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September 20, 2005
Chief Counsel Ruling 2005-0008

Dear ************:

This Chief Counsel Ruling is issued in response to your request for advice dated **************, concerning the application of Revenue and Taxation Code 17041(i)(3) with respect to ************** capital loss carryforwards from the sale of stock and her gain on the sale of her California residence upon her establishing residency in a state other than California. You requested written confirmation of oral advice previously provided by Franchise Tax Board staff.

FACTS

Taxpayer, ****************, is a long-time resident and domiciliary of California. Within the estate inherited by Taxpayer from her husband in **** were a substantial number of security positions, as well as her principal residence.[1] In accordance with California law, Taxpayer took each item of inherited property with a tax basis equal to the fair market value of that item on the date of death of her late husband. A portion of the security positions lost substantial value over the succeeding years and in ******************, Taxpayer disposed of such security positions, realizing substantial capital losses that resulted in a substantial capital loss carryover that remains to this date. In contrast, over the period since the death of her husband, the value of Taxpayer's California residence has appreciated substantially. As a result, were Taxpayer to sell the California residence, she would realize a substantial capital gain on the sale.

Taxpayer is currently considering selling her California residence and establishing residence in a state other than California. It is uncertain at this time whether the sale of

[1] It is noted that Taxpayer is not the direct owner of some of the security positions and is not the titleholder of the California residence. These properties are held in the *** (the "Trust"). The Trust is treated as a grantor trust for tax purposes because the Taxpayer has power of appointment over the assets of the Trust. Taxpayer is the sole beneficiary of the Trust. As a result, the income and expenses incurred by the Trust flow directly to Taxpayer's individual income tax returns. This advice is given with respect to Taxpayer as an individual.

her California residence will occur in the same tax year as the change of residency or in the year immediately subsequent to the change of residency. Taxpayer seeks guidance on whether her anticipated change of residency would limit her ability to apply her capital loss carryover against the substantial capital gain she expects to realize on the sale of her California residence.

ISSUE

Whether Taxpayer, upon selling her California residence and establishing residence in a state other than California, may apply her capital loss carryforward against the gain realized upon the sale of her California residence.

HOLDING

Yes. Taxpayer may apply her capital loss carryforward against the gain realized upon the sale of her residence because both items would be sourced to California.

DISCUSSION

Revenue and Taxation Code section 17041 subsection (i) paragraph (3) provides as follows:

For purposes of computing "taxable income of a nonresident or part-year resident" under paragraph (1), any carryover items, deferred income, suspended losses, or suspended deductions shall only be includable or allowable to the extent that the carryover item, deferred income, suspended loss, or suspended deduction was derived from sources within this state, calculated as if the nonresident or part-year resident, for the portion of the year he or she was a nonresident, had been a nonresident for all prior years.

The amendments to section 17041 in 2002, and subsequently, did not alter California's sourcing rules. Instead, they were meant to clarify how carryover items should be applied when a taxpayer changes her residency. Because residents are taxed on all income regardless of source, source is not considered when carryover and other deferred items are being applied. Nonresidents, on the other hand, are taxed only on sourced income so the source of each carryover and other deferred item becomes important. Upon changes in residency, carryover and other deferred items must be restated to reflect the taxpayer's current residency status.

The gain on the sale of Taxpayer's residence in California is clearly sourced to California. The source of that income is the location of the property sold. Since it is real property it is simple to ascertain the location of the property. To offset her capital gain, Taxpayer would like to be able to use any applicable capital losses that she has carried forward.

As a nonresident, Taxpayer may only apply loss carryovers to offset the gain from California sources if such loss carryovers are sourced to California. Were the losses from the sale of securities sourced to California? Under the doctrine of *mobilia sequuntur personam*, intangible property has a taxable situs at the domicile of the owner. On the dates of the sales of the securities, California was the domicile of the owner (Taxpayer). The fact that she subsequently moved from California does not alter that fact. Furthermore, after the sale, Taxpayer was no longer the "owner" of the securities so her domicile would no longer be relevant.

Please be advised that the tax consequences expressed in this Chief Counsel Ruling are applicable only to the named taxpayer and are based upon and limited to the facts you have submitted. In the event of a change in relevant legislation, or judicial or administrative case law, a change in federal interpretation of federal law in cases where our opinion is based upon such an interpretation, or a change in the material facts or circumstances relating to your request upon which this opinion is based, this opinion may no longer be applicable. It is your responsibility to be aware of these changes, should they occur.

This letter is a legal ruling by the Franchise Tax Board's Chief Counsel within the meaning of paragraph (1) of subdivision (a) of section 21012 of the Revenue and Taxation Code. Please attach a copy of this letter and your request to the appropriate return(s) (if any) when filed or in response to any notices or inquiries which might be issued.

Very truly yours,

Natasha Sherwood Page
Tax Counsel III