

Summary of December 2014 Interested Parties Meeting  
Apportionment of Income for Combined Reporting Groups with Financial and Non-Financial  
Members

I. Administration.

An interested parties meeting ("IPM") was held on December 4, 2014 to discuss possible revisions of Regulation 25137-10.<sup>1</sup> Parties attended in person and by telephone. Those physically present were asked to register at the entrance. Phone participants introduced themselves. The session was tape-recorded for reference but participants were advised there would be no attribution of comments and no transcript. Carl Joseph, as Assigned Staff, facilitated the meeting. Available handouts were: (1) notice of the meeting; and (2) Discussion Topic setting forth the background of the problem and specific issues to be discussed.

II. Discussion.

The discussion during the IPM revolved around the following topics:

1. Should the Franchise Tax Board ("FTB") begin a regulatory effort to address the fact pattern described in the [Discussion Topic document](#), or is this issue simply one that is more appropriately addressed on an individual taxpayer by taxpayer basis such that a regulation is not feasible?

Several participants questioned whether the number of taxpayers with this issue is large enough to warrant a regulatory effort. Assigned Staff responded that he had seen at least 7 to 8 cases with this issue involving gigantic as well as regional players and that even with a small number of taxpayers, due to the consolidation between banks and securities firms, the size of the industry they represent is large. Assigned Staff stated that several taxpayers have approached the FTB and indicated their interest in a regulatory solution.

2. If the FTB were to regulate in this area, what should be the proper scope of the effort?

Assigned Staff indicated that the industry in question is a complex one and that there are 3 different tests under the California tax scheme which impact a taxpayer's return. First, a gross business receipts test under section 25128 determines whether an apportioning trade or business should apportion its income to California using an evenly-weighted 3-factor formula or a single sales factor formula. Second, a gross income test under Regulation 23183 at the entity level determines if a corporation is a financial corporation subject to special apportionment factor rules under Regulation 25137-4.2. Finally, a gross income test under Regulation 25137-10 determines how a combined reporting group with both general and financial corporation members, the general corporation activity being predominant, computes its factors.

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<sup>1</sup> All section references are to the California Revenue and Taxation Code, and all references to regulations are to the California Code of Regulations, title 18, unless otherwise specifically noted.

Assigned Staff asked if the industry would like to tackle all 3 issues set forth above in a regulation but pointed out that the section 25128 apportionment formula is a statutory issue that is more appropriate for the Legislature to address. The participants made no specific comment about this question but seemed to agree that the section 25128 issues should not be part of the regulation effort.

### 3. Market sourcing rules

One participant inquired about whether the new market sourcing rules may mitigate the distortive effect the FTB perceives and is evaluating how to address. Assigned Staff responded that FTB had not started the examination of 2011 and 2012 returns and thus did not have a clear understanding of the impact of the market sourcing rules on this issue. Assigned Staff indicated FTB will look into the actual returns and gather more information.