

INITIAL STATEMENT OF REASONS FOR THE  
AMENDMENT OF REGULATION  
SECTIONS 25106.5-0, 25106.5 AND 25106.5-2,  
TITLE 18, CALIFORNIA CODE OF REGULATIONS

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

Section 25106.5 of the Revenue and Taxation Code was enacted in 1987 to provide specific authority to promulgate regulations dealing with combined reporting. Before the enactment of that section, combined reporting procedures were generally reflected in FTB Publication 1061 (Guidelines for Corporations Filing a Combined Report) and case law. Regulations were adopted under Section 25106.5 of the Code on June 13, 1999, but a number of provisions in those regulations were reserved for later amendment.

SPECIFIC PURPOSE OF THE REGULATIONS

The proposed amendments would provide detailed rules relating to the steps of combined reporting. In general, the proposed amendments to Section 25106.5 of the California Code of Regulations provide rules for aggregation of business income of a combined reporting group, collection of apportionment factor data, apportionment of business income to the taxpayer members of the group, and application of the taxpayer member's nonbusiness income and other California source income. The proposed amendment to Regulation Section 25106.5-2 would prescribe rules for the treatment of capital loss carryforwards.

NECESSITY

The rules prescribing the steps of apportionment and allocation for combined reporting groups have been reserved in the existing combined reporting regulations. Accordingly, the Franchise Tax Board does not have a comprehensive set of regulations that deal with those issues, which are currently reflected in Publication 1061, and case law. The Franchise Tax Board has an obligation to regulate when it seeks to prescribe rules of general application.

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

The Franchise Tax Board examined and considered the regulatory history of 18 Cal. Code of Reg. Section 25106.5 and 25106.5-2, including notices, statements of reasons, public hearing documents, written comments and responses thereto, records of the proceedings of the Franchise Tax Board, Publication 1061 (Guidelines for Corporations Filing a Combined Report), and the decision of the Board of Equalization in Appeal of Huffy, Inc., decided April 22, 1999. 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.

The Franchise Tax Board has determined that there were no alternatives considered which would be more effective in carrying out the purpose of the proposed regulation or would be as effective and less burdensome to affected private persons or small businesses than the proposed regulation. In addition, the proposed regulation pertains to corporate taxpayers and therefore does not affect private individuals.

ADVERSE ECONOMIC IMPACT ON BUSINESS

The Franchise Tax Board has determined that proposed amendments to Section 25106.5 of the California Code of Regulations will not have a significant overall economic impact on business. Some taxpayers will be adversely affected by the application of the apportionment rules of the proposed regulations, because they represent a significant departure from existing practices. However, other taxpayers are favorably affected those same rules when compared to existing practices. For the most part, the remainder of the proposed amendments reflect existing practices.

Some taxpayers may be adversely affected by the capital loss carryover rules of proposed Subsection 25106.5-2(g), while others may be benefited by them.