

DISCUSSION TOPICS

Franchise Tax Board Interested Parties Meeting - Intercompany Transactions, Regulation Section 25106.5-1 August 16, 2011

1. Background

The first interested parties meeting for possible amendments to Regulation section 25106.5-1 was held on April 21, 2010. The Discussion Topics from the April 21, 2010 interested parties meeting provided a general background of the problems being addressed and will not be repeated in this Discussion Topics. ([April 21, 2010 IPM Discussion Topics](#)) The second interested parties meeting for possible amendments to Regulation was held on September 22, 2010. The Discussion Topics from the September 22, 2010 interested parties meeting addressed specific issues that will not be repeated in this Discussion Topics. ([September 22, 2010 IPM Discussion Topics](#)) This third interested parties meeting offers an opportunity to discuss additional proposed amendments to Regulation section 25106.5-1 [[PROPOSED AMENDMENTS](#)]

2. The DISA rules of Regulation section 25106.5-1, subsection (f).

At the last interested parties meeting, members of the public commented that while they appreciated the changes to the DISA regime that have been addressed, they believed that the Franchise Tax Board could go further in making the DISA rules match the federal rules relating to Excess Loss Accounts (ELA). Specifically members of the public commented that the regulation should make it possible to “cure” a DISA through a subsequent capital contribution by the stockholder. This would allow for more consistent treatment with the ELA regime and would make the rules easier for taxpayers.

Staff responded at the time that they did not contemplate allowing such a cure but that it would be given further consideration. Staff has since researched the issue and is now prepared to offer language to allow a cure provision to be included in Regulation section 25106.5-1. At the third interested parties meeting, the public will have an opportunity to review and comment upon staff’s approach to creating a cure provision. Specifically staff suggests the following proposed amendments:

- Proposed Amendments

Amend Regulation section 25106.5-1, subsection (f)(1)(B)2, to state that a subsequent capital contribution can reduce an existing DISA, as well as providing a rule that states that any subsequent capital contribution by the stockholder with the DISA to the entity that made the distribution creating the DISA will first be used to offset the DISA and will not be treated as increasing the stockholder's basis in the stock of the entity receiving the distribution until the DISA has been eliminated.

Amend Regulation section 25106.5-1, subsection (f)(1)(B)4, to state that if stock with an existing DISA attributed to it is transferred from a member of the combined

reporting group to another member of the combined reporting group and the transferee member already possesses stock with a positive basis, the DISA attributable to the transferred shares will be reduced by the amount of the positive basis in the existing stock held by the transferee member.

Staff also proposes to add Examples to illustrate the preceding.

Of course, if interested parties wish to suggest other methods and means to achieve this result, this interested parties meeting will be the time to discuss such other proposals.