

FINAL STATEMENT OF REASONS
FOR PROPOSED REGULATION SECTION 25106.5-1
INTERCOMPANY TRANSACTIONS

The proposed regulation does not impose any mandate on local agencies or school districts.

Update of Initial Statement of Reasons

The public notice required by section 11346.4 of the Government Code was mailed and published on May 26, 2000. The hearing was held, as scheduled, on July 14, 2000. Oral testimony was offered with respect to the proposed regulation (Transcript of Hearing, Tab 10). Four sets of written comments were received during the comment period related to this proposed regulation. Responses to those comments, both written and oral, are contained in the regulation file.

Minor editing changes were made to the proposed regulation for clarity. With one exception, the proposed modifications constitute nonsubstantial changes (within the meaning of Govt. Code section 11346.8). There is one sufficiently related change (within the meaning of Govt. Code section 11346.8) which is described below:

The department received comments at the public hearing concerning the complexity of the proposed regulation, expressing a desire to defer its implementation until 2001. The department agreed and amended subsection (k) to reflect a January 1, 2001, effective date.

This proposed regulation was presented to the three-member Franchise Tax Board at its September 19, 2000, meeting, with the nonsubstantial and sufficiently related changes. The Board adopted the regulation with these changes and directed the staff to proceed with the necessary steps for adoption. The nonsubstantial and sufficiently related changes were reflected in a 15-day public notice, which was mailed on September 28, 2000. Two sets of written comments were received during the comment period which ended on October 13, 2000. These comments, as well as the department's responses thereto, are part of the regulation file. No changes were necessary as a result of these comments.

Prior to the first hearing, the United States Supreme Court held that section 24344(b) of the California Revenue and Taxation Code (also known as the "interest offset") was unconstitutional (*Hunt-Wesson, Inc. v. Franchise Tax Board*, ___ U.S. ___, 120 S. Ct. 1022 [145 L.Ed. 2d 974] (2000)). The Supreme Court accepted the taxpayer's petition for certiorari in that case during the period when the department was considering this proposed regulation; at this time, the Franchise Tax Board is trying to determine what part, if any, of section 24344(b) can be saved. The proposed regulation makes reference to and may affect computations made under section 24344(b) and/or interest offset; however, regardless of whether any part of Section 24344(b) can be saved, the

application of the proposed regulation will not be impacted. In other words, if section 24344(b) is completely invalidated and or repealed, then the department would only need to make a Form 100 change deleting all references to section 24344(b) and/or the interest offset.

Alternatives Determined

The Franchise Tax Board has determined that no alternative would be more effective in carrying out the purpose for which the regulation is proposed or would be as effective and less burdensome to affected private persons than the proposed regulation.