

EXPLANATION OF PROPOSED DRAFT OF REGULATION SECTION 25137-8: MOTION PICTURE AND TELEVISION PRODUCERS, DISTRIBUTORS, AND TELEVISION NETWORKS – APPORTIONMENT OF INCOME

This discussion of the proposed draft of Regulation section 25137-8 attempts to take into account the concerns of the various interested parties. Although we have attempted to note all input, this draft may not include all parties' recommendations. The key points of the discussion draft are set forth with explanations below:

1. *Descriptive title:* While the working title of any regulation is drafted and inserted by the publisher and is not a substantive part of the regulation, we have suggested the title be changed to include the word "Distributors" to make it clear that they are a member of the group covered by this regulation.
2. Proposed Regulation section 25137-8(a)"In General" mirrors MTC Regulation IV.18(h)(1) as amended April 25, 1996. This is not a substantive change. Because this MTC language has been adopted in large part by many other states, it provides a level of uniformity. The application years originally contained in this introductory paragraph have been removed and inserted at the end of the regulation (see Regulation section 25137-8(d)) in order to conform to the format set forth in other special regulations under Revenue and Taxation Code (R&TC) section 25137.
3. *Definitional Sections:* This part of the discussion draft addresses definitions of various terms contained in the rules to follow. This section includes definitions contained in MTC Regulation IV.18(h)(3), existing Regulation Section 25137-12, and those suggested by interested parties.
 - (1) By eliminating the former exclusionary language, proposed Regulation section 25137-8(b)(1) redefines "film" to include news or sports films produced for telecast. This is consistent with the definition of "film" in MTC Regulation IV.18(h)(3)(i). The proposed change recognizes that (1) since the inception of the existing definition of film in the 1970's, news and sports films have become similar to other film types already included in the existing definition, and (2) this inclusion of news and sports film makes the definition of "film" similar to that set forth in MTC Regulation IV.18(h)(3)(i)and thus provides a level of uniformity with other states.

The language, "any other type of format or medium" is taken directly from the definition of "film" in MTC Regulation IV.18(h)(3)(i), thereby updating the existing definition (1) to include new and always changing technology and (2) to provide the definition with a level of uniformity with other states.

Recognizing that a "film" is deemed to be tangible personal property for purposes of this regulation is not new language and is not a substantive change. The existing language of Regulation section 25137-8(b)(4) has been included verbatim in proposed Regulation

section 25137-8(b)(1) so that all definitions of "film" are placed in the same paragraph for easier reference.

Proposed Regulation section 25137-8(b)(1) clarifies that film intended for home viewing is "deemed to be tangible personal property" for sales factor purposes. The term "intended for home viewing" is replaced by "sold for personal use." This is not a substantive change.

- (2) Proposed Regulation sections 25137-8(b)(3) and 25137-8(b)(4) have been expanded to include additional definitions for "producer" and "distributor." The inclusion of these groups and the clarification that "a distributor does not include theaters" were requested by interested parties. The proposed Regulation section 25137-8(b)(4) does not include cable television networks or satellite providers as "distributors."
 - (3) Proposed Regulation section 25137-8(b)(9) defines "telecast" by using language taken directly from MTC Regulation IV.18(h)(3)(vii). This MTC language has been adopted in large part by many other states and therefore provides a level of uniformity. This revision makes no substantive change to the existing regulation.
 - (4) Proposed Regulation section 25137-8(b)(10) has been added to define "advertising revenue" as used in this regulation. This is clarifying language requested by interested parties who must use the term for apportionment purposes. The proposed language makes no substantive change to the existing regulation.
4. Proposed Regulation section 25137-8(c) "Apportionment of Business Income" adds "distributors" to the list of those taxpayers covered by this regulation for purposes of consistency.
 5. Proposed Regulation section 25137-8(c)(3)(A) clarifies that gross receipts include those derived from all sources within this state, including but not limited to those categories specifically identified in the regulation. Gross receipts from advertising revenue is added to make it congruent with both historical practice and the language set forth in MTC Regulation IV.18(h)(4)(iv)(B)(1). This language addresses the concern expressed by some taxpayers over categories not specifically identified. This language makes no substantive change to the regulation.
 6. Proposed Regulation section 25137-8(c)(3)(A) (i), (ii), and (iii) now specifically include advertising revenue in gross receipts. This language is taken from existing Regulation section 25137-12 and MTC Regulation IV.18(h)(4)(iv)(B)(1), thereby making the regulatory language in Regulation section 25137-8 consistent with other special regulations under R&TC section 25137 and providing uniformity with other states. This language makes no substantive change to the regulation.

7. Proposed Regulation section 25137-8(c)(3)(A)(ii) and (iii) add "provided that the source selected is consistently used from year to year for that purpose." This wording clarifies historical administrative practice and provides consistency in reporting of data. This language makes no substantive change to the regulation.
8. Proposed Regulation section 25137-8(3)(A)(iv) clarifies that receipts from sales and rentals also include receipts from "licensing or other disposition" of video cassettes and discs "or any other format or medium intended for personal use," and that these receipts shall be included in the numerator of the sales factor. This language is taken in large part from MTC Regulation IV.18(h)(4)(iv)(B)(4) to provide uniformity with other states. It makes no substantive change to the regulation.
9. Proposed Regulation section 25137-8(d) provides that this regulation will apply to taxable years beginning on and after January 1, 2010 [or January 1 of the tax year of the adoption of the revised regulation] at the request of interested parties. While there are substantive changes from the existing regulation (specifically identifying distributors as a part of the industry covered by this regulation, redefining "film," and identifying new technology used by the industry since the prior regulation was adopted), staff does not believe that the inclusion of advertising revenue as a gross receipt is a substantive change to the existing regulation. This clarification of existing law makes no new demands upon taxpayers.
10. Proposed Note: The authority cited for this regulation is updated from R&TC Section 26422 to R&TC Section 19503, since the prior section is no longer applicable as a result of the passage of SB 3 (Stats. 1993, ch. 31). This makes no substantive change to the regulation. The reference remains Section 25137, Revenue and Taxation Code.