

FINAL STATEMENT OF REASONS
FOR PROPOSED AMENDMENTS TO CALIFORNIA CODE OF REGULATIONS,
TITLE 18, SECTION 25136

The proposed regulations do 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 in the California Notice Register on October 23, 2009. The hearing was held, as noticed, on January 13, 2010, to consider the adoption of proposed amendments to Regulation section 25136, which addresses the sales factor for sales of other than tangible personal property. There were sixteen attendees at the hearing and oral testimony was received from seven individuals representing various interests. Four written comments were received during the comment period, which ended at 5:00 p.m. on January 13, 2010.

As a result of comments received, changes were made to the initial proposed regulation. The changes were noticed in a 15-day change notice, mailed on February 23, 2010. No comments were received regarding the 15-day changes.

Minor editing changes were made to the proposed regulation for clarity as part of the 15-day changes. The proposed modifications constitute nonsubstantial changes (within the meaning of Govt. Code section 11346.8). These modifications are described below:

1. The first sentence in the examples under Regulation sections 25136(d)(3)(A), (B), (C), (D) and (E) is amended so that it is clear that the taxpayer in the example is not a provider of personal services which would instead be governed by the provisions of Regulation 25136(d)(2)(C). The examples in each subsection referred to above are amended to read:

The taxpayer, a satellite TV provider, contracts with its customer, an owner of apartment buildings, to provide and install satellite dishes for \$1,000,000 in this state.

2. The last sentence in the examples under Regulation sections 25136(d)(3)(B), (C), (D), and (E) was determined to be unnecessary and as a result caused confusion. It is deleted in order to simplify the examples:

~~(See subsection (d)(2), Special Rules, for examples of exceptions to this method of assignment of a receipt to the sales factor numerator.)~~

3. The entire example in Regulation section 25136(d)(3)(C) is amended because several commentators felt it was disjointed and confusing. In addition some facts were unnecessarily repeated. The example is amended to read:

The taxpayer, a satellite TV provider, contracts with its customer, an owner of apartment buildings, to provide and install satellite dishes for \$1,000,000 in this state and States A and B on an as needed basis. The taxpayer then subcontracts with and pays agent or independent contractor X to install the satellite dishes in

this state and States A and B for \$200 per installation. The taxpayer's records show that X installed 1,000 satellite dishes each in this state and State A and 1,750 satellite dishes in State B. The contract between the taxpayer and X does not indicate the taxpayer's costs associated with X's installation of the satellite dishes in each state. However, the taxpayer's contract with its customer indicates that the activity will take place in this state and States A and B, and the taxpayer's records indicate the number of installations in each state. the taxpayer's contract with its customer indicates that the cost of X's performance is \$200 per installation. Accordingly, the taxpayer can reasonably determine at the time of filing its return the costs of performing installation services in each state because the taxpayer's records the number of installations in each state and the contract between the taxpayer and its customers indicate the costs of each installation. The taxpayer's cost of performance is \$200,000 in both this State and State A and is \$350,000 in State B. The taxpayer's greater cost of performance of \$350,000 will be assigned to State B pursuant to subsection (d)(3)(C) for purposes of assigning the \$1,000,000 receipt to the numerator of the sales factor. (See subsection (d)(2), Special Rules, for examples of exceptions to this method of assignment of a receipt to the sales factor numerator.)

4. Subsection (e) is added to set forth that the amendments to the regulation are applicable to taxable years beginning on or after January 1, 2008. Interested parties requested that the proposed regulation include an effective date within the regulation and the January 1, 2008 date is reasonable as the date had been publicly disclosed and discussed in two Franchise Tax Board public meetings: the first in September, 2007 and the second in June 2008. In the June 2008 Franchise Tax Board public meeting, staff requested and the Board approved that the applicable date for the amendments to the regulation would be for taxable years beginning on or after January 1, 2008. The new language reads:

(e) The amendments to this regulation are applicable to taxable years beginning on or after January 1, 2008.

The final version of the regulation was presented to the Franchise Tax Board for its approval at its April 6, 2010 public meeting. The Board was provided with all of the comments received during the regulatory process as well as responses to the comments. The Board approved the regulation by a vote of 3-0.

Alternatives Determined

The Franchise Tax Board has not received any proposed alternatives that would lessen the adverse economic impact that the proposed regulations would have on small businesses. The Franchise Tax Board has determined that no alternative would be more effective in carrying out the purpose of the proposed regulations or would be as effective and less burdensome to affected private persons than the proposed amendments to the existing regulation.