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Agilent Technologies and the Inclusion of Foreign Holding Companies in Combined Corporate Income Tax Returns

November 28, 2017
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In the famous Seinfeld episode titled "The Lip Reader," George Costanza's girlfriend breaks up with him by telling him "It's not you, it's me." George famously replied, "You're giving me the 'It's not you, it's me' routine? I invented 'It's not you, it's me.'" In the recent case of *Agilent Technologies, Inc. v. Colorado Department of Revenue*, the taxpayer leaned on the ramblings of George Costanza to "break up" with one of its own corporate affiliates to refute a $13 million dollar assessment of corporate income taxes.

The taxpayer was comprised of numerous domestic and foreign corporations doing business all over the world, including Colorado. Colorado requires corporate taxpayers to include certain affiliates for purposes of filing a combined return. The income of the combined group is then apportioned to Colorado based on the presence of certain factors in the state – i.e., payroll, property and sales. The taxpayer attempt to comply with these requirements and filed combined returns in Colorado for all years in dispute.

The crux of the dispute related to a corporate affiliate of the taxpayer – Agilent Technologies World Trade, Inc. (WT). WT was a Delaware corporation formed as a holding company to own foreign entities operating

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solely in Venezuela, Russia, Poland, and Turkey. WT did not own or rent property and had no payroll. The Colorado Department of Revenue sought to include WT in the taxpayer's combined group. By contrast, the taxpayer wanted to exclude WT.

The Department had two theories for including WT in the combined return. First, under Colorado law, a corporate affiliate is generally included in the combined return if 20 percent or more of its property and payroll were assigned to locations inside the United States. Because the taxpayer did not rent or own property or have payroll, the court rejected the Department's argument on this point. The court also rejected the Department's position that the statute should be interpreted to include WT.

The Department's second argument was that it could rely on an "anti-abuse" statute to include WT in the taxpayer's combined return. The relevant statute permits the Department to "allocate income and deductions among corporations that are owned or controlled by the same interests on a fair and impartial basis in order to clearly reflect income and avoid abuse." The court interpreted this statute to only give the Department authority to allocate income within a defined combined corporate group. This provision could not be used by the Department to alter the members of the combined group.

The composition of the combined group – in states that require combined filing – is critical to the resulting corporate tax liability for multistate taxpayers. In some states, inclusion of members reduces tax liability while in others it makes sense to seek to exclude certain affiliates. In Agilent Technologies, the court sustained the exclusion of WT from the combined group to defeat a multi-million dollar assessment. There is no truth to the rumor that George Costanza assisted the taxpayer in successfully arguing the "It's not you, it's me" routine.