# INITIAL STATEMENT OF REASONS FOR THE AMENDMENT OF CALIFORNIA CODE OF REGULATIONS, TITLE 18, SECTION 25106.5-1

## PUBLIC PROBLEM, ADMINISTRATIVE REQUIREMENT, OR OTHER CONDITION OR CIRCUMSTANCE THAT THE REGULATION IS INTENDED TO ADDRESS

During 1999, the Franchise Tax Board promulgated California Code of Regulations, title 18 ("Regulation"), section 25106.5-1, which addresses the treatment of intercompany transactions in a combined report context occurring on or after January 1, 2001. Regulation section 25106.5-1 generally follows the federal consolidated intercompany regulations (Treasury Regulation section 1.1502-13 et seq.) with respect to many of the issues in those regulations, but because income is not apportioned for federal purposes, Regulation section 25106.5-1 also provides applicable apportionment rules.

Regulation Section 25106.5-1(a) – In General.

As stated, Regulation section 25106.5-1 generally follows the federal consolidated intercompany regulations (Treasury Regulation section 1.1502-13 et seq.) Specifically, the current version of Regulation section 25106.5-1, subsection (a)(2), states that it incorporates the version of Treasury Regulation section 1.1502-13 that was in effect as of March 17, 1997. Since that date, Treasury Regulation section 1.1502-13 has had many revisions. Therefore, Regulation section 25106.5-1, subsection (a)(2), is being revised to state that it incorporates the version of Treasury Regulation section 1.1502-13 that was in effect as of April 1, 2012, which is its most current version. Moreover, this section is being revised to state that if a provision of Treasury Regulation section 1.1502-13 which California conforms to requires that the taxpayer not derive any federal tax benefit from its application, then similarly, when that provision of Treasury Regulation section 1.1502-13 is applied for California purposes, then the taxpayer may not derive any California tax benefit from its application.

Regulation Section 25106.5-1(e) -- Simplifying Rules Issue

For income tax purposes, gain or loss from intercompany transactions is ordinarily deferred until there is a triggering event, such as the sale of the deferred item outside the group to a third party. Notwithstanding this general principle, both the California and federal intercompany regulations allow taxpayers in specified circumstances to elect to account for their income or loss from intercompany transactions on a "separate entity" basis. This election allows current recognition of income or loss from intercompany transactions. The election is governed by Regulation section 25106.5-1, subsection (e), for California tax purposes and Treasury Regulation section 1.1501-13, subsection (e)(3), for federal tax purposes.

Both the California and federal regulations include "simplifying rules" provisions. This election is included within those "simplifying rules." Regulation section 25106.5-1, subsection (e), authorizes federal "separate entity" elections to be effective for California tax purposes. Even in situations in which the taxpayer has not made a federal "separate entity" election, taxpayers can elect to recognize intercompany income or loss on a separate entity basis as long as they have "properly reported" the intercompany income or loss on a separate entity basis for federal or foreign national tax purposes.

Questions have arisen regarding the proper sales factor treatment of intercompany transactions that are recognized on a separate entity basis due to the above-described election. Some taxpayers have suggested that because the election results in current income recognition from intercompany transactions, as opposed to the normal scheme of deferral, that the sales factor for the year of election should contain the gross receipts related to the income recognized currently due to the election, which results in a higher sales factor denominator and reduced California apportioned income. Staff believes that it is prudent to clarify that a Regulation section 25106.5-1, subsection (e), election does not allow taxpayers to include intercompany transaction receipts in their sales factor denominator in the year of election. Instead, receipts are only included in the sales factor when the intercompany items are sold to third parties, giving rise to economic gain or loss to the group as a whole. If intercompany receipts were to be recognized currently due to the election, the receipts that arise when the items are eventually sold outside the group would result in a double counting of the actual economic activity in the sales factor. Furthermore, inclusion of these intercompany receipts in the sales factor in the current year due to a subsection (e) election is inconsistent with Regulation section 25106.5(a)(5)(A) and (a)(5)(B).

<u>Regulation Section 25106.5-1(f) – Stock of Members</u>

Regulation section 25106.5-1, subsection (f)(1)(B), addresses the situation where a member of the combined reporting group receives a distribution from another member of the combined reporting group that is in excess of the distributor's earnings and profits and the distributee's basis in the stock of the distributor. Within the context of the federal consolidated return group regulations, which California does not incorporate, this type of excess distribution is treated as creating a negative basis in the distributee's stock in the distributor. On the other hand, pursuant to Internal Revenue Code section 301, subsection (c)(3), which California incorporates pursuant to California Revenue and Taxation Code section 24451, the excess distribution would ordinarily be treated as a taxable gain, irrespective if the distribution is between members of a combined reporting group. Therefore, to allow the gain from the excess distribution to be deferred when the distribution is between members of a combined reporting group, Regulation section 25106.5-1, subsection (f), provides for a Deferred Intercompany Stock Account (DISA). Generally, the DISA is not taken into income until a triggering event occurs, such as when the distributee disposes of the stock in the distributor.

Since the original combined reporting intercompany transaction regulations were initially promulgated, taxpayers and their representatives have encountered situations involving DISAs that were not originally addressed. For instance, when a merger occurs between members of a combined reporting group that are owned by the same members of the combined reporting group, the stock in the non-surviving member is essentially eliminated, although the assets of the non-surviving member continue to be held within the combined reporting group. If the applicable tax laws are strictly followed, any DISA attributable to the non-surviving member's stock must be recognized. Moreover, because the DISA is a deferred income item, according to financial accounting rules, its tax impact must be reflected, thereby reducing financial statement net income. If the DISA could be reduced by means of a subsequent capital contribution, the financial accounting rules would not apply. However, the current DISA rules do not provide for a mechanism that allows subsequent capital contributions to reduce existing DISAs. Additionally, situations have arisen when one member of a combined reporting group transfers stock in another member of the combined reporting group that has no attributable DISA to a third member of the combined reporting group that already possesses stock in the member whose stock was transferred and there is a DISA attributable to that stock. Currently, there is no mechanism to allow the remaining basis in the transferred stock to reduce the DISA in the shares of stock that the transferee already possesses.

Staff has concluded that the current DISA rules included in the combined reporting intercompany transaction regulations should be revised to address these situations encountered by taxpayers and their representatives. To that end, provisions have been added that allow for further deferral of a DISA even if it is attributable to the stock in a non-surviving corporation that was merged and for subsequent capital contributions and the basis in transferred stock to reduce existing DISAs.

Regulation Section 25106.5-1(j) – Miscellaneous Operating Rules

Another situation that has been encountered by taxpayers and their representatives pertaining to DISAs involves the same amount of money or the same property being distributed through various tiers of members of a combined reporting group. It is possible that multiple DISAs result from essentially the same distribution. Currently, the combined reporting intercompany transaction regulations that address earnings and profits, which are contained in subsection (j), do not allow intercompany transactions to create earnings and profits. However, if an excess distribution that would ordinarily result in a DISA was allowed to create earnings and profits, when the distributee distributes the same amount of money or the same property to another member of the combined reporting group, the second distributee would not have a DISA. With this in mind, staff has determined that the combined reporting intercompany transaction regulations pertaining to earnings and profits should be revised to eliminate multiple DISAs from arising in situations involving the same property or the same amount of money being distributed through various tiers of members of a combined reporting group.

As stated previously, the proposed revisions provide for a DISA to be reduced through subsequent capital contributions. The current version of subsection (j)(7) requires taxpayers to report outstanding DISAs on their tax returns. This provision is being revised to state that a corresponding reduction in a DISA from a subsequent capital contribution must also be disclosed on a tax return.

In 2006, California Revenue and Taxation Code section 25110, subdivisions (a)(4) and (6), were renumbered subdivisions (a)(2)(A)(i) and (a)(2)(A)(ii), respectively. These statutory sections are referenced in subsection (j)(3) of the regulation, which is being revised accordingly.

## SPECIFIC PURPOSE OF THE REGULATIONS

The purposes of the proposed revisions to the regulation are to:

1. Indicate the version of Treasury Regulation section 1.1502-13 to which Regulation section 25106.5-1 conforms.

2. Clarify for taxpayers that when an election is made under Regulation section 25106.5-1(e) to currently recognize income from an intercompany transaction, that the receipts from that transaction are not also currently included in the taxpayer's sales factor.

3. Provide rules addressing the treatment of DISAs in the context of certain mergers and tiered distributions and to allow for DISAs to be reduced through subsequent capital contributions and by the basis in transferred stock.

## NECESSITY/PROBLEM THE REGULATION INTENDS TO ADDRESS

<u>Regulation Section 25106.5-1(a)(2) – Conformity to Treasury Regulation Section 1.1502-13.</u>

A revision is necessary to subsection (a)(2) to indicate that the combined report intercompany transaction regulations incorporate the April 1, 2012 version of Treasury Regulation section 1.1502-13, rather than the March 17, 1997 version of Treasury Regulation section 1.1502-13. This will ensure that the combined report intercompany transaction regulations are based on the most current version of the applicable federal rules. Without this proposed revisions, taxpayers would still be required to follow rules that are over fifteen years out of date.

<u>Regulation Section 25106.5-1(e) -- Simplifying Rules Issue.</u>

Amendments are needed to clarify Regulation section 25106.5-1 so that taxpayers understand better that when a subsection (e) election is made to currently recognize intercompany income, the receipts associated with that intercompany transaction are not included in the taxpayer's sales factor in the year of recognition.

Subsection (a)(5) contains the sourcing rules for intercompany transactions. Subsection (a)(5)(A) addresses sourcing of receipts from intercompany transactions for purposes of the California sales factor. The rule is already stated at subsection (a)(5)(A)1., "Sales attributable to intercompany items are not included in S's sales factor either in the year of the transaction or in the years in which such intercompany items are taken into account." While the rule is clearly stated at subsection (a)(5)(A) 1., a second statement of the rule is proposed by adding a new subsection (a)(5)(A) 4., which states: "<u>Subsections (a)(5) 1. through 3. above, shall apply regardless of whether an election is made under subsection (e)(2) of this regulation to recognize income or loss from an intercompany transaction on a</u>

separate entity basis." (Emphasis added.) This second statement makes it clear that subsections (a)(5)(A) 1. through 3 continue to apply when a subsection (e)(2) election is made. That is, making a subsection (e)(2) election does not somehow turn off the application of the sales factor sourcing rules located in subsection (a)(5)(A). This second statement was modeled after the one for the property factor at subsection (A)(5)(B) 5. The regulation drafter included the property factor subsection (A)(5)(B) 5. that restates that the general property factor rules continue to apply even if a subsection (e)(2) election has been made, but the sales factor subsection did not because when Regulation section 25106.5-1 was drafted there was California appellate court case law, *Chase Brass & Copper Company, Inc. v. Franchise Tax Board* (1977) 70 Cal.App.3d 457, that applied to require elimination of intercompany transaction receipts from the sales factor. This case law still applies today.

Subsection (b) contains the definitions of terms used in Regulation section 25106.5-1. Subsection (b)(6) defines "treatment as a separate entity" and states that this phrase means treatment outside of "the rules of this regulation (other than the rules in subsection (a)(4))...." The proposed amendments to subsection (b)(6) would change this to state, "Treatment as a separate entity means treatment without application of the rules of this regulation (other than the rules in subsections (a)(4) and (5)), but with the application of the other combined reporting regulations (as promulgated under the authority of section 25106.5 of the Revenue and Taxation Code)." (Emphasis added.) As currently written, subsection (b)(6) states that "treatment as a separate entity" means that the transaction will be treated in whatever way it would be treated outside of Regulation section 25106.5-1, and then this subsection makes an exception to that general statement. That exception, as currently written, refers to subsection (a)(4) of Regulation section 25106.5-1. Subsection (a)(4) sets forth that "other law" applies in addition to this regulation. In other words, subsection (a)(4) makes it clear that Regulation section 25106.5-1 does not stand alone; rather, all other statutes, regulations, and case law also apply. Therefore, when read together as currently written, subsection (b)(6) explains that the term "treatment as a separate entity" means the transaction would be treated however it would be treated outside of Regulation section 25106.5-1, except, when looking outside of Regulation section 25106.5-1 one has to disregard subsection (a)(4), which states that all other statutes, regulations, and case law or "other law" apply in addition to this regulation. If subsection (b)(6) did not exclude subsection (a)(4), it would not make any sense as they would cancel each other out. The proposed amendments add subsection (a)(5) to the list of subsections excluded from the definition at subsection (b)(6) for "treatment as a separate entity." Subsection (a)(5) contains the assignment rules for the sales factor for intercompany transactions. The effect of excluding subsection (a)(5) sales factor sourcing rules for intercompany transactions from subsection (b)(6)'s definition that states that "treatment as a separate entity" means treatment without application of the rules of Regulation section 25106.5-1, is to make it clear that if a subsection (e) election to currently recognize intercompany income is made (or to treat an intercompany transaction on a separate entity basis), that the sales factor sourcing rules at subsection (a)(5) still apply so that the intercompany receipts are not included in the sales factor.

Subsection (e) contains the simplifying rules that generally follow those at Treasury Regulation section 1.1502-13(e), "unless otherwise provided." Subsection (e)(2) contains the "Election to treat intercompany transactions on a separate entity basis." The proposed amendments make additions to subsections (e)(2)(A), (B), and (C) to include "recognize income or loss from" intercompany transactions. Including this phrase rather than the more generic word "treat" provides more clarity for taxpayers. Subsection (e)(2)(A) as currently written states, in pertinent part, "If members of the combined reporting group make a federal election to treat intercompany transactions on a separate entity basis . . . ." The amendments would alter the first sentence of subsection (e)(2)(A) so that it would state, "If members of the combined reporting group make a federal election to <u>recognize income or loss from</u> intercompany transactions on a separate entity basis...." (Emphasis added.)

In the same subsection (e)(2)(A), another amendment is proposed. As currently written, subsection (e)(2)(A) states, a little later in the paragraph, "A taxpayer which is qualified to request federal consent to treat intercompany transactions on a separate entity basis . . . ." It is proposed to amend that portion of the paragraph so that it states, "A taxpayer which is qualified to request federal consent to <u>recognize income or loss from</u> intercompany transactions on a separate entity basis . . . ." (Emphasis added.) Subsection (e)(2)(B) also has two proposed amendments that would add this same phrase twice. As currently written, subsection (e)(2)(B) states, in pertinent part, "If the members of the combined reporting group properly report transactions on a separate entity basis for federal or foreign national tax purposes and subsection (e)(2)(A) of this regulation does not apply, the taxpayer members may elect to treat those transactions on a separate entity basis for California purposes." After the proposed amendments, this sentence would state, "If the members of the combined reporting group properly report <u>income or loss from intercompany</u> transactions on a separate entity basis for federal or foreign national tax purposes and subsection (e)(2)(A) of this regulation does not apply, the taxpayer members may elect to <u>recognize the income or loss</u> from those i<u>ntercompany</u> transactions on a separate entity basis for California purposes." (Emphasis added.) Then, there is one additional proposed amendment to subsection (e)(2)(C). As written, that subsection states, in pertinent part, "Elections described by subsection (e)(2) of this regulation are made by reporting the intercompany transactions in the manner required by the election on a timely filed original tax return (not an amended return) for the first year to which the election is to apply." After the proposed amendment, the sentence would state, "Elections described by subsection (e)(2) of this regulation are made by reporting <u>income or loss from</u> the intercompany transactions in the manner required by the election on a timely filed original tax return (not an amended return) for the first year to which the election is to apply." (Emphasis added.) The above proposed amendments are needed to clarify that a subsection (e) election to currently recognize income only allows a taxpayer to report the income or loss from an intercompany transaction currently. By adding these phrases it avoids the possibility of misconstruing the subsections to include receipts from intercompany transactions in the sales factor in the year of recognition, which is explicitly forbidden at subsection (a)(5) of this regulation.

<u>Regulation Section 25106.5-1(f)(1)(B) - Deferred Intercompany Stock Accounts.</u>

Existing subsection (f)(1)(B) generally provides that a DISA is taken into income when the stock to which it is attributable is disposed of. A proposed revision, designated subsections (f)(1)(B)2 and (f)(1)(B)4, is necessary to set forth the new proposed rules pertaining to the various issues. The first paragraph of subsection (f)(1)(B)2 contains the rules relating to a merger between combined reporting group members that are owned by other members of the combined reporting group.  This revision specifically states that a merger between combined reporting group members that are owned by other members of the combined reporting group will not result in a disposition requiring a DISA to be taken into income.  It goes on to provide that the DISA attributable to the non-surviving member's stock will be included with any DISA attributable to the surviving members' stock and will be taken into income when the surviving member's stock is disposed of.  Without this proposed revision, even though the assets remain within the combined reporting group, taxpayers would be forced to recognize the DISA when this type of merger occurs, thereby increasing their taxable income.

As stated previously, whenever a DISA arises, for financial statement purposes taxpayers are forced to recognize the tax implications, thereby reducing financial statement net income. Currently there is no mechanism whereby a DISA can be reduced through a subsequent capital contribution, thereby eliminating the need to recognize the financial statement tax implications.  The proposed second paragraph to subsection (f)(1)(B)2 contains the rules pertaining to subsequent capital contributions reducing an existing DISA.  The revision allows P (the putative parent corporation) to make a contribution to S (the putative subsidiary) in order to reduce the DISA attributable to P's stock in S.  Without this proposed revision, taxpayers would always be required to recognize the tax implications for financial statement purposes whenever a DISA arises.

The current version of subsection (f)(1)(B)4 provides that if P (the putative parent corporation) transfers stock in S (the putative subsidiary) to another transferee member of the combined reporting group, any attributable DISA will continue to be deferred.  A second sentence is being proposed to be added to subsection (f)(1)(B)4 to provide that if the transferee already possess shares in S that do not have a DISA attributed to it, the transferee's basis in its existing stock can reduce the DISA attributable to the shares of stock transferred from P.  Without this proposed revision, a transferee would be forced to retain two separate classes of stock in S: one class of stock with a DISA attributable to it and the other class of stock without the DISA attributable to it.

<u>Regulation Section 25106.5-1(f)(2) – Examples.</u>

Example 8 is being added to provide an illustration as to how the merger revisions to the DISA rules should be applied.  Example 9 is being added to provide an illustration as to how the subsequent capital contribution DISA rules should be applied.  Finally, Example 10 is added to provide an illustration of the treatment of transferring stock with a DISA attributable to it.  Each of these proposed examples will assist taxpayers and their representatives in complying with the revisions.

Regulation Section 25106.5(j)(3) – Partially Included Water's Edge Corporations.

The current version of Regulation section 25106.5-1, subsection (j)(3), references portions of the water's edge provisions of the California Revenue and Taxation Code section 25110, as it was numbered in the year the regulation was promulgated, which was 2001.  In 2006, portions of California Revenue and Taxation Code section 25110 was renumbered without substantive effect. California Revenue and Taxation Code section 25110, subdivision (a)(4) and (6), were renumbered section 25110, subdivision (a)(2)(A)(i) and (a)(2)(A)(ii), respectively. Regulation section 25106.5-1, subsection (j)(3), is being revised accordingly.

Regulation Section 25160.5-1(j)(4) – Earnings and Profits.

The current version of Regulation section 25106.5-1, subsection (j)(4), provides that intercompany items are not reflected in earnings and profits until those intercompany items are taken into account under the terms of the combined reporting intercompany transaction regulations. However, as stated previously, a DISA will result if the distribution exceeds the distributor's earnings and profits. As stated previously, if the same property or the same amount of money is distributed through multiple tiers of combined reporting group members, a DISA will result at every ownership level. On the other hand, if a DISA that results at the initial level also creates earnings and profits at that level, an additional DISA will not result when the same property or the same amount of money is distributed to another combined reporting group member. To alleviate this, a sentence is proposed to be added to subsection (j)(4) which will treat the DISA arising from the initial distribution as creating earnings and profits. Without this proposed revision, taxpayers would be subject to multiple DISAs arising from essentially the distribution of the same amount of money or the same property.

Additionally, two examples with different fact patterns are being proposed. These examples will assist taxpayers and their representatives in complying with the revisions.

Regulation Section 25106.5-1(j)(7) – Reporting DISAs.

The proposed revision to subsection (f)(1)(B)2 will allow a DISA to be reduced by a subsequent capital contribution. The current version of subsection (j)(7) requires taxpayers to report DISAs on their annual tax returns. It does not address reductions pertaining to subsequent capital contributions. Therefore, if the proposed revision to subsection (f)(1)(B)2 is adopted, the proposed revision to (j)(7) is necessary to require taxpayers to also annually report reductions to DISAs brought about by subsequent capital contributions.

## BENEFITS OF THE REGULATION

Taxpayers and the Franchise Tax Board will benefit from being able to use the current version of Treasury Regulation section 1.1502-13, to which Regulation section 25106.5-1 conforms. Taxpayers will also benefit from the clarification made in situations where an election is made under Regulation section 25106.5-1, subsection (e), to currently recognize income from an intercompany transaction, will not result in the receipts from that transaction being included in the taxpayer's sales factor, Finally, taxpayers will benefit from the changes to the DISA rules dealing with certain mergers and tiered contributions and the reduction of DISAs through subsequent capital contributions and by the basis in transferred stock. There are no benefits of the regulation to the health and welfare of California residents, worker safety, and the state's environment.

## TECHNICAL, THEORETICAL, AND/OR EMPIRICAL STUDIES, REPORTS, OR DOCUMENTS

In drafting the proposed amendment to subsection (a)(5) to add subsection (a)(5)(A)4., the Franchise Tax Board relied upon this same Regulation at subsection (a)(5)(B)5. In addition, the current version of Treasury Regulation section 1.1502-13 was reviewed. Other than the above items, the Franchise Tax Board did not rely upon any other technical, theoretical, or empirical studies, reports or documents in proposing the adoption of this regulation.

## ALTERNATIVES TO THE PROPOSED REGULATORY ACTION THAT WOULD LESSEN ANY ADVERSE IMPACT ON AFFECTED PRIVATE PERSONS OR SMALL BUSINESS.

In accordance with the requirement of Government Code section 11346.2, subdivision (b)(5), that the Franchise Tax Board consider alternatives to the proposed regulatory action, staff of the Franchise Tax Board conducted three interested parties meetings.

A first interested parties meeting was held on April 22, 2010 to solicit input from the public. Staff did not provide proposed language at that time. The discussion centered on the separate entity treatment and DISA provisions of the existing regulations and how they needed to be clarified to assist the taxpayer and tax practitioner communities. Numerous participants contributed suggestions. Additionally, written comments were received after the April 22, 2010 interested parties meeting.

A second interested parties meeting was held on September 22, 2010. Staff provided proposed language pertaining to the separate entity treatment and DISA provisions. Comments about the separate entity treatment proposed provisions centered on the proposition that current recognition of income compels the use of the factors pertaining to the income, including the receipts factor. However, it was pointed out that allowing the intercompany receipts to be included in the receipts factor will lead to double counting when the subject of the intercompany transaction is sold to an independent party. The comments about the DISA provisions centered on the brother/sister merger issue and the creation of earnings and profits as a result of an excess distribution to eliminate the possibility of multiple DISA resulting for the distribution of the same property or the same amount of money. An item was raised that was not addressed in the proposed DISA provisions regarding whether subsequent capital contributions should be allowed to reduce an existing DISA balance.

As a result of the discussion pertaining to the issue of subsequent capital contributions being allowed to reduce an existing DISA balance, a third interested parties meeting was held on August 16, 2011 to discuss proposed language pertaining to the matter. The comments indicated that the participants were in agreement with the proposed revisions pertaining to the matter.

As a result, the Franchise Tax Board has determined that the proposed regulation pertains only to corporate taxpayers and therefore does not affect private individuals. In addition, it pertains only to multistate and multinational businesses and therefore will have little or no impact on small business.

ECONOMIC IMPACT ANALYSIS

California Revenue and Taxation Code section 25106.5 provides the Franchise Tax Board with the authority to issue regulations pertaining to corporations that are included in a combined report. Intercompany transactions between members of a combined report can create many complicated situations. Regulation section 25106.5-1 was promulgated in 2001 to alleviate many complications. Since its adoption, situations have come to the Franchise Tax Board's attention that indicates revisions are necessary to the combined report intercompany transaction regulations to address the separate entity treatment and DISA provisions. The proposed revisions will provide taxpayers and the tax practitioner communities with the necessary guidance to alleviate complications with respect to separate entity treatment and DISAs. The Franchise Tax Board will save resources by additional taxpayer self compliance.

Creation or Elimination of Jobs Within the State

Since the proposed regulation benefits major corporations that conduct business within and without California by offering more specific guidance as to how to account for certain intercompany transactions, there are no effects on the creation or elimination of jobs within the state

Creation of New or Elimination of Existing Businesses Within the State

Since the proposed regulation benefits major corporations that conduct business within and without California by offering more specific guidance as to how to account for certain intercompany transactions, there will be no effect on the creation of new businesses or elimination of existing businesses within the state.

Expansion of Businesses or Elimination of Existing Businesses Within the State

Since the proposed regulation benefits major corporations that conduct business within and without California by offering more specific guidance as to how to account for certain intercompany transactions, there will be no effect on the expansion of businesses or the elimination of existing business within the state.

ADVERSE ECONOMIC IMPACT ON BUSINESS

The Franchise Tax Board estimates that hundreds of businesses will be impacted by the proposed regulations. All are major corporations that conduct business within and without California. While it is unknown if any small business will be impacted, it is highly unlikely that any will be. The Franchise Tax Board has determined in the economic impact analysis that there are no effects on the creation or elimination of jobs in the state, no effect on the creation of new businesses or elimination or expansion of existing business within the state and that the proposed revisions to Section 25106.5-1 will benefit taxpayers by clarifying the separate entity treatment rules and the DISA rules. In addition, the Franchise Tax Board will save resources by enhanced taxpayer self-compliance. There are no benefits of the regulation to the health and welfare of California residents, worker safety, and the state's environment.