CALIFORNIA FRANCHISE TAX BOARD

Legal Ruling No. 321

April 10, 1967

TAXABILITY OF U.S. TREASURY BILLS: GAIN ON SALE

Syllabus:

Treasury bills are United States obligations, issued at a discount and redeemable at maturity value on a specified date within one year of issuance.

On their federal returns for 1962-1964, taxpayers reported as taxable interest income the amount by which the sale price of their Treasury bills exceeded the purchase price. However, on their 1962 and 1963 California returns, the taxpayers reported this amount as capital gain. On the taxpayers' 1964 State return, no income attributable to Treasury bills was reported.

Regulation 17137(b) provides "Interest on bonds and other obligations of the United States . . . is exempt from State taxation under the Constitution and laws of the United States." Since for purposes of taxation a discount is considered to be the equivalent of interest, Rev. Rul. 51, 1953-1 Cum. Bull. 497, it is our opinion that the discount at which a Treasury bill is issued is exempt from California taxation. If the Treasury bill is held for the entire period of maturity, the entire amount of the discount is exempt from California taxation. If the Treasury bill is held for any shorter period, only that part of the total discount which is proportionate to the part of the total maturity period for which the Treasury bill was held is exempt from tax; the remainder is taxable as gain.

Regulation 17137(c) provides that gains and profits from the sale or other disposition of Treasury bills are taxable to the same extent as gains and profits from the disposition of other property. It is our opinion that under Section 18161 Treasury bills are to be considered capital assets for California purposes. Therefore, on any disposition of a Treasury bill which constitutes a "sale or exchange," the amount of any realized gain or profit will be taxed as capital gain. If the bill is held for the entire period of maturity, only the amount by which the sales price exceeds the matured value will be taxable. If the bill is held for a shorter period, that portion of the discount which is not exempt is taxable as capital gain. On a disposition other than a sale or exchange, the gain will be taxable as ordinary income.