

# Summary of Interested Parties Meeting

## Revenue and Taxation Code Section 23663 Assignment of Credits Among Combined Report Members

- I. **Administration:** On April 3, 2009, at 1:30 p.m., members of the public attended an interested parties meeting at the Franchise Tax Board office in Sacramento. Parties attended in person and by telephone. Those physically present were asked to register at the entrance and all participants introduced themselves. The session was to be tape recorded, but technical difficulties ensued, and the recording failed.

The IPM panel was comprised of Andrea Chang, an attorney with FTB's Multistate Tax Law Bureau, William Gardner, an attorney with FTB's General Tax Law Bureau, and David Scott, an auditor with FTB's Technical Resources Section.

- II. **Background:** Revenue and Taxation Code section 23663 allows the assignment of credits among members of the same combined report. Section 23663 was added by Section 10 of AB 1452 (Stats. 2008, ch. 763) and is specifically operative for assignments made in taxable years beginning on or after July 1, 2008 and for applications of assigned credits against the “tax” of the assignee in taxable years beginning on or after January 1, 2010.

Section 8(a) of SBX 1 28 (Stats. 2008, 1<sup>st</sup> Ex. Sess. 2008, ch. 1), which is effective December 19, 2008 (91<sup>st</sup> day after adjournment under special session rules in Cal. Const., Art. IV, sec. 9(c)(1)), provides that “[f]or purposes of applying Section 23663 of the Revenue and Taxation Code, as added by Assembly Bill 1452 of the 2007–08 Regular Session, any limitations on allowance of any credit against the “tax” that would apply to the assigning taxpayer in the absence of an assignment shall also apply to the same extent to the allowance of that assigned credit against the “tax” of the eligible assignee.”

- III. **Purpose:** The purpose of this IPM was to discuss the provisions of Revenue and Taxation Code section 23663 and elicit public input. The IPM panel did so through the discussion of a list of frequently asked questions (FAQs), and a discussion of newly issued FTB Form 3544 and its accompanying instructions.
- IV. **Discussion of the FAQs:** The IPM panel acknowledged that the list of FAQs had been issued only a week in advance of the IPM, and assured the interested parties that they would have until April 13 to submit questions or comments regarding those FAQs. Those FAQs that do not receive any questions or comments by that date will become final, but the list of FAQs itself will not be final, so we will continue to add new FAQs to it as we receive them. Questions and/or comments were made at the IPM regarding the following FAQs:

**FAQ #3: Can the assignment be made to a "division" or is that allowed under the current law?**

The question that was raised with respect to FAQ #3 was whether "division" includes a single member LLC. In addition, a participant asked whether this new statute applies to LLCs.

The panel replied that staff is currently looking at this issue and we will post the question and answer as soon as we can.

**FAQ #7: When does the election have to be filed? The election must be filed with the originally filed return for the tax year. This would be the first return filed for a tax year regardless of due date.**

The question that was raised with respect to FAQ #7 was whether a second return filed by the original due date would be considered an "original return" for purposes of making the credit assignment.

The panel replied that staff had looked at this issue, and had determined that for purposes of section 23663, "original return" would mean only the first return filed. Asked why, the panel deferred to a staff member in the audience, who explained that section 23663 provides for an "irrevocable" assignment of the credit, and that was potentially inconsistent with allowing a second return filed by the original filing due date to be considered an "original return" (i.e. using the federal rule regarding "original returns" would allow A to assign a credit to B on A's first return, then change its mind and file an amended return before the original filing due date to reassign the credit to C).

Another party inquired whether the language in section 23663 regarding "irrevocable" assignment was intentionally included to prevent interpretation of "original return" as including a second return filed before the original filing due date. Staff replied that it believed that had been the intent of the legislature, but that it did not know for sure.

Several interested parties requested that FTB staff re-examine this issue because, otherwise, the term "original return" would have a different meaning for section 23663 than it would for other sections of the Revenue and Taxation Code. The panel agreed to re-examine this issue.

**FAQ #9: What if the election form is filed without being signed? The procedures prescribed by the FTB would not have been met, and the assignment would be invalid.**

The question that was raised with respect to FAQ #9 was whether FTB staff could re-examine its position on this issue as well. The panel agreed to do so.

**FAQ #10: Can the election to transfer credits be revoked? No. The election to transfer credits is irrevocable.**

The question that was raised with respect to FAQ #10 was whether the one-time credit assignment under Revenue and Taxation Code section 23663 would prevent transfers of credit under Internal Revenue Code sections 331, 332, 368 or 381. The panel agreed to examine the issue and address it in the FAQs as a new question and answer.

**FAQ #12: If a corporation that has been assigned credits leaves the combined reporting group, can they take those credits with them? Yes. They take the credits and the limitations on the use of those assigned credits with them. They must be able to support the credit assignment should they get audited after leaving the combined report group. They are also potentially liable for any increase in tax liability if all or part of the assigned credit is disallowed on audit of either the assignee or assignor.**

The question that was raised with respect to FAQ #12 was how FTB would disallow the credits. For example, would FTB disallow the credits by order of assignment, or would FTB do a pro-rata disallowance? The panel responded that under the statute, both the assignor and the assignee are jointly and severally liable, so the answer to this question would depend on the facts and circumstances in each case. That is, the FTB would address this issue on a case by case basis.

**FAQ #20: Does the assignee have to make a wage addback when it receives an assigned credit? No, the wage addback should have occurred when the original entity earned the credit.**

The comment relating to FAQ #20 was that staff should clarify what it is talking about (e.g. which credit) when it refers to the "wage addback."

**FAQ #22: Does utilization by the eligible assignee (EA) look at the EA's Enterprise Zone (EZ) factors or the assignor's Enterprise Zone factors? The EA must look to its own Enterprise Zone factors to determine the credit utilization.**

The question that arose relating to FAQ #22 was whether if an assignor generates a LA EZ hiring credit, the assignee must have income from the LA EZ to be able to use that credit. The panel answered, "Yes, those zone restrictions would apply." (This issue is actually already addressed in FAQ #25.)

**FAQ #23: Does the utilization limit look to the factors in the year of transfer or the year the credit will be used? Just like the limitation placed on the assignor using credits, the assignee would look at the factors in the year they are trying to utilize the credits.**

A comment relating to FAQ #23 was that the question should be clarified to specify that the factors in this question are the EZ factors, and not the apportionment factors.

Another comment was that terms such as "utilization limit" should clearly indicate what those terms refer to.

- V. **Additional FAQs:** Additional questions were asked that did not directly pertain to the FAQs already listed. FTB staff will analyze the issues in those questions and add them to the FAQs list as soon as it is feasible.
- a. Can an entity specifically allocate a specific portion of the tax credit that it is assigning? For example, can an entity assign its EZ hiring credit solely related to the TEA employees? Or can an entity assign its manufacturer's investment credit (MIC) solely with respect to one particular asset (e.g. a specific factory)? Or can an entity assign its R&D credit from a specific project? The goal would be to limit the risk to the assignee upon any subsequent audit.
  - b. Would an entity that is assigned an R&D credit have to be engaged in qualified research in order to be able to use the assigned R&D credit?
  - c. If an EZ credit assignee also generates EZ credit on its own, would it have to compute two separate EZ income limitations (i.e. assignee's EZ income limitation applied to credit it generated on its own v. assignor's EZ income limitation applied to credit the assignee received from the assignor)?
  - d. Questions using terms like "wage addback" or "utilization limit" should clearly indicate what those terms refer to.
- VI. **Discussion of Form 3544 and Instructions:** The only comment made was that the Form 3544 Instructions need to make it clear that the AMT credit is not eligible for assignment under Revenue and Taxation Code section 23663. Staff from FTB's Tax Forms Section informed the parties that this issue is already being taken care of, and the next scheduled revision will contain that clarification.
- VII. **Future Action:** The panel asked whether the parties would like to see formal guidance on section 23663, but did not receive any responses. The panel thanked all the parties for their attendance and input, and indicated that it will aim to issue a revised list of FAQs in two or three weeks.