

**Illinois Department of Revenue
Regulations**

Title 86 Part 100 Section 100.9700 Unitary Business Group Defined (IITA Section 1501)

TITLE 86: REVENUE

**PART 100
INCOME TAX**

SUBPART BB: DEFINITIONS

Section 100.9700 Unitary Business Group Defined (IITA Section 1501)

- a) **Scope**

This regulation is designed to clarify the meaning of IITA Section 1501(a)(27), defining "unitary business group", which definition became effective for tax years ending on or after December 31, 1982.

- b) **Persons required to use combined apportionment**

Any person subject to Illinois income taxation may be a member of a unitary business group and required to use combined apportionment under IITA Section 304(e). Corporations (other than Subchapter S corporations) who are members of a unitary business group are required to file combined returns under IITA Section 502(e). For the treatment of certain partners and partnerships engaged in a unitary business, see Section 100.3380(d) of this Part. Every member of a unitary business group who is neither a corporation required to join in a combined return nor a partnership excluded from combined apportionment under Section 100.3380 of this Part shall determine the Illinois portion of its business income pursuant to IITA Section 304(e) by computing the combined business income of the unitary business group in the manner prescribed in Section 100.5270(a) of this Part, and apportioning such unitary business income to Illinois using the combined "everywhere" apportionment factors of the unitary business group and that person's own "Illinois" apportionment factors. If one or more other members of the unitary business group have taxable years different from the taxable year of the taxpayer filing the return, that taxpayer shall compute the combined business income of the group for its taxable year by including the incomes of the members using a different taxable year in the manner prescribed by Section 100.5265 of this Part.

- c) **The 80-20 U.S. business activity test for prospective members**

The factors to be used in determining whether 80% or more of a person's business activity is conducted outside the United States shall be gross figures without eliminations premised on the person's membership in any unitary business group. However, the factors should relate to the common taxable year, as defined in Section 100.5265 of this Part, of the unitary business group of which the person being tested could become a member were the person's business activity found to be less than 80% outside the United States. The factors to be used are as follows:

 - 1) persons required to apportion business income under IITA Section 304(a) will use property and payroll,

- 2) persons required to apportion business income under IITA Sections 304(b), 304(c) or 304(d) will use the respective factors prescribed in those provisions.
 - A) In accordance with IITA Section 102 and 26 USC 7701(b)(9), the phrase "United States" as used in IITA Section 1501(a)(27) shall include only the fifty states and the District of Columbia.
 - B) Mechanically, the computation of the 80-20 U.S. business activity test requires the formation of one or two fractions, as the case may be, and the subsequent averaging of those fractions to arrive at an overall U.S. business activity in relation to world-wide business activity. The numerators of the fraction represents U.S. property, U.S. payroll, U.S. revenue miles, insurance premiums on property or risk in the U.S. or financial organization business income from sources within the U.S.; the respective denominators are world-wide figures.
 - C) In the case of a person who would be a member of a unitary business group for only part of a taxable year if less than 80% of its business activities were conducted outside the United States, the 80-20 U.S. business activity test shall be applied only to that part of the person's taxable year for which the prospective member otherwise qualifies for membership in the unitary business group. If that person is a corporation and is a prospective member of a unitary business group required to file combined returns under IITA Section 502(f), the 80-20 U.S. business activity test shall be applied only to that part of the combined group's common taxable year for which that person otherwise qualifies for membership in the combined group.
- d) Entities using different apportionment formulas under IITA Section 304
 - 1) All members of a unitary business group must be eligible under IITA Section 304 to use the same apportionment formula. As a consequence, a corporation required to use the three factor apportionment formula of Section 304(a) cannot be a member of the same unitary group as a corporation required to use the one factor apportionment formula of IITA Section 304(c), nor may a corporation required to use the one factor apportionment formula of IITA Section 304(c) be a member of the same unitary business group as a corporation required to use the one factor apportionment formula of IITA Section 304(b). The proper method for determining unitary business group memberships under IITA Section 1501(a)(27) is first to identify all entities that are related through common ownership and engaged in either horizontally or vertically integrated enterprises with the requisite exercise of strong centralized management and second, to create from the population of entities thus identified one unitary business group composed of entities required to apportion under IITA Section 304(a), one unitary business group composed of entities required to apportion under IITA Section 304(b), one unitary business group composed of entities required to apportion under IITA Section 304(c) and one unitary business group composed of entities required to apportion under IITA Section 304(d).
 - 2) EXAMPLE:

- A) **FACTS:** Corporation A owns all of the outstanding common stock of Corporations B and C. Corporations B and C each own 30% of the outstanding common stock of Corporation D. Corporation D owns 60% of the outstanding common stock of Corporation E. Corporation A is a mining company operating exclusively in Illinois. Corporation D is a manufacturing company with factories in Illinois and Indiana. Corporation C is an insurance company earning premiums for insuring property and risks located in Illinois and Indiana. Corporation B is an air freight company and Corporation E is a trucking company, both operating nationwide. In their relationships to one another, the five companies: are "steps in a vertically structured enterprise or process" and are "functionally integrated through the exercise of strong centralized management."
- B) **ANALYSIS AND CONCLUSION:** As a result of these facts, Corporations A and D, which would ordinarily be required to apportion business income by means of the three factor apportionment formula of IITA Section 304(a), will constitute one unitary business group; Corporations B and E, which would ordinarily be required to apportion business income by means of the one factor transportation formula IITA Section 304(d) will constitute a second unitary business group; and Corporation C will compute its liability on a non-combined apportionment basis under IITA Section 304(b).

e) **Common ownership**

In the case of a corporation, common ownership means direct or indirect control or ownership of more than 50% of outstanding voting stock. In the case of any other entity, common ownership means direct or indirect ownership of an interest sufficient to exercise control over the activities of the entity. For example, ownership of a general partnership interest gives the partner the authority to act on behalf of the partnership and bind the partnership, regardless of actual ownership share. See Section 9 of the Uniform Partnership Act [805 ILCS 205/9]. Accordingly, a general partner in any partnership has an interest in the partnership sufficient to establish common ownership. Insofar as corporations are concerned, one has direct ownership of the outstanding voting stock of another to the extent that it owns such stock and indirect control to the extent that it owns the voting stock of a third corporation that itself owns such stock. Any combination of direct and indirect control or ownership aggregating more than 50% will suffice to qualify the corporation whose stock is owned for membership in the unitary business group if other tests unrelated to ownership are met.

- 1) Corporation A owns 60% of the outstanding voting stock of Corporation B which in turn owns 60% of the outstanding voting stock of Corporation C. There is common ownership of Corporations A, B and C by reason of Corporation A's direct ownership of more than 50% of the outstanding voting stock of Corporation B and indirect control of more than 50% of the outstanding voting stock of Corporation C.
- 2) Corporation A owns 60% of the outstanding voting stock of Corporation B and 60% of the outstanding voting stock of Corporation C. Corporations B and C in turn each own 30% of the outstanding voting stock of Corporation D. Corporations A, B, C and D are all under common ownership by reason of Corporation A's direct ownership of more than 50% of the outstanding voting stock of Corporations B and C and by reason of Corporation A's indirect control

of more than 50% of the outstanding voting stock of Corporation D.

- 3) Corporation A owns 60% of the outstanding voting stock of Corporation B and 40% of the outstanding voting stock of Corporation C. Corporations B and C each in turn own 30% of the outstanding voting stock of Corporation D. Corporations A and B are under common ownership by reason of Corporation A's direct ownership of more than 50% of the outstanding voting stock of Corporation B, but neither Corporations C or D are under common ownership with Corporations A and B because neither Corporation A nor Corporation B has direct or indirect control or ownership of more than 50% of the outstanding voting stock of Corporations C or D.
 - 4) Corporation A owns 60% of the outstanding voting stock of Corporation B and 40% of the outstanding voting stock of Corporation C. Corporation B owns 30% of the outstanding voting stock of Corporation D and Corporation C owns 60% of the outstanding voting stock of Corporation D. Corporations A and B are under common ownership by reason of the fact that Corporation A owns more than 50% of the outstanding voting stock of Corporation B, and Corporations C and D are under separate common ownership by reason of the fact that Corporation C owns more than 50% of the outstanding voting stock of Corporation D.
- f) Attribution of stock ownership among certain persons
For the purpose of IITA Section 1501(a)(27), a person shall be considered to have indirect control over any stock that that person is considered as owning under IRC section 318(a). EXAMPLE: Strictly as an investment, Mr. X and his wife, Mrs. X, each individually own 30% of the outstanding voting stock of Corporation A and 30% of the outstanding voting stock of Corporation B. Corporations A and B are under common ownership within the meaning of Section 1501(a)(27), and assuming that they meet the other requirements of IITA Section 1501(a)(27), they will be members of the same unitary business group. The common ownership stems from the fact that, under IRC section 318(a)(1), the stock holdings of Mr. X are imputed to his wife and vice versa. Note that it is not necessary in order for Corporations A and B to be members of a unitary business group that the "person" in whom the common ownership is embodied also be a member of the unitary business group.
- g) Strong centralized management
Under IITA Section 1501(a)(27), no group of persons can be a unitary business group unless they are functionally integrated through the exercise of strong centralized management. It is this exercise of strong centralized management that is the primary indicator of mutual dependency, mutual contribution and mutual integration between persons that is necessary to constitute them members of the same unitary business group. The exercise of strong centralized management will be deemed to exist where authority over such matters as purchasing, financing, tax compliance, product line, personnel, marketing and capital investment is not left to each member. Thus, some groups of persons may properly be considered as constituting a unitary business group under IITA Section 1501(a)(27) when the executive officers of one of the persons are normally involved in the operations of the other persons in the group and there are centralized units that perform for some or all of the persons functions that truly independent persons would perform for themselves. Note in this connection that neither the existence of central management authority, nor the exercise of that authority over any particular function (through centralized operations), is determinative in itself; the entire operations of the group must be examined in order to determine whether or not

strong centralized management exists. A finding of "strong centralized management" cannot be supported merely by showing that the requisite ownership percentage exists or that there is some incidental economic benefit accruing to a group because such ownership improves its financial position. Both elements of strong centralized management, i.e., strong central management authority and the exercise of that authority through centralized operations, must be present in order for persons to be a unitary business group under IITA Section 1501(a)(27). Finally, a finding of strong centralized management can be supported even though the authority resides in a person that is not a member of the group, provided that the authority is actually exercised by such person.

h) General line of business and vertically structured enterprises

- 1) Section 1501(a)(27) of the Act establishes that persons meeting all of the other tests for inclusion in a unitary business group, including common ownership, strong centralized management and comparability of apportionment method, will ordinarily be in one of the following relationships to one another:
 - A) in the same general line of business, or
 - B) steps in a vertically structured enterprise or process.
- 2) IITA Section 1501(a)(27) recites that two persons will ordinarily be considered to be in the same general line of business if they are both involved in one of the following activities:
 - A) manufacturing
 - B) wholesaling
 - C) retailing
 - D) insurance
 - E) transportation, or
 - F) finance
- 3) IITA Section 1501(a)(27) does not contemplate that the above list be exclusive. For example, two persons that are both involved in rendering services to the public would ordinarily be considered to be in the same general line of business. In this regard, a retailer that renders services that are incidental to its retail business will not be in the same general line of business as a person that is primarily a service dispenser.
- 4) It is not a requirement of IITA Section 1501(a)(27) that the activities of the two persons in whichever category is applicable relate to the same product or product line in order for the two persons to be in the same general line of business.
- 5) Two persons are steps in a vertically structured enterprise or process under IITA Section 1501(a)(27) even though other persons who are also steps in that enterprise or process are not members of the same unitary business group

because of the intervention of: the 80-20 U.S. business activity test or the rules stated in subsection (d) of this Section, relating to the comparability of apportionment formulas of members of a unitary business group.

EXAMPLE 1:

- A) **FACTS:** Corporation A manufactures furniture. Corporation C retails the furniture manufactured by Corporation A. Corporation B is a furniture finisher and wholesaler operating exclusively in Mexico which purchases Corporation A's unfinished furniture, applies the appropriate finishing materials in its Mexican plants, and sells the finished furniture to Corporation C.
 - B) **ANALYSIS AND CONCLUSION:** Corporations A and C are steps in a vertically structured enterprise and as such can be members of the same unitary business group. They do not lose their status as steps in a vertically structured enterprise by reason of the fact that they never directly deal with one another, since they both deal with Corporation B which is also a step in the vertically structured enterprise and which would be a member of the unitary business group were it not for the intervention of the 80/20 U.S. business activity test.
- 6) A person will not be a step in a vertically structured enterprise or process unless it is connected to one or more other persons that are steps in the vertically structured enterprise or process by a flow of goods or services, including management services, to itself or from itself. However, if the flow of goods or service is present with respect to a particular person, that person's status as a step in the vertically structured enterprise or process shall not depend on the relationship between the price at which this flow exists and the fair market price at which this flow would exist in an arm's length transaction.

EXAMPLE 2:

- A) **FACTS:** Same facts as in the previous example, except that Corporation A can establish that it sells its unfinished furniture to Corporation B at a fair market arm's length price and Corporation C can establish that it purchases the finished furniture from Corporation B at a fair market arm's length price.
- B) **ANALYSIS AND CONCLUSION:** Even with their respective showings that the flow of furniture connecting them to Corporation B existed at an arm's length price, Corporations A and C are still steps in a vertically structured enterprise and can still be members of the same unitary business group.

(Source: Amended at 32 Ill. Reg. 10170, effective June 30, 2008)