

## Income/Franchise:

### South Carolina ALJ Says Combined Reporting Corrects Distortion Resulting from Intercompany Transactions and East-West Structure

*Case No. 21-ALJ-17-0182-CC, S.C. Admin. Law Ct. (7/12/24).* In a case involving a national retailer and its various affiliates (including customer financing, trademark/tradename, back-office management, marketing, and real estate holding affiliates) whose overall organization included an “east-west structure” where the “East” taxpayer in this case challenged a South Carolina Department of Revenue (Department) audit assessment for fiscal years 2016 through 2018, the chief administrative law judge with the South Carolina Administrative Law Court (Court) sided with the Department in concluding that separate reporting, along with South Carolina standard allocation and apportionment, failed to capture or correct resulting distortion from the taxpayer’s use of “intercompany transfer pricing and a partnership with an east-west structure” and that combined unitary reporting (“CUR”) constituted a reasonable and equitable alternative method to correct the distortion and result in a fair representation of the taxpayer’s in-state business activity. In doing so, the judge noted that the taxpayer’s intercompany transfer pricing and partnership with an east-west structure significantly distorted its in-state business activity and artificially lowered its tax burden in South Carolina “without reasonable and reliable justification,” and that, pursuant to state caselaw, CUR was an authorized alternative apportionment method.

**URL:** <https://www.scalc.net/search.aspx>

However, because the Department did not “complete the application of CUR by applying the Finnegan method to divide the taxable income attributable to South Carolina” between the organization’s “East” South Carolina taxpayer versus the “West” South Carolina taxpayer, the judge remanded the matter to the Department to do so and then issue amended assessments, respectively, to each of the two South Carolina taxpayers for the audit period. Responding to one of the arguments made by the taxpayer against mandated combined reporting and requesting intercompany adjustments under “482-principles” be made instead, the judge also noted that “although correcting the intercompany transactions may have allowed separate reporting to remain intact, as this case clearly demonstrates, correcting transfer prices in distortive intercompany transactions is a complicated and fraught venture that takes enormous time and resources to ostensibly arrive at the same result as CUR achieves in this case: a fair representation of the taxable business activity in this state for a single taxpayer.” Please contact us with any questions.

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