

STATE OF CALIFORNIA
LEGAL DIVISION MS A260
FRANCHISE TAX BOARD
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NOTICE OF AMENDMENTS TO TEXT OF PROPOSED REGULATION SECTIONS 25137-1 AND 17951-4 IN TITLE 18 OF THE CALIFORNIA CODE OF REGULATIONS RELATING TO APPORTIONMENT AND ALLOCATION OF PARTNERSHIP INCOME

On November 3, 2017, the Franchise Tax Board (FTB) published a Notice of Proposed Rulemaking in the California Regulatory Notice Register in accordance with section 11346.4 of the Government Code, providing notice to the public of the FTB's intention to amend portions of Title 18 of the California Code of Regulations (CCR), sections 25137-1 and 17951-4. On December 18th, 2017, the FTB held a hearing on the proposed amendments to CCR sections 25137-1 and 17951-4, with department staff serving as the "hearing officer." The proposed amendments to CCR Section 25137-1 and 17951-4 for which the hearing was held are summarized here as follows:

1. To provide that the rules for partnerships in which an interest is held by an apportioning corporation also pertain to tiered partnerships.
2. To provide that the rules for the determination of whether the distributive share of income from a non-unitary partnership is treated as apportionable business income or allocable nonbusiness income are based on the activities of the non-unitary partnership.
3. To provide the rules for eliminating sales between a unitary partnership and any member of the partner's combined reporting group.
4. To provide the rules for treating unitary partnerships that engage in long-term construction contracts.
5. To provide the rules for determining the income sourced to California when a partnership and a nonresident partner are unitary with one another.

Department staff reviewed the proposed regulation language and considered the comments submitted during the comment period and at the hearing. The hearing officer now recommends a substantive change to the proposed amended regulation at subsection (d)(1) of CCR section 17951-4. Pursuant to the requirements of Government Code section 11346.8 (c), and section 44 of Title 1 of the California Code of Regulations, the FTB is hereby providing notice of the changes made to the proposed regulation at CCR section 17951-4, which was the subject of the regulatory hearing held on December 18th, 2017.

The proposed sufficiently related and substantive change is summarized and explained below, and appears in underline and double strikeout as follows:

(1) Except as provided, the total business income of the partnership shall be apportioned at the partnership level in accordance with the apportionment rules of the Uniform Division of Income for Tax Purposes Act, Sections 25120 to 25139, Revenue and Taxation Code, and the regulations thereunder.
~~Revenue and Taxation Code section 17952 is not applicable in determining the source of income allocated to the nonresident taxpayer by the partnership.~~

Current subsection (d)(1) of CCR section 17951-4 provides that California's version of the Uniform Division of Income for Tax Purposes Act (UDITPA) is applicable for determining a nonresident partner's California-sourced income from a partnership that conducts business within and without California. The proposed addition to CCR section 17951-4 (d)(1), which was originally noticed on November 3, 2017, would have added a provision intended to make Revenue and Taxation Code (RTC) section 17952 inapplicable in situations where a nonresident owns an interest in a partnership that conducts business within and without California. However, commentators at the hearing objected to this language because it was perceived as a regulation narrowing the application of a statute. Moreover, the hearing officer has come to the conclusion that the language that is proposed to be stricken is repetitive in that only non-business income from a partnership will be subject to the purview of RTC section 17952. This is because business income from a partnership that conducts business within and without California is apportioned in all situations. As a result, the hearing officer now recommends a change to remove the originally proposed addition to the text at CCR section 17951-4(d)(1). This removal will serve two purposes: (1) It will eliminate a possible regulatory authority issue the hearing officer thought might be caused by the language because of a regulation potentially narrowing the application of a statute; and (2) It will make it clear that California's version of UDITPA is still applicable for determining a nonresident partner's California-sourced income from a partnership that conducts business within and without California.

This substantive and sufficiently related change is being made available to the public for the 15-day period required by Government Code section 11346.8(c) and section 44 of Title 1 of the California Code of Regulations.

In addition, the hearing officer is also making a nonsubstantive change to the text of the originally noticed regulation at CCR section 17951-4 to add the punctuation mark of a period and a carriage return after the title of the section and before the beginning of subsection (a) of the section. This nonsubstantive change will make the regulation language at CCR section 17951-4 consistent with the formatting in the existing California Code of Regulations.

A copy of these proposed amendments is being sent to all individuals who requested notification of such changes, as well as those who attended the hearing and those who commented orally or in writing, and will be available to other persons upon request.

All written comments concerning this notice must be submitted to FTB no later than 5:00 p.m. on March 5, 2018, and should be directed to:

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All written comments received by March 5, 2018, which pertain to the indicated changes will be reviewed and responded to by FTB's staff as part of the compilation of the rulemaking file. Please limit your comments to the proposed substantive modifications to the text.