of a commonly controlled group under R&TC Section 25105. Generally, a commonly controlled group exists when stock possessing more than 50% of the voting power is owned, or constructively owned, by a common parent corporation (or chains of corporations connected through the common parent), or by members of the same family. A commonly controlled group also includes corporations that are stapled entities. Special rules are provided in R&TC Section 25105 for partnerships, trusts and transfers of voting power by proxy, voting trust, written shareholder agreement, etc.

The Use of a Combined Report

Corporations conducting a unitary business within and outside California are required to use the combined reporting approach to determine California source income subject to tax by California.

For years after beginning on or after January 1, 1980, R&TC Section 25101.15 allows corporations conducting a unitary business wholly within California to elect to use a combined report.

A corporation that has made a valid election to be treated as an "S corporation," however, may not generally be included in a combined report. However, in some cases, the FTB may use combined reporting methods to clearly reflect income of an S corporation (R&TC Section 23801(d)(1)).

The combined report is a means by which the income of a unitary business is divided among the taxing jurisdictions in which the trade or business is conducted. A combined report is not a "return," but merely the name given to the calculations by which multi-entity unitary businesses apportion income on a geographic basis. There is no "combined report" form; tax is calculated on

an attachment to Form 100 using the format described in this publication.

In a combined report, the entire amount of unitary business income of all corporations in the unitary group (including unitary members with no property, payroll or sales within California) is aggregated in the combined report.

The combined business income of the unitary group is then apportioned to California by the apportionment formula (details of this formula are discussed in the instructions to Schedule R, Apportionment and Allocation of Income). Income apportioned to California is then further apportioned between the unitary members subject to tax in California. (This is commonly referred to as "intrastate apportionment." The computations are explained in FTB Legal Ruling 234 and FTB Notice 90-3.) The taxable income of each member is then computed, taking into account its share of apportioned business income or loss, California source nonbusiness income or loss, and allowable California source net operating loss. Credits are applied against the tax on a separate entity basis. Unless otherwise provided by statutory authority, specific credit(s) are only available to the taxpayer corporation that incurred the expense that generated the credit(s). Generally, each California taxpayer included in the combined report must file its own tax return using Form 100. However, as explained on page 7 of these instructions, some unitary groups may elect to file a group Form 100 and report the sum of the separate tax liabilities of the unitary members.

Unlike a consolidated return, in which the group is treated as a single taxpayer, members of a unitary business are taxed individually and each affiliate doing business, qualified to do business or incorporated in California is subject to at least the minimum franchise tax.

Contents of a Combined Report

A combined report should contain the following:

- A combined profit and loss statement in columnar format disclosing each corporation's statement of profit and loss.
- A schedule in columnar format disclosing the various adjustments for each corporation necessary to convert the combined profit and loss statement to the combined income subject to apportionment. This schedule includes any adjustments necessary to revise federal or foreign income to that reported for California purposes, as well as adjustments for nonbusiness income or loss.
- A combined apportionment formula in columnar format disclosing for each corporation the total amount of property, payroll and sales, and the amount of California property, payroll and sales.
- A schedule in columnar format disclosing for each corporation any items of nonbusiness income or expense allocated to California.
- Schedules disclosing the computations of the amount of the interest offset and the charitable contributions adjustment.
- A schedule in columnar format of the alternative minimum tax calculation by corporation.

- Schedules in columnar format disclosing for each corporation all data required by Form 100. These schedules include:

1. Balance sheets;
2. Gains and losses from sale or exchange of assets;
3. Taxes on or measured by income;
4. Dividends and interest received;
5. Income or loss from rentals, royalties, partnerships, and miscellaneous sources; and
6. Net operating losses.

- Schedules in columnar format showing the computation of income apportionable and allocable to this state for each member of the group, and the computation of each member's tax credits and tax liability.

A comprehensive example illustrating the use of the above schedules begins on page 8.

Consolidated Return Distinguished From a Combined Report

Unless specifically stated otherwise, California does not follow the federal consolidated return regulations provided under Internal Revenue Code (IRC) Section 1502. With respect to earnings and profits and stock basis, California has no provisions similar to the investment adjustments allowed for federal purposes under Treas. Reg. Sections 1.1502-32 and -33. The earnings and profits of each entity in the combined report are calculated on a separate accounting basis, and do not reflect the earnings of any lower tier unitary subsidiaries (see *Appeal of Young's Market Company*, Cal. St. Bd. of Equal., 11/19/86). Likewise, the cost basis of a unitary subsidiary's stock is not adjusted to reflect the earnings of that subsidiary (see *Appeal of Safeway Stores*, Cal. St. Bd. of Equal., 3/2/62 and *Appeal of Rapid American Corp.* Cal. St. Bd. of Equal., 10/10/96).

Corporations Having Different Accounting Periods

Common Accounting Period Necessary

When filing a combined report, the income of all corporations must be determined on the basis of the same accounting period. Where there is a parent-subsidiary relationship in the combined report, the income of all corporations should be determined generally on the basis of the parent's income year.

Where there is no common parent corporation, the income of the related corporations should be determined generally on the basis of the income year of the corporation required to file a California return. If more than one member is required to file in California, the income should be determined on the basis of the income year of the California reporting corporation expected to have, on a recurring basis, the largest amount of income allocated and apportioned to California.

Income Calculation

Each member of the group should generally use the actual figures taken from its books of account to determine the proper income and related computations for the common accounting period. This will usually require an interim closing of the books for members whose normal accounting period differs from the common income year of the group. Alternatively, a pro-rata method of

converting income to the common income year will be accepted as long as the results do not produce a material misstatement of income apportioned to the state.

Pro-Rata Method

Under the pro-rata method, income of a member of the group is converted to the common income year on the basis of the number of months falling within the applicable income year. For example, if a parent corporation operates on a calendar year basis and a subsidiary includable in a combined report operates on a September 30 income year, it is necessary to assign 9/12 of the subsidiary's unitary income of one income year and 3/12 of the unitary income of the succeeding income year to arrive at a full twelve months' income to be included in the combined report. Where this procedure results in using the income of a corporation whose income year has not yet closed, it may be necessary to make an estimate based on available information and amend the return at a later date.

Apportionment of Combined Unitary Income Using a Common Accounting Period

The factors of the combined formula should be computed on the basis of the same common income year as was used to compute the unitary income. If an interim closing of the books was done to determine income attributable to the common income year, then the actual figures from the interim closing should be used to determine the apportionment factors as well. If the pro-rata method is used to convert income, then a pro-rata method should also be used to convert the factors of a member of the group to the common income year.

Once income and apportionment factors have been placed on a common income year, combined unitary business income is apportioned to California and further apportioned to each of the member corporations filing returns in California. For each California reporting corporation with a normal accounting period which differs from the common income year, the California income apportioned to that corporation is then converted back to the corporation's normal accounting period. This conversion is made on the basis of the number of months falling within the common income year of the group.

The computations necessary to determine the combined income under the pro-rata method when members of the group are on different accounting periods are illustrated in the example beginning on page 8 of this publication.

Part-Year Members

A part-year member is a corporation that either becomes a member or ceases to be a member of the unitary group after the beginning of the income year. If the part-year member is required to file two short period returns for the income year, then the income for the period in which the member was unitary with the group must be determined on a combined basis. The income for the remaining short period will be determined on a separate basis (or on a combined basis with a different group if the taxpayer had a unitary relationship with one or more corporations in that short period).

If the part-year member is **not** required to file short period returns, then it must file a single

return for the entire year. The income reported on that return would be determined by combined reporting procedures for any period in which the part-year member was part of a unitary group, and by separate accounting for any period it was not part of a unitary group. Use the actual income and apportionment data from the common unitary period to apportion income for that period, see the use of interim closing discussed above regarding common accounting period. However, the comprehensive example beginning on page 8 contains an acceptable alternative method for this computation, if that method does not cause income apportioned to this state to be materially misstated.

Note: R&TC Section 24632 provides that the income year of a taxpayer may not be different than the taxable year used for purposes of the Internal Revenue Code, unless initiated or approved by the FTB. Whenever a taxpayer is required to file a federal return for a period of less than 12 months, a California return for that period is also required. Federal due dates for these short period returns also apply for California.

Adjustments for Intercompany Transactions

The following guidelines reflect the FTB's current policy regarding adjustments necessary to properly reflect intercompany transactions among unitary affiliates included in the combined report.

Note: The FTB is presently reviewing the treatment of intercompany transactions between members of a combined group with the intention of promulgating regulations to provide more specific guidance. The following guidelines are subject to change and may be superseded by regulation.

Inventories

In computing cost of goods sold, intercompany profits are eliminated from beginning and ending

inventories. The elimination of intercompany profits shall also be done for property factor purposes.

Intangible Assets

Gain or loss from intercompany sales of intangible assets shall be eliminated from unitary business income. The seller's basis in the intangible assets will carry over to the buyer in the intercompany sale.

Fixed Assets and Capitalized Items

The gain or loss on intercompany sales of business fixed assets or capitalized intercompany charges and expenditures between members of a combined group are generally deferred. The exception to this rule occurs when an affiliated group that files a consolidated federal return elects not to defer gain or loss on intercompany transfers, in which case the federal election will be allowed for the combined report.

Under the general rule, the gain or loss remains deferred as long as both the seller and the purchaser remain in the combined group and the asset is not sold to outsiders. When either the seller or purchaser is no longer a member of the combined group, or the group for any reason terminates combined reporting, the gain or loss is reportable by the seller at a time immediately preceding the date either corporation ceases to be a member of the group. If the asset is sold to third parties, the deferred gain or loss is reportable by the combined group in the year of sale. A water's-edge election is also a restoration event which will cause previously deferred intercompany gains and losses to be included in income on a pro-rata basis over the original election term (refer to FTB Notice 89-601 for further details of this computation). The amount of gain recognized upon the occurrence of a restoration event is generally the same amount as would be reportable for federal purposes under similar circumstances in a consolidated return.

Where intercompany gain or loss is deferred, the basis of the asset for property factor purposes shall be the seller's cost.

Other Factor Adjustments

For factor purposes, intercompany sales and other intercompany revenue items are eliminated in computing the numerator and denominator of the sales factor. Intercompany rent charges are also eliminated from the property factor computation.

Dividends

To the extent that intercompany dividends are paid out of earnings and profits derived from apportionable business income, they are eliminated in computing the California measure of tax (R&TC Section 25106). In determining whether a dividend is paid out of apportionable business income, distributions are deemed to be paid first out of current earnings and profits and then out of prior years' accumulation in reverse order of accumulation. Distributions paid out of nonbusiness income or distributions from earnings and profits accumulated prior to the time the payor corporation became a member of the combined group are not eliminated from the income of the recipient corporation (although such dividends may be subject to deduction under R&TC Section 24402).

Unitary Partnerships

When a corporation is a partner in a partnership and the partnership's activities are unitary with the corporation's activities (disregarding ownership requirements), then the corporation's share of the partnership's trade or business is combined with the corporation's trade or business (see 18 Cal. Code Regs. Section 25137-1). For example, assume that Corporation A has a 20% partnership interest in Partnership P, and the activities of Corporation A and Partnership P are unitary. The apportionment factors for A and P are as follows:

	EVERYWHERE		CALIFORNIA	
	Corporation A	Partnership P	Corporation A	Partnership P
Property	400,000	250,000	300,000	75,000
Payroll	100,000	50,000	50,000	25,000
Sales	500,000	300,000	400,000	100,000

Corporation A's 20% share of Partnership P's property, payroll and sales are included in the combined apportionment factor:

		EVERYWHERE	CALIFORNIA	FACTOR
Combined Property:	Corporation A	400,000	300,000	70%
	Partnership P (20%)	50,000	15,000	
	Combined	450,000	315,000	
Combined Payroll:	Corporation A	100,000	50,000	50%
	Partnership P (20%)	10,000	5,000	
	Combined	110,000	55,000	
Combined Sales:	Corporation A	500,000	400,000	75%
	Partnership P (20%)	60,000	20,000	
	Combined	560,000	420,000	
Combined x 2				150%
Average Apportionment Factor				67.5%

Net business income for Corporation A and Partnership P was \$300,000 and \$100,000 respectively. Assuming that Corporation A's distributive share of Partnership P's profits and losses was also 20%, Corporation A's net income apportioned to California would be:

Corporation A net business income	\$300,000
Corporation A's distributive share of Partnership P's net business income (\$100,000 x 20%)	20,000
	<u>320,000</u>
Multiplied by combined apportionment factor	x 67.5%
Corporation A's net income apportioned to California	<u>\$216,000</u>

Net Operating Losses (NOLs)

California incorporates, with specific modifications, the provisions of IRC Section 172, concerning carryovers of NOLs incurred in the conduct of a trade or business. In general, California law allows 50% of the NOLs incurred in income years beginning on or after January 1, 1987, to be carried forward for up to 5 years. For any NOL carryover for which a deduction was not allowed in 1991 or 1992 due to the R&TC Section 24416.3 suspension of NOL carryovers, the carryover period shall be extended as follows:

1. By two years, for losses sustained in income years beginning prior to January 1, 1991.
2. By one year, for losses sustained in income years beginning in 1991.

For income years beginning on or after January 1, 1994, new businesses may carry over 100% of the NOL incurred during the first 3 years of operation. The carryover period is 8 years for losses incurred in the first income year of business, 7 years for losses incurred in the second year of business, and 6 years for losses incurred in the third year.

In addition, small businesses may carry over 100% of a NOL incurred in income years

beginning on or after January 1, 1994. The carryover period is 5 years. A small business is a business with total receipts of less than \$1,000,000 during the income year.

For more information regarding "eligible small business" and "new business" net operating losses, get FTB Legal Ruling 96-5.

California does not have a provision for NOL carrybacks.

For income years where the taxpayer has a water's-edge election in effect, the deduction of an NOL carryover is not allowed to the extent that such NOL was determined by taking into account the income and factors of a bank or corporation that would not have been included in the combined report if a water's-edge election had been in effect in the year in which the loss was incurred.

Further information regarding the general NOL carryover can be found in form FTB 3805Q, Net Operating Loss (NOL) Computation and NOL and Disaster Loss Limitations — Corporations. California also has special NOL provisions for losses incurred in enterprise zones, program areas, and the Los Angeles Revitalization Zone and Local Agency Military Base Recovery Areas. For further information regarding these NOLs, see R&TC

Sections 24416 through 24416.3, and form FTB 3805Z, Enterprise Zone and Program Area Business Booklet, form FTB 3806, Los Angeles Revitalization Zone Booklet and form FTB 3807, Local Agency Military Base Recovery Areas.

Application of NOL Carryovers in a Combined Report

The NOL for each taxpayer in the combined group is determined by adjusting each taxpayer's share of the unitary business income or loss by any nonbusiness income or loss. In a subsequent year when a member of the group has positive net income, only the amount of NOL **attributable to that particular taxpayer** may be deducted. The example below shows the computations involved in determining and applying an NOL in a combined report.

Another example of an NOL is shown in Schedule 4-E in the comprehensive example beginning on page 18 of this booklet. Although unitary business income apportioned to each taxpayer in that example was positive, a nonbusiness loss caused Corporation C to have a net loss for California. Fifty percent of that loss will be available to be carried forward to subsequent years, although a deduction will only be allowed from California net income apportioned or allocated to Corporation C.

YEAR 1:	Corp. X	Corp. Y	Corp. Z	Combined
Unitary business income (loss) subject to apportionment	(400,000)	(10,000)	60,000	(350,000)
Apportionment percentages	5%	1%	3%	9%
Loss apportioned to California (Combined loss x %)	(17,500)	(3,500)	(10,500)	(31,500)
Nonbusiness items wholly attributable to California	50,000	(2,500)	0	
California net income (loss)	<u>32,500</u>	<u>(6,000)</u>	<u>(10,500)</u>	
NOL available to be carried forward (50% of loss)	0	(3,000)	(5,250)	

YEAR 2:	Corp. X	Corp. Y	Corp. Z	Combined
Unitary business income (loss) subject to apportionment	50,000	80,000	(5,000)	125,000
Apportionment percentages	6%	4%	4%	14%
Income apportioned to California (Combined income x %)	7,500	5,000	5,000	17,500
Nonbusiness items wholly attributable to California	2,500	(10,000)	0	
California net income (loss) before carryover	10,000	(5,000)	5,000	
Application of NOL carryover from Year 1	0	0	(5,000)	
California net income (loss)	<u>10,000</u>	<u>(5,000)</u>	<u>0</u>	

	Corp. X	Corp. Y	Corp. Z
Remaining NOL from Year 1		(3,000)	(250)
50% of loss in Year 2		(2,500)	
NOL available to be carried forward	0	(5,500)	(250)

Alternative Minimum Tax

Generally, the calculation of alternative minimum taxable income (AMTI) must incorporate the same concepts used in the calculation of regular California taxable income. The AMTI of the members of a combined group must therefore be allocated or apportioned to California and to each member in the same manner as is regular taxable income. The AMT NOL is computed based upon AMTI, and is determined for each member of the combined group using the computations described on page 7.

The calculation of AMTI includes an adjustment that represents 75% of the difference between the adjusted current earnings (ACE) of the corporation over the AMTI determined without regard to the ACE adjustment or the AMT NOL deduction (pre-adjustment AMTI). To compute this adjustment, the ACE of the members of a combined group must be allocated or apportioned in the same manner as regular taxable income and AMTI. Each taxpayer member must compare the ACE, after apportionment and allocation to California (California source ACE), with its pre-ACE adjusted AMTI, after apportionment and allocation to California (California source pre-adjusted AMTI).

If California source ACE exceeds California source pre-adjusted AMTI (a positive ACE adjustment), 75% of the difference must be added to California source pre-adjusted AMTI. On the other hand, if California source pre-adjusted AMTI exceeds the ACE (a negative ACE adjustment), the negative adjustment may be applied to reduce California source pre-adjusted AMTI only to the extent that the aggregate positive California source ACE adjustments in prior years for that particular taxpayer member exceeded its aggregate negative ACE California source adjustments. See FTB Legal Ruling 94-3.

The computations necessary to calculate AMT for taxpayers in a combined report are shown in Schedule 5 of the comprehensive example beginning on page 19 of this publication.

Election to File a Group Return

As a convenience, the FTB has adopted procedures under which some or all of the taxpayer members of a combined reporting group may elect to file a group return. The group return satisfies the requirement of each electing member to file its own return. The tax liability of each member of the unitary group must be computed using the combined reporting procedures described in this booklet. Each member incorporated, qualified to do business or doing business in this state must pay at least the minimum franchise tax set forth in R&TC Sections 23153 and 23181. The tax liabilities of the electing group members are then aggregated and reported on the group return. Filing a group return does not change the tax liabilities of the taxpayer members.

The designated "key corporation" makes the election on behalf of itself and the electing members by completing Schedule R-7 (Form 100, Schedule R), and attaching the schedule to the return. By filing a group return and the completed Schedule R-7, each electing member indicates acceptance of all terms and conditions set forth in the Schedule R-7 and instructions. The elec-

tion is binding for the income year of the election and for all matters pertaining to the income year of the election. If estimated payments are made by the key corporation on behalf of the electing members prior to the initial filing of the Schedule R-7 (or prior to the filing of a Schedule R-7 which reflects a change in the electing members), the key corporation should, at the time of payment, provide the name and corporation number of all members intending to make the election.

To be eligible, each corporation must: 1) be a member of a single unitary group for the entire income year; 2) have the same income year as the key corporation or the income year is wholly included within the income year of the key corporation; and 3) have the same statutory filing date as the key corporation for the income year.

Exceptions — Where Group Return Is Not Allowed

Except as provided above, because of statutory filing requirements, California taxpayer corporations that have different accounting periods may not be included in a group return. The business income of such corporations must be apportioned in accordance with the instructions for corporations that have different accounting periods (see page 5) and reported on a separate return.

Corporations may not file a group return if more than one unitary business is being conducted by any one taxpayer. For further information, get Schedule R, Schedule R-7 and their instructions.

Example of Combined Report Computations and Schedules

The following is an example of how the combined report approach is applied:

Corporation A, the parent corporation, and its subsidiaries B, C, D and E engage in a unitary business of manufacturing and selling items of tangible personal property. Corporations A, B, C and E compute their income on a calendar year basis and Corporation D computes its income on the basis of a September 30 fiscal year end. Since the income of the members of the group was earned evenly throughout the year, interim closings of the books were unnecessary in this example.

Corporation A, a California domiciliary, manufactures a product, some of which it sells to its subsidiaries at cost. Corporation A has \$100,000 interest income from its outstanding accounts receivable, \$60,000 of which was attributable to California receivables. Losses of \$100,000 were attributable to sales of obsolete equipment. The total gross receipts from the sales were \$170,000, \$68,000 of which were attributable to California. In addition to income from its unitary business activity, Corporation A had dividend income of \$100,000 from nonbusiness investments and a \$30,000 nonbusiness partnership loss from an oil and gas limited partnership operating entirely within California. The partnership had tax preference items for depletion and intangible drilling costs, of which Corporation A's distributive share was \$40,000 and \$10,000 respectively. After the tax preference items were applied, Corporation A's net nonbusiness AMTI attributable to the partnership was a positive \$20,000.

Corporation B operates outside California but has some mail order sales to California customers. This example assumes that Corporation B is not taxable in California. (For further discussion of taxability within the state, refer to FTB Pub.

1050, Application and Interpretation of Public Law 86-272). Corporation B also derives interest income from its outstanding accounts receivable. During the year, Corporation B sold a fixed asset to Corporation D for a gain of \$150,000. As explained in the section entitled "Adjustments for Intercorporate Transactions" on page 6, the gain was deferred.

Sixty percent of the stock of Corporation C, a retailer of goods manufactured by Corporation A, was acquired by Corporation A on July 1 from an unrelated individual. Because of the economic relationship that existed prior to the acquisition, Corporation C became a member of the unitary group immediately upon acquisition. Because a short period federal return was not required, Corporation C was not required to file a short period return for California as a result of the acquisition but did an interim closing of its books on July 1. Corporation C also has business rental income from leasing a portion of the ground floor of its headquarters to unrelated third parties. Corporation C was a limited partner in an oil and gas partnership operated within California and incurred a \$150,000 partnership loss. The partnership had a December 31 year end. The partnership had tax preference items for depletion and intangible drilling costs, of which Corporation C's distributive share was \$200,000 and \$15,000 respectively. After the tax preference items were applied, Corporation C's net non-business AMTI attributable to the partnership was a positive \$65,000.

The following schedules show the income computations for Corporations A, B, C, D and E under the combined report approach:

Schedule 1: Computation of combined net income subject to apportionment. For Corporations A, B and E, this schedule reflects items of income and deduction for the calendar year ending 12/31/96. For Corporation C, only income and deductions incurred during the post-acquisition period of 7/1/96 through 12/31/96 are included. If the interim closing of the books method had been used to determine Corporations D's income for the 12/31/96 income year, then Corporation D's actual income for the calendar year would have been included in this schedule. In this example, however, Corporation D is using the pro-rata method of combining corporations with different accounting periods. Adjustments to convert Corporation D's income to the common year end are shown on Schedule 2.

Schedule 2: Computations to place Corporation D income and apportionment factors on a calendar year basis. The schedule calculates 9/12 of the income and deductions from the period ending 9/30/96, and 3/12 of the income and deductions from the period ending 9/30/97 to derive the income and deductions assigned to the 12/31/96 calendar year. The property, payroll and sales are calculated and included in the same manner.

Schedule 3: Calculation of combined interest offset.

Schedule 4: Combined apportionment formula and entity income assignment. This schedule first computes the combined property, payroll and sales within and outside California (Schedule 4-A through 4-C). For Corporation D the property, payroll and sales figures are from Schedule 2. On Schedule 4-D, the combined California apportionment percent is computed and is then multiplied by the combined unitary business income (from Schedule 1-A) to arrive at the group's combined business income apportioned to California. The relative apportionment percent is then computed for each California taxpayer corporation and each taxpayer is assigned its relative share of the group's California business income.

Corporation A's share of California business income is adjusted by nonbusiness income attributable to California, and the interest offset is applied.

The California business income of Corporation C is adjusted by its nonbusiness loss to derive its net income for state purposes for the period 7/1/96 through 12/31/96. This figure is combined with Corporation C's separate income for the period 1/1/96 through 6/30/96 to arrive at Corporation C's net income for the entire calendar year. In this example, Corporation C has a net loss, 50% of which will be available to be carried forward and applied against Corporation C's net income in subsequent years.

The California business income assigned to Corporation D for the 1996 calendar year period is adjusted by 9/12, and is combined with 3/12 of the 1995 calendar year income (from the prior year calculation) to arrive at Corporation D's net income for its 9/30/96 fiscal period.

Schedule 5: Computations of combined alternative minimum taxable income (Schedule 5-A), the ACE adjustment (Schedule 5-B), and alternative minimum tax (Schedule 5-C) for each taxpayer corporation.

In this example, Corporation A and Corporation E may elect to file a group return. The aggregate tax amount that would be reported on the group return would be \$41,143 (\$23,850 for Corporation A, \$17,293 for Corporation E). Neither Corporation C nor Corporation D is eligible to be included in a group return (Corporation C is a part-year member whose net income includes its separate income from the pre-acquisition period, and Corporation D files its returns on a different year end from the remainder of the group). Corporation C and Corporation D must therefore file their own returns and include a copy of the combined report computations.

The computations involved in the above steps are shown on the following pages.

Please identify the corporation by providing the complete name as registered with the Secretary of State for each corporation qualified to do business or incorporated in California and the California ID number and/or the Federal ID number.

For example: **Corporation A**

CA #9512345
FEIN #12-3456789

SCHEDULE 1 — COMBINED INCOME SUBJECT TO APPORTIONMENT

1-A: COMBINED PROFIT & LOSS STATEMENT AS OF 12/31/96

	CORP A	CORP B	CORP C (7/1/96-12/31/96)	CORP D (from Sch. Z)	CORP E	TOTAL BEFORE ADJUSTMENT	INTRA-GROUP ADJUSTMENTS	COMBINED
California ID Number								
Federal ID Number								
Net sales	\$7,000,000	\$4,000,000	\$1,900,000	\$2,600,000	\$3,000,000	\$18,500,000	(\$500,000)	\$18,000,000
Cost of goods sold	(5,900,000)	(2,500,000)	(1,000,000)	(1,500,000)	(2,000,000)	(12,900,000)	500,000	(12,400,000)
Gross profit	\$1,100,000	\$1,500,000	\$900,000	\$1,100,000	\$1,000,000	\$5,600,000	\$0	\$5,600,000
Dividends	350,000					350,000		350,000
Interest on U.S. obligations						0		0
Other interest	100,000	70,000	10,000	60,000		180,000	(10,000)	170,000
Gross rents						60,000		60,000
Gross royalties						0		0
Net gains and losses	(100,000)	150,000				50,000	(150,000)	(100,000)
Other income (partnership loss)	(30,000)		(150,000)			(180,000)		(180,000)
Total Income	\$1,420,000	\$1,720,000	\$820,000	\$1,100,000	\$1,000,000	\$6,060,000	(\$160,000)	\$5,900,000
Compensation of officers	300,000					300,000		300,000
Salaries & wages	430,000	1,000,000	350,000	570,000	600,000	2,950,000		2,950,000
Repairs						0		0
Bad debts						0		0
Rents	4,800	30,000	8,000	7,200		50,000		50,000
Taxes	99,000	20,000	5,000	26,000	22,000	172,000		172,000
Interest	250,000	10,000				260,000	(10,000)	250,000
Contributions						0		0
Depreciation	150,000	50,000	37,000	63,000	23,000	323,000		323,000
Depletion						0		0
Advertising						0		0
Pension, profit-sharing, etc., plans	25,000					25,000		25,000
Employee benefit plans	75,000					75,000		75,000
Other deductions						0		0
Total Deductions	\$1,333,800	\$1,110,000	\$400,000	\$666,200	\$645,000	\$4,155,000	(\$10,000)	\$4,145,000
NET INCOME BEFORE STATE ADJUSTMENTS	\$86,200	\$610,000	\$420,000	\$433,800	\$355,000	\$1,905,000	(\$150,000)	\$1,755,000

SCHEDULE 1 — COMBINED INCOME SUBJECT TO APPORTIONMENT

1-B: STATE ADJUSTMENTS, NONBUSINESS INCOME AND BUSINESS INCOME SUBJECT TO APPORTIONMENT

	CORP A	CORP B	CORP C	CORP D	CORP E	TOTAL BEFORE ADJUSTMENT	INTRA-GROUP ADJUSTMENTS	COMBINED
NET INCOME BEFORE STATE ADJUSTMENTS	\$86,200	\$610,000	\$420,000	\$433,800	\$355,000	\$1,905,000	(\$150,000)	\$1,755,000
ADD:								
Taxes measured by income	\$5,000	\$1,000	\$4,000	\$2,000	\$2,000	\$12,000		\$12,000
California Bank & Corporation tax	12,000		1,000	23,000	19,000	55,000		55,000
Interest on government obligations						0		0
Capital gain/loss adjustments	10,000					10,000		10,000
Excess depreciation	5,000	3,000	6,000	5,000	(1,000)	18,000		18,000
Excess amortization						0		0
Other additions						0		0
Total Additions	\$32,000	\$4,000	\$11,000	\$28,000	\$20,000	\$95,000		\$95,000
DEDUCT:								
Intercompany dividends (Sec. 25106)	\$200,000					\$200,000		\$200,000
Other dividends (Sec. 24402, 24410)	50,000					50,000		50,000
Water's-edge dividend deduction						0		0
Capital gain/loss adjustments						0		0
Additional contributions						0		0
Net interest deduction (enterprise zones)						0		0
Other deductions						0		0
Total Deductions	\$250,000	\$0	\$0	\$0	\$0	\$250,000		\$250,000
NET INCOME AFTER STATE ADJUSTMENTS	(\$131,800)	\$614,000	\$431,000	\$461,800	\$375,000	\$1,750,000	(\$150,000)	\$1,600,000
REVERSE NONBUSINESS ITEMS								
Show as: (INCOME)/LOSS:								
Dividends not deducted above	(100,000)					(100,000)		(100,000)
Interest						0		0
Net rental (income)/loss						0		0
Royalties						0		0
(Gain)/loss from sale of assets						0		0
Partnership (income)/loss	30,000		150,000			180,000		180,000
Miscellaneous (income)/loss						0		0
	(\$201,800)	\$614,000	\$581,000	\$461,800	\$375,000	\$1,830,000	(\$150,000)	\$1,680,000
Interest Offset from Schedule 3								80,000
UNITARY BUSINESS INCOME SUBJECT TO APPORTIONMENT								<u>1,760,000</u>

**SCHEDULE 2 — COMPUTATIONS TO PLACE CORP D INCOME AND
APPORTIONMENT FACTORS ON A CALENDAR YEAR BASIS**

	9/30/96 ACTUAL	9/12 of 9/30/96	9/30/97 ACTUAL	3/12 of 9/30/97	TOTAL 12/31/96
Net sales	\$2,800,000	\$2,100,000	\$2,000,000	\$500,000	\$2,600,000
Cost of goods sold	(\$1,600,000)	(\$1,200,000)	(\$1,200,000)	(\$300,000)	(\$1,500,000)
Gross profit	\$1,200,000	\$900,000	\$800,000	\$200,000	\$1,100,000
Salaries & wages	\$600,000	\$450,000	\$480,000	\$120,000	\$570,000
Rents	\$7,200	\$5,400	\$7,200	\$1,800	\$7,200
Taxes	\$28,000	\$21,000	\$20,000	\$5,000	\$26,000
Depreciation	\$60,000	\$45,000	\$72,000	\$18,000	\$63,000
California Bank & Corporation Tax	\$24,000	\$18,000	\$20,000	\$5,000	\$23,000
Excess depreciation	\$4,000	\$3,000	\$8,000	\$2,000	\$5,000
Nonbusiness income items	\$0	\$0	\$0	\$0	\$0
Property everywhere (year end)					
Inventory	\$128,000	\$96,000	\$176,000	\$44,000	\$140,000
Fixed depreciable assets	\$420,000	\$315,000	\$500,000	\$125,000	\$440,000
Land	\$10,000	\$7,500	\$10,000	\$2,500	\$10,000
California property (year end)					
Inventory	\$12,000	\$9,000	\$20,000	\$5,000	\$14,000
Fixed depreciable assets	\$24,000	\$18,000	\$28,000	\$7,000	\$25,000
Rent expense	\$1,800	\$1,350	\$1,800	\$450	\$1,800
Payroll everywhere	\$696,000	\$522,000	\$540,000	\$135,000	\$657,000
California payroll	\$16,000	\$12,000	\$100,000	\$25,000	\$37,000
Sales everywhere	\$2,800,000	\$2,100,000	\$2,000,000	\$500,000	\$2,600,000
California sales	\$716,000	\$537,000	\$1,000,000	\$250,000	\$787,000

Note: The Total column is the sum of the 9/12 column and the 3/12 column.

SCHEDULE 3 — CALCULATION OF COMBINED INTEREST OFFSET

	COMBINED TOTALS	
1 Total interest expense deducted	\$260,000	
2a Water's-edge offset (from form FTB 2424)	0	
b Intercompany interest expense	(10,000)	
c Nonbusiness interest expense	0	
3 Net interest expense (amount on line 1 less amounts on line 2a, line 2b and line 2c)		\$250,000
4 Total interest income	\$180,000	
5 Less nonbusiness interest income	0	
6 Less intercompany interest income	(10,000)	
7 Business interest income		\$170,000
8 Balance: line 3 minus line 7, but not less than zero		<u>\$80,000</u>
9 Total dividend income	\$350,000	
10a Less Water's-edge dividends deducted	0	
b Less intercompany dividends deducted	(200,000)	
c Other dividends deducted (R&TC Secs. 24402 and 24410)	(50,000)	
11 Balance	\$100,000	
12 Business dividend income	0	
13 Net nonbusiness dividend income (line 11 minus line 12)		<u>\$100,000</u>
14 Total nonbusiness interest and dividends (line 5 plus line 13)		<u>\$100,000</u>
15 Interest offset (Assignable 100% to Corp. A): (enter lesser of line 8 or line 14)		<u>\$80,000</u>

In the example only one entity has nonbusiness dividend income. If more than one entity had nonbusiness interest and/or nonbusiness dividend income, the interest offset would be prorated between entities by the ratio of each entity's nonbusiness interest and/or nonbusiness dividends to the total nonbusiness interest and nonbusiness dividends.

Note: A contributions adjustment applicable to nonbusiness income of multiple entities may also require such computations.

SCHEDULE 4 — COMBINED APPORTIONMENT FORMULA AND ENTITY INCOME ASSIGNMENT

4-A: COMBINED APPORTIONMENT DATA

PROPERTY FACTOR	CORP A	CORP B	CORP C	CORP D	CORP E	COMBINED
Property everywhere						
Inventory – 12/31/96	100,000	150,000		140,000	120,000	
Fixed depreciable assets – 12/31/96	1,100,000	310,000	See Monthly Average	440,000	400,000	
Land – 12/31/96	50,000	0	Average	10,000	100,000	
Less intercompany profit included above	0	0	Computation	(150,000)	0	
Total – end of year	1,250,000	460,000	(Sch. 4-B)	440,000	620,000	
Total – beginning of year (from 1995 report)	1,370,000	575,000		755,000	580,000	
Total beginning and ending	2,620,000	1,035,000		1,195,000	1,200,000	
Average owned property (divide by 2)	1,310,000	517,500	175,000	597,500	600,000	3,200,000
Rent expense (excluding intercompany and nonbusiness)	4,800	30,000	8,000	7,200	0	50,000
Capitalize (times 8)	38,400	240,000	64,000	57,600	0	400,000
Combined property everywhere	1,348,400	757,500	239,000	655,100	600,000	3,600,000
California property						
Inventory – 12/31/96	41,000	0		14,000	95,000	
Fixed depreciable assets – 12/31/96	400,000	0	See Monthly Average	25,000	330,000	
Land – 12/31/96	20,000	0	Average	0	70,000	
Less intercompany profit included above	0	0	Computation	0	0	
Total – end of year	461,000	0	(Sch. 4-B)	39,000	495,000	
Total – beginning of year (from 1995 report)	427,000	0		47,000	453,000	
Total beginning and ending	888,000	0		86,000	948,000	
Average owned property (divide by 2)	444,000	0	175,000	43,000	474,000	1,136,000
Rent expense (excluding intercompany and nonbusiness)	1,200	0	8,000	1,800	0	11,000
Capitalize (times 8)	9,600	0	64,000	14,400	0	88,000
Combined California property	453,600	0	239,000	57,400	474,000	1,224,000

SCHEDULE 4 — COMBINED APPORTIONMENT FORMULA AND ENTITY INCOME ASSIGNMENT

**4-B: COMPUTATION OF AVERAGE PROPERTY VALUES FOR CORP C
(PARTIAL YEAR COMBINATION)**

MONTHLY AMOUNTS TO BE INCLUDED IN THE COMBINED PROPERTY FACTOR	INVENTORY	FIXED DEPRECIABLE	LAND	TOTAL
	January	\$0	\$0	\$0
February	0	0	0	\$0
March	0	0	0	\$0
April	0	0	0	\$0
May	0	0	0	\$0
June	0	0	0	\$0
July	10,000	260,000	30,000	\$300,000
August	50,000	260,000	30,000	\$340,000
September	60,000	260,000	30,000	\$350,000
October	70,000	260,000	30,000	\$360,000
November	80,000	260,000	30,000	\$370,000
December	90,000	260,000	30,000	\$380,000
TOTAL	\$360,000	\$1,560,000	\$180,000	\$2,100,000
AVERAGE	\$30,000	\$130,000	\$15,000	\$175,000

NOTE: All of Corporation C's owned tangible property is located in California, so the same amounts will be included in both the numerator and denominator of the property factor (see Schedule 4-A).

SCHEDULE 4 — COMBINED APPORTIONMENT FORMULA AND ENTITY INCOME ASSIGNMENT

4-C: COMBINED APPORTIONMENT DATA

	CORP A	CORP B	CORP C	CORP D	CORP E	COMBINED
PAYROLL FACTOR						
Payroll everywhere	1,630,000	1,293,000	420,000	657,000	750,000	4,750,000
California payroll	553,000	0	210,000	37,000	530,000	1,330,000

SALES FACTOR

Sales everywhere						
Gross receipts, less returns and allowances	7,000,000	4,000,000	1,900,000	2,600,000	3,000,000	18,500,000
Other gross receipts (rents, royalties, etc.)	270,000	70,000	60,000	0	0	400,000
Less intercompany receipts	(500,000)	0	0	0	0	(500,000)
Total sales everywhere	6,770,000	4,070,000	1,960,000	2,600,000	3,000,000	18,400,000

California sales

Sales delivered or shipped to California purchasers:

i) Shipped from outside California	3,000,000	1,203,000				1,203,000
ii) Shipped from within California			1,190,000	787,000	1,292,000	6,269,000

Sales shipped from California by a unitary member to:

i) The United States Government						0
ii) Purchasers in a state where the corporation and all of its unitary affiliates are immune under Public Law 86-272	100,000					100,000
Other gross receipts (rents, royalties, etc.)	128,000		60,000			188,000
Less intercompany receipts	(400,000)					(400,000)
Total California sales	2,828,000	1,203,000	1,250,000	787,000	1,292,000	7,360,000

SCHEDULE 4 — COMBINED APPORTIONMENT FORMULA AND ENTITY INCOME ASSIGNMENT

4-D: COMBINED APPORTIONMENT FACTORS AND ENTITY INCOME ASSIGNMENT

	CORP A	CORP B	CORP C	CORP D	CORP E	COMBINED
1 EVERYWHERE: Property						3,600,000
2 Payroll						4,750,000
3 Sales						18,400,000
4 CALIFORNIA: Property	453,600	0	239,000	57,400	474,000	1,224,000
5 Payroll	553,000	0	210,000	37,000	530,000	1,330,000
6 Sales	2,828,000	1,203,000	1,250,000	787,000	1,292,000	7,360,000
COMBINED CALIFORNIA APPORTIONMENT PERCENT (California property, payroll, sales divided by combined property, payroll, sales)						
7 Property	12.6000%	0.0000%	6.6389%	1.5944%	13.1667%	34.0000%
8 Payroll	11.6421%	0.0000%	4.4211%	0.7789%	11.1579%	28.0000%
9 Sales	15.3696%	6.5380%	6.7935%	4.2772%	7.0127%	80.0000%
9a Sales percentage (line 9) multiplied by 2	30.7391%	13.0761%	13.5870%	8.5543%	14.0435%	142.0000%
10 Total						35.5000%
11 AVERAGE CALIFORNIA APPORTIONMENT PERCENT (Divide by 4)						\$1,760,000
12 UNITARY BUSINESS INCOME TO BE APPORTIONED						\$624,800
13 COMBINED INCOME APPORTIONED TO CALIFORNIA (Multiply line 11 by line 12)						
ENTITY INCOME ASSIGNMENT (excluding Corp B – not subject to tax)						
14 Property factor (line 7)	12.6000%		6.6389%	1.5944%	13.1667%	34.0000%
15 Payroll factor (line 8)	11.6421%		4.4211%	0.7789%	11.1579%	28.0000%
16 Sales factor (line 9a)	30.7391%		13.5870%	8.5543%	14.0435%	66.9239%
17 Total	54.9812%		24.6469%	10.9277%	38.3680%	128.9239%
18 Average percent (divide by 4)	13.7453%	0.0000%	6.1617%	2.7319%	9.5920%	32.2310%
19 Relative percent (line 18 average factor for each entity divided by line 18 combined average)	42.6463%	0.0000%	19.1174%	8.4761%	29.7602%	100.0000%
20 BUSINESS INCOME ASSIGNED TO CALIFORNIA (Line 13 x line 19)	\$266,454	\$0	\$119,446	\$52,959	\$185,942	\$624,800

SCHEDULE 4 — COMBINED APPORTIONMENT FORMULA AND ENTITY INCOME ASSIGNMENT

4-E: CALIFORNIA NET INCOME

	CORP A 1/1/96-12/31/96	CORP B None	CORP C 7/1/96-12/31/96	CORP D 10/1/95-9/31/96	CORP E 1/1/96-12/31/96
BUSINESS INCOME APPORTIONED TO CALIFORNIA					
CORP A (from Schedule 4-D)	\$266,454				
CORP C (from Schedule 4-D)			\$119,446		
CORP D:					
For 12 months ended 12/96 (from Schedule 4-D)				\$52,959	
Portion reportable in current year (9/12)				\$39,719	
For 12 months ended 12/95 (prior year calculation)				\$50,000	
Portion reportable in current year (3/12)				\$12,500	
CORP D Total for year ended 9/31/96				\$52,219	
CORP E (from Schedule 4-D):					\$185,942
Nonbusiness income or losses wholly					
Attributable to California					
Dividends	100,000				
Net rental income/(loss)					
Gain/(loss) on sale of assets					
Partnership income (loss)	(30,000)		(150,000)		
Total	\$336,454	\$0	(\$30,554)		\$52,219
Interest offset (from Schedule 3)	\$80,000				\$185,942
Net income before contributions adjustment	\$256,454	\$0	(\$30,554)		\$52,219
Contributions adjustment					
Add California separate net income for pre-acquisition period					
1/1/96-6/30/96 (cannot be included in the combined report)			25,000		
Net income for state purposes	\$256,454	\$0	(\$5,554)		\$52,219
Franchise Tax (9.3% tax rate)	\$23,850	\$0	\$800		\$4,856
Alternative Minimum Tax (from Schedule 5-C)	\$0	\$0	\$12,978		\$0
TOTAL TAX	\$23,850	\$0	\$13,778		\$4,856
					\$17,293

SCHEDULE 5 — COMBINED ALTERNATIVE MINIMUM TAX

5-A: ALTERNATIVE MINIMUM TAXABLE INCOME

	CORP A	CORP B	CORP C	CORP D	CORP E	TOTAL BEFORE ADJUSTMENT	INTRA-GROUP ADJUSTMENTS	COMBINED
1 NET INCOME AFTER STATE ADJUSTMENTS (from Schedule 1-B)	(\$131,800)	\$614,000	\$431,000	\$461,800	\$375,000	\$1,750,000	(\$150,000)	\$1,600,000
AMT ADJUSTMENTS & PREFERENCES:								
2a Depreciation	\$40,000	\$4,000	\$3,000	\$6,000	(\$1,000)	\$52,000	0	\$52,000
2b Basis adjustment in determining gain or loss from sale/exchange	2,000					2,000	0	2,000
2c Depletion	40,000		200,000			240,000		240,000
2d Intangible drilling costs	10,000		15,000			25,000		25,000
3 TOTAL AMTI	(\$39,800)	\$618,000	\$649,000	\$467,800	\$374,000	\$2,069,000	(\$150,000)	\$1,919,000
LESS NONBUSINESS ITEMS (adjusted for AMTI)						0		0
4a Dividends	(100,000)					(100,000)		(100,000)
4b Partnership (income)/loss	(20,000)		(65,000)			(85,000)		(85,000)
Add: Interest offset	80,000					80,000		
5 Unitary business AMTI	(\$79,800)	\$618,000	\$584,000	\$467,800	\$374,000	\$1,964,000	(\$150,000)	\$1,814,000
6 Average apportionment percentage (from Schedule 4-D, line 11)								35.5000%
7 COMBINED BUSINESS AMTI APPORTIONED TO CALIFORNIA								\$643,970
8 Relative percentage (from Schedule 4-D, line 19)	42.6463%	0.0000%	19.1174%	8.4761%	29.7602%			100.0000%
9 Business AMTI assigned to California	\$274,629	\$0	\$123,110	\$54,584	\$191,647			\$643,970
Nonbusiness items assigned to California (adjusted for AMTI)								
10a Dividends	100,000							
10b Partnership income/(loss)	20,000		65,000					
Less: Interest offset	(\$80,000)							
11 PRE-ADJUSTMENT AMTI	\$314,629	\$0	\$188,110	\$54,584	\$191,647			
12 ACE adjustment (from Schedule 5-B)	3,009	0	1,349	598	2,100			
13 ALTERNATIVE MINIMUM TAXABLE INCOME	\$317,638	\$0	\$189,459	\$55,182	\$193,747			

SCHEDULE 5 — COMBINED ALTERNATIVE MINIMUM TAX

5-B: ACE ADJUSTMENT

	CORP A	CORP B	CORP C	CORP D	CORP E	TOTAL BEFORE ADJUSTMENT	INTRA-GROUP ADJUSTMENTS	COMBINED
1 TOTAL AMTI (from Schedule 5-A, line 3)	(\$39,800)	\$618,000	\$649,000	\$467,800	\$374,000	\$2,069,000	(\$150,000)	\$1,919,000
ADJUSTMENT FOR ACE:								
2a Depreciation	25,000	1,500	1,000	(2,000)	500	26,000		26,000
2b Basis adjustment in determining gain or loss from sale/exchange	500					500		500
3 Pre-apport. adjusted current earnings	(\$14,300)	\$619,500	\$650,000	\$465,800	\$374,500	\$2,095,500	(\$150,000)	\$1,945,500
LESS NONBUSINESS ITEMS								
(adjusted for ACE):								
4a Dividends	(100,000)					(100,000)		(100,000)
4b Partnership (income)/loss	(20,000)		(65,000)			(85,000)		(85,000)
Add: interest offset	\$80,000					\$80,000		\$80,000
5 Preapportionment business ACE						\$1,990,500	(\$150,000)	\$1,840,500
6 Average apportionment percentage (from Schedule 4-D, line 11)								35.5000%
7 COMBINED BUSINESS ACE APPORTIONED TO CALIFORNIA								\$653,378
8 Relative percentage (from Schedule 4-D, line 19)	42.6463%	0.0000%	19.1174%	8.4761%	29.7602%			100.0000%
9 Business ACE assigned to California	\$278,641	\$0	\$124,909	\$55,381	\$194,447			\$653,378
Nonbusiness items assigned to California (adjusted for ACE)								
10a Dividends	100,000							
10b Partnership income/(loss)	20,000		65,000					
Less: interest offset	(\$80,000)							
11 ADJUSTED CURRENT EARNINGS	\$318,641	\$0	\$189,909	\$55,381	\$194,447			
12 Pre-adjustment AMTI (Schedule 5-A, line 11)	\$314,629	0	\$188,110	\$54,484	\$191,647			
13 Difference	\$4,012	\$0	\$1,798	\$797	\$2,800			
14 75% of Difference	3,009	0	1,349	598	2,100			
15 Negative ACE limitation: for each taxpayer excess of aggregate prior year positive line 16 ACE adjustments over aggregate prior year negative line 16 ACE adjustments:	0	0	0	0	0	0	0	0
16 ACE ADJUSTMENT*	\$3,009	\$0	\$1,349	\$598	\$2,100			

*If line 14 is negative, it is allowed as a negative ACE adjustment only to the extent of that taxpayer's cumulative net California ACE from prior years.

SCHEDULE 5 — COMBINED ALTERNATIVE MINIMUM TAX

5-C: ALTERNATIVE MINIMUM TAX

	CORP A 1/1/96-12/31/96	CORP B None	CORP C 1/1/96-12/31/96	CORP D 10/1/95-9/31/96	CORP E 1/1/96-12/31/96
AMTI APPORTIONED TO CALIFORNIA (from Schedule 5-A)					
CORP A	\$317,638		\$189,459		
CORP C			\$30,000		
Add California separate AMTI for pre-acquisition period 1/1/96-6/30/96 (computation not shown)					
CORP D				\$55,182	
For 12 months ended 12/96					
Portion reportable in current year (9/12)				\$41,387	
For 12 months ended 12/95 (from prior year calculation)				\$53,000	
Portion reportable in current year (3/12)				\$13,250	
CORP D Total				\$54,637	
CORP E					\$193,747
AMTI ADJUSTED FOR EACH CORPORATION					
INCOME YEAR	\$317,638	0	\$219,459		\$54,637
Less exemption (subject to phaseout when AMTI exceeds \$150,000)					
AMTI subject to tax	0		(\$22,635)		(\$40,000)
	\$317,638	\$0	\$196,824		\$14,637
Tentative minimum tax (7% tax rate)					
	\$22,235	\$0	\$13,778		\$1,025
Less regular franchise or income tax (from Schedule 4-E)					
ALTERNATIVE MINIMUM TAX	\$23,850	0	800		\$4,856
	\$0	\$0	\$12,978		\$0

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How To Get California Tax Information

Regular Toll-Free Phone Service

Our regular toll-free phone service is available from 7:00 a.m. until 8:00 p.m. Monday through Friday from January 2 through April 15, 1997. The best times to call are between 7:00 and 10:00 in the morning and between 6:00 and 8:00 in the evening. Service is also available on Saturday, April 5 and April 12, from 8:00 a.m. until 5:00 p.m. After April 15, service is available Monday through Friday, between 8:00 a.m. and 5:00 p.m.

From within the United States 1-800-852-5711
From outside the United States 1-916-845-6500
(not toll-free)
For hearing impaired with TDD 1-800-822-6268
For federal tax questions,
call the IRS at 1-800-829-1040

Bilingual Assistance

Para obtener servicio bilingüe de información sobre impuestos o formularios, llame al número de teléfono (anotado arriba) que le corresponde.

Letters

We can serve you quickly if you call us for information to complete your California income tax return, or to find out about your tax refund. However, you may want to write to us if you are replying to a notice we sent you, or to get a written reply. If you write to us, be sure to include your California Corporation number or federal employer identification number, your daytime and evening telephone numbers and a copy of the notice with your letter. Send your letter to:

FRANCHISE TAX BOARD
PO BOX 942857
SACRAMENTO CA 94257-0540

We will acknowledge receipt of your letter within six to eight weeks. In some cases, we may need to call you for additional information.

Your Rights As A Taxpayer

Our goal at the FTB is to make certain that your rights are protected so that you will have the highest confidence in the integrity, efficiency and fairness of our state tax system. FTB Pub. 4058, California Taxpayers' Bill of Rights, includes information on your rights as a California taxpayer, the Taxpayers' Rights Advocate Program and how you can request written advice from the FTB on whether a particular transaction is taxable. You can order FTB Pub. 4058 by calling or writing the FTB using the address above for letters.

Where To Get Income Tax Forms

By Internet – If you have Internet access, you may download, view and print California income tax forms and publications. Our Internet address is:

<http://www.ftb.ca.gov>

By phone – Use F.A.S.T. to order the 1996 California tax forms listed to the right. To order a form on the list:

- Call 1-800-338-0505, from within the United States; or
- 1-916-845-6600, from outside the United States (not toll-free)
- Select bank and corporations income tax form requests.
- Enter the three-digit code shown to the left of the form title when you are instructed to do so.

We will send you two copies of each tax form and one copy of each set of instructions. Please allow two weeks to receive your order.

For prior year California tax forms, call our toll-free number listed under "Regular Toll-Free Phone Service."

In person – Most libraries, post offices and banks provide free California tax booklets during the filing season. Many libraries and some quick print businesses have forms and schedules for you to photocopy (you may have to pay a nominal fee). Note that employees at libraries, post offices, banks and quick print businesses cannot provide tax information or assistance.

By mail – Write to: TAX FORMS REQUEST UNIT, FRANCHISE TAX BOARD, PO BOX 307, RANCHO CORDOVA CA 95741-0307.

California Tax Forms and Publications

- 817 California Corporation Tax Forms and Instructions. This booklet contains:
Form 100, California Corporation Franchise or Income Tax Return
- 821 Schedule P (100), Alternative Minimum Tax and Credit Limitations — Corporations
- 822 FTB 3885, Depreciation/Amortization
- 807 FTB 3805Q, Net Operating Loss (NOL) Computation and NOL and Disaster Loss Limitations — Corporations
- 816 California S Corporation Tax Forms and Instructions. This booklet contains:
Form 100S, California S Corporation Franchise or Income Tax Return
- 823 Schedule B(100S), S Corporation Depreciation and Amortization
Schedule C (100S), S Corporation Tax Credits
Schedule H (100S), Dividend Income
- 824 Schedule D (100S), Capital Gains and Losses and Built-In Gains
- 825 Schedule K-1 (100S), Shareholder's Share of Income, Deductions, Credits
- 826 FTB 3830, S Corporation's List of Shareholders and Consents
- 814 Form 109, Exempt Organization Business Income Tax Return
- 818 Form 100-ES, Corporation Estimated Tax
- 813 Form 100X, Amended Corporation Return
- 815 Form 199, Exempt Organization Return
- 819 Schedule R, Apportionment and Allocation of Income
- 812 FTB Pub. 1038, Guide for Corporations Dissolving, Withdrawing or Merging
- 809 FTB Pub. 1060, Guide for Corporations Starting Business in California
- 810 FTB Pub. 1061, Guidelines for Corporations Filing a Combined Report
- 827 Form 100-WE, Water's-Edge Booklet
- 829 FTB 3564, Authorization of Agent Under Revenue and Taxation Code Section 19141.6
- 820 FTB Pub. 1068, Exempt Organizations Requirements for Filing Returns and Paying Filing Fees
- 802 FTB 3500, Exemption Application
- 808 FTB 3539, Payment Voucher for Automatic Extension for Corporations and Exempt Organizations
- 803 FTB 3555, Request for Tax Clearance
- 804 FTB 3557, Application for Revivor
- 811 FTB 3560, S Corporation Election or Termination/Revocation
- 806 FTB 5806, Underpayment of Estimated Tax by Corporations



F.A.S.T. Toll-Free Phone Service

Call Fast Answers about State Taxes, the F.A.S.T. toll-free phone service you can use to:

- Get recorded answers to many of your questions about California taxes; and
- Order current year California tax forms.

F.A.S.T. is available in English and Spanish to callers with touch-tone or rotary dial telephones.

When Is F.A.S.T. Available?

To answer your questions, F.A.S.T. is available 24 hours a day, seven days a week. To order forms F.A.S.T. is available from 6:00 a.m. to 10:00 p.m., seven days a week, except state holidays.

How To Use F.A.S.T.

Have paper and pencil handy to take notes.

Call from within the United States 1-800-338-0505

Call from outside the United States (not toll-free) . . . 1-916-845-6600

Follow the recorded instructions and enter the three-digit code when you are instructed to do so.

To Order Forms

Use F.A.S.T. to order 1996 California tax forms and publications. See the list of forms and instructions for ordering them on page 23.

To Get Information

If you need an answer to any of the following questions, call 1-800-338-0505, select general tax information, follow the recorded instructions and enter the three-digit code when you are instructed to do so.

Code-Filing Assistance:

- 715 – If my actual tax is less than the minimum franchise tax, what figure do I put on line 22 of Form 100?
- 717 – What are the tax rates for corporations?
- 718 – How do I get an extension of time to file?
- 722 – When do I have to file a short-period return?
- 730 – May I claim net operating losses in the first year?
- 731 – Are corporations allowed to use MACRS/ACRS or Section 179 expensing?
- 733 – Can the prepayment to the Secretary of State be applied to my last year of business?
- 734 – What is the difference between franchise tax and income tax?

S Corporations

- 704 – Is an S corporation subject to the minimum franchise tax?
- 705 – Are S corporations required to file estimate payments?
- 706 – What forms do S corporations file?
- 707 – The tax for my S corporation is less than the minimum franchise tax. What figure do I put on line 21 of Form 100S?
- 708 – Where do S corporations make the state tax adjustment on Schedule K-1(100S)?

Exempt Organizations

- 709 – How do I get tax exempt status?
- 710 – Does an exempt organization have to file Form 199?
- 735 – How can an exempt organization incorporate without paying corporation fees and costs?
- 736 – I have exempt status. Do I need to file Form 100 or Form 109 in addition to Form 199?

Minimum Tax and Estimate Tax

- 711 – Why can't I claim my prepayment tax as credit or estimate payment on my return?
- 712 – What is the minimum franchise tax?
- 714 – I'm not doing business; do I have to pay the minimum franchise tax?
- 716 – When are my estimate payments due?

Billings and Miscellaneous Notices

- 723 – I received a bill for \$250. What is this for?
- 728 – Why was my corporation suspended?
- 729 – Why is my subsidiary getting a request for a return when we file a combined report?

Tax Clearance

- 724 – How do I dissolve my corporation?
- 725 – What do I have to do to get a tax clearance?
- 726 – How long will it take to get a tax clearance certificate?
- 727 – My corporation was suspended/forfeited. Can I still get a tax clearance?

Miscellaneous

- 700 – Who do I need to contact to start a business?
- 701 – I need a state ID number for my business. Who do I contact?
- 702 – Can you send me an employer's tax guide?
- 703 – How do I incorporate?
- 719 – How do I properly identify my corporation when dealing with the Franchise Tax Board?
- 720 – How do I change my corporation name?
- 721 – How do I change my accounting period?
- 732 – What is the water's-edge election?
- 737 – Where do I send my payment?
- 738 – What is electronic funds transfer?
- 739 – How do I get a copy of my state corporate tax return?

