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california legislature—2009–10 regular session

ASSEMBLY BILL No. 1178

Introduced by Assembly Member Block
(Coauthors: Assembly Members Blumenfield*, Brownley*, Nava*,* ~~and~~ Ruskin*, and Salas*)

February 27, 2009

An act to amend, repeal, and add Section 25110 of, and to add ~~Section 6361.7 to~~ *and repeal Section 17052.1 of,* the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.

legislative counsel's digest

AB 1178, as amended, Block. ~~Sales, use, and corporation taxes.~~ *Taxation: personal income tax credit: corporation taxes: tax havens.*

~~The Sales and Use Tax Law imposes a tax on retailers measured by the gross receipts from the sale of tangible personal property sold at retail in this state, or on the storage, use, or other consumption in this state of tangible personal property purchased from a retailer for storage, use, or other consumption in this state. That law provides various exemptions from those taxes.~~

~~This bill would provide a partial exemption from those taxes, on and after July 1, 2011, and before January 1, 2015, for the sale of, and the~~

~~storage, use, or other consumption of, textbooks and supplies, as defined, purchased by a student enrolled in an institution of higher education, as defined to mean the University of California, the California State University, or a California community college.~~

~~The Bradley-Burns Uniform Local Sales and Use Tax Law authorizes counties and cities to impose local sales and use taxes in conformity with the Sales and Use Tax Law, and existing law further authorizes various local governmental entities to levy transactions and use taxes in accordance with the procedures and requirements of the Transactions and Use Tax Law.~~

~~Exemptions from state sales and use taxes are incorporated in these laws. Section 2230 of the Revenue and Taxation Code provides that the state will reimburse counties and cities for revenue losses caused by the enactment of sales and use tax exemptions.~~

~~This bill would specify that this exemption does not apply to local sales and use taxes, transactions and use taxes, and specified state sales and use taxes.~~

The Personal Income Tax Law authorizes various credits against the taxes imposed by that law.

This bill would authorize a credit against those taxes for certain qualified teachers in an amount equal to $500 for each taxable year beginning on or after January 1, 2011, and before January 1, 2012, and in an amount equal to $850 for each taxable year beginning on and after January 1, 2012, and before January 1, 2014, as specified.

The Corporation Tax Law imposes taxes measured by income and, in the case of a business with income derived from or attributable to sources both within and without this state, apportions the income between this state and other states and foreign countries in accordance with a specified apportionment formula based on the property, payroll, and sales within and without this state, except as otherwise provided. That law allows corporations to elect whether their income is determined on a water's-edge basis or on a worldwide unitary basis. In general, a corporation that makes a water's-edge election is subject to tax on income only from sources within the United States but is required to take into account the income and apportionment factors of certain specified affiliated entities.

This bill would expand the list of specified affiliated entities for taxable years beginning on or after July 1, 2011, and before July 1, 2014, to include a corporation that is incorporated, headquartered, or located in a country that is a tax haven, as defined, and would make related legislative findings and declarations.

This bill would take effect immediately as a tax levy.

Vote: majority. Appropriation: no. Fiscal committee: yes. State-mandated local program: no.

The people of the State of California do enact as follows:

SECTION 1. (a) The Legislature finds and declares all of the following:

(1) Offshore tax haven jurisdictions impose zero or nominal corporate tax rates and exhibit at least one of the following characteristics: lack of effective exchange of tax information with foreign tax authorities; lack of transparency in the operation of legislative, legal, or administrative provisions; no requirement for a substantive local presence; or self-promotion as an offshore financial center.

~~(1)~~

(2) The sheltering of income in offshore tax haven countries has been a major means of tax avoidance for multinational corporations.

~~(2)~~

(3) In many cases the sheltering occurs because income that should be properly attributed to activities in the United States is being attributed to those tax haven countries.

~~(3)~~

(4) The water's-edge election provisions enacted by California addressed these concerns by requiring that some foreign incorporated entities be included within a corporate taxpayer's water's-edge combined report. However, additional strategies have been developed by multinational corporations to assign income to foreign incorporated entities that perform limited economic activity in those countries and are not included within the water's-edge combined report.

(b) It is the intent of the Legislature, therefore, in amending Section 25110 of the Revenue and Taxation Code by this act, to further limit the ability of multinational corporations to use tax haven countries to exclude income from the water's-edge combined report as a means of domestic tax avoidance, to the extent that such income is not derived from, or attributable to, the active conduct of a trade or business in the tax haven country.

(c) In granting regulatory authority to the Franchise Tax Board with regard to a determination of whether a corporation has established the active conduct of a trade or business in a tax haven country, the Legislature intends that the Franchise Tax Board examine whether economic factors, including payroll and property, are located in the tax haven in a manner proportionate to the income attributable to the tax haven.

~~SEC. 2. Section 6361.7 is added to the Revenue and Taxation Code, to read:~~

~~6361.7. (a) On and after July 1, 2011, and before January 1, 2015, there are exempted from the taxes imposed by this part, the gross receipts from the sale in this state of, and the storage, use, or other consumption in this state of, textbooks or supplies that are purchased by a student enrolled in an institution of higher education, and the textbooks or supplies are recommended or required for a course in which the student is enrolled.~~

~~(b) For purposes of this section, the following definitions apply:~~

~~(1) "Institution of higher education" means the University of California, the California State University, or a California community college.~~

~~(2) "Supplies" means pens, paper, blue books, notebooks, art supplies, uniforms, safety equipment, tools, computer paper, and flashdrives necessary for the course of study in which a student is enrolled at the institution of higher education. Supplies shall not include computers, printers, or related hardware and software.~~

~~(3) "Textbooks" means any published material that is principally designed for use by a student at an institution of higher education as a source of instructional material and includes, but is not limited to, any book or edition of a book that is directed or recommended by an instructor at an institution of higher education to a student to purchase for use as a basis for a course of study in which that student is enrolled at that institution.~~

~~(c) (1) (A) Notwithstanding subdivision (a), on and after July 1, 2011, and before July 1, 2012, the exemption provided by this section shall not apply with respect to any tax levied pursuant to Section 6051.2, 6051.5, 6201.2, or 6201.5, pursuant to Section 35 of Article XIII of the California Constitution, or with respect to~~

~~that portion of the tax levied at a rate of 2 percent pursuant to Section 6051 or 6201.~~

~~(B) Notwithstanding subdivision (a), on and after July 1, 2012, the exemption provided by this section shall not apply with respect to any tax levied pursuant to Section 6051.2, 6051.5, 6201.2, or 6201.5, or pursuant to Section 35 of Article XIII of the California Constitution.~~

~~(2) Notwithstanding any provision of the Bradley-Burns Uniform Local Sales and Use Tax Law (Part 1.5 (commencing with Section 7200)) or the Transactions and Use Tax Law (Part 1.6 (commencing with Section 7251)), the exemption established by this section shall not apply with respect to any tax levied by a county, city, or district pursuant to, or in accordance with, either of those laws.~~

SEC. 2. Section 17052.1 is added to the Revenue and Taxation Code, to read:

17052.1. (a) For each taxable year beginning on or after January 1, 2011, and before January 1, 2014, a qualified taxpayer shall be allowed a credit against the "net tax," as defined in Section 17039, an amount equal to five hundred dollars ($500) for each taxable year beginning on and after January 1, 2011, and before January 1, 2012, and an amount equal to eight hundred fifty dollars ($850) for each taxable year beginning on and after January 1, 2012, and before January 1, 2014.

(b) For purposes of this section, "qualified taxpayer" means a taxpayer who is a teacher holding a valid teaching credential, certificate, authorization, or permit issued by the Commission on Teacher Credentialing and either is employed, or was employed on or after January 1, 2010, and before January 1, 2014, but was subject to lay off, on either a full-time or a part-time basis in a California public school in which kindergarten or any of grades 1 to 12, inclusive, are taught.

(c) In the case where the credit allowed by this section exceeds the "net tax," the excess may be carried over to reduce the "net tax" in the following year, and succeeding years if necessary, until the credit is exhausted.

(d) This section shall remain in effect only until December 1, 2015, and as of that date is repealed. However, any unused credit may continue to be carried forward, as provided in subdivision (c), until the credit is exhausted.

SEC. 3. Section 25110 of the Revenue and Taxation Code, as added by Section 2 of Chapter 22 of the Statutes of 2006, is amended to read:

25110. (a) Notwithstanding Section 25101, a qualified taxpayer, as defined in paragraph (2) of subdivision (b), that is subject to the tax imposed under this part, may elect to determine its income derived from or attributable to sources within this state pursuant to a water's-edge election in accordance with the provisions of this part, as modified by this article. A taxpayer, that makes a water's-edge election on or after January 1, 2006, shall take into account that portion of its own income and apportionment factors and the income and apportionment factors of its affiliated entities to the extent provided below:

(1) The entire income and apportionment factors of any of the following corporations:

(A) Domestic international sales corporations, as described in Sections 991 to 994, inclusive, of the Internal Revenue Code and foreign sales corporations as described in Sections 921 to 927, inclusive, of the Internal Revenue Code.

(B) Any corporation (other than a bank), regardless of the place where it is incorporated if the average of its property, payroll, and sales factors within the United States is 20 percent or more.

(C) Corporations that are incorporated in the United States, excluding corporations making an election pursuant to Sections 931 to 936, inclusive, of the Internal Revenue Code.

(D) Export trade corporations, as described in Sections 970 to 972, inclusive, of the Internal Revenue Code.

(E) (i) Subject to clause (ii), for taxable years beginning on or after July 1, 2011, and before July 1, 2014, any corporation that, for any portion of the taxable year, was doing business in, or had income derived from or attributable to, a tax haven. For purposes of this subparagraph, "doing business in" or "doing business within" means being engaged in activity that is sufficient to impose a tax under United States constitutional standards.

(ii) If the application of clause (i) would result in the inclusion of the income and apportionment factors of a corporation engaged in the active conduct of trade or business, within the meaning of Section 367(a)(3)(A) of the Internal Revenue Code and the regulations thereunder, in a tax haven, the taxpayer may petition the Franchise Tax Board to treat the corporation as not doing business within, or having income derived from or attributable to, the tax haven. The procedure to petition as described in this clause shall be developed in a form and manner determined by the Franchise Tax ~~Broad~~ *Board* and in accordance with Section 25137. The ~~determination~~ *decision* of the Franchise Tax Board may be appealed to the State Board of Equalization in the form and manner described in Article 3 (commencing with Section 19031) of Chapter 4 of Part 10.2.

(iii) Any decision by the Franchise Tax Board or the Board of Equalization described in clause (ii) that would grant an exclusion of income and apportionment factors of a corporation engaged in the active conduct of trade or business in a tax haven may remain in effect for a period of three years after the date of decision for purposes of subsequent years' filings by that corporation, provided that no additional activity that is sufficient to impose a tax under United States constitutional standards is engaged in by the corporation beyond the circumstances under consideration by the Franchise Tax Board at the time of the appeal.

~~(iii)~~

(iv) The Franchise Tax Board shall prescribe any regulations that may be necessary or appropriate to carry out the purposes of the amendments made to this section by the act adding this clause, including regulations prescribing the extent to which an activity in, or income derived from or attributable to, a tax haven will be presumed to be from the active conduct of a trade or business in the tax haven, and the extent to which income will be presumed to be not derived from or attributable to a tax haven.

(2) (A) With respect to a corporation that is not described in subparagraphs (A), (B), (C), (D), and (E) of paragraph (1), as provided in either one or both of the following clauses:

(i) The income and apportionment factors of that corporation to the extent of its income derived from or attributable to sources within the United States and its factors assignable to a location within the United States in accordance with paragraph (3) of subdivision (b). Income of that corporation derived from or attributable to sources within the United States as determined by federal income tax laws shall be limited to, and determined from, the books of account maintained by the corporation with respect to its activities conducted within the United States.

(ii) The income and apportionment factors of that corporation that is a “controlled foreign corporation,” as defined in Section 957 of the Internal Revenue Code, to the extent determined by multiplying the income and apportionment factors of that corporation without application of this subparagraph by a fraction not to exceed one, the numerator of which is the “Subpart F income” of that corporation for that taxable year and the denominator of which is the “earnings and profits” of that corporation for that taxable year.

(B) For purposes of this paragraph, both of the following apply:

(i) “Subpart F income” means “Subpart F income” as defined in Section 952 of the Internal Revenue Code.

(ii) “Earnings and profits” means “earnings and profits” as described in Section 964 of the Internal Revenue Code.

(3) The income and apportionment factors of the corporations described in this subdivision shall be taken into account only to the extent that they would have been taken into account had no election under this section been made.

(4) The Franchise Tax Board shall prescribe regulations to coordinate implementation of subparagraph (A) of paragraph (2) to prevent multiple inclusion or exclusion of income and factors in situations where the same item of income is described in both clauses.

(b) For purposes of this article and Section 24411, all of the following definitions apply:

(1) An “affiliated corporation” means a corporation that is a member of a commonly controlled group as defined in Section 25105.

(2) A “qualified taxpayer” means a corporation that does both of the following:

(A) Files with the state tax return, on which the water’s-edge election is made, a consent to the taking of depositions, at the time and place most reasonably convenient to all parties, from key domestic corporate individuals and to the acceptance of subpoenas duces tecum requiring reasonable production of documents to the Franchise Tax Board, as provided in Section 19504, by the State Board of Equalization, as provided in Section 5005 of Title 18 of the California Code of Regulations, or by the courts of this state, as provided in Chapter 2 (commencing with Section 1985) of Title 3 of Part 4 of, and Chapter 9 (commencing with Section 2025.010) of Title 4 of Part 4 of, the Code of Civil Procedure. The consent relates to issues of jurisdiction and service and does not waive any defenses that a taxpayer may otherwise have. The consent shall remain in effect as long as the water's-edge election is in effect, and shall be limited to providing that information necessary to review or adjust income or deductions in a manner authorized by Section 482, 861, Subpart F of Part III of Subchapter N, or similar provisions, of the Internal Revenue Code, together with the regulations adopted pursuant to those provisions, and for the conduct of an investigation with respect to any unitary business in which the taxpayer may be involved.

(B) Agrees that, for purposes of this article, dividends received by any corporation whose income and apportionment factors are taken into account pursuant to subdivision (a) from either of the following are functionally related dividends and shall be presumed to be business income:

(i) A corporation of which more than 50 percent of the voting stock is owned, directly or indirectly, by members of the unitary group and which is engaged in the same general line of business.

(ii) Any corporation that is either a significant source of supply for the unitary business or a significant purchaser of the output of the unitary business, or that sells a significant part of its output or obtains a significant part of its raw materials or input from the unitary business. "Significant," as used in this subparagraph, means an amount of 15 percent or more of either input or output.

All other dividends shall be classified as business or nonbusiness income without regard to this subparagraph.

(3) The definitions and locations of property, payroll, and sales shall be determined under the laws and regulations that set forth the apportionment formulas used by the individual states to assign net income subject to taxes on, or measured by, net income in that state. If a state does not impose a tax on, or measured by, net income or does not have laws or regulations with respect to the assignment of property, payroll, and sales, the laws and regulations provided in Article 2 (commencing with Section 25120) shall apply.

Sales shall be considered to be made to a state only if the corporation making the sale may otherwise be subject to a tax on, or measured by, net income under the Constitution or laws of the United States, and shall not include sales made to a corporation whose income and apportionment factors are taken into account pursuant to subdivision (a) in determining the amount of income of the taxpayer derived from or attributable to sources within this state.

(4) "The United States" means the 50 states of the United States and the District of Columbia.

(5) (A) For purposes of this section, a "tax haven" means any ~~jurisdictions~~ *jurisdiction previously* identified ~~in Table 1 of Appendix I to the December 2008 Report of the United States Government Accountability Office on International Taxation (GAO-09-157) for which a United States District Court order granted leave for the federal Internal Revenue Service to serve a "John Doe" summons.~~ *by both the Internal Revenue Service as a secrecy jurisdiction in federal court proceedings and by the Organization for Economic Cooperation and Development in a 2002 list of committed jurisdictions and uncooperative tax havens, as described in Table 1 of Appendix I to the December 2008 Report of the United States Government Accountability Office on International Taxation (GAO-09-157), which means one of the following foreign jurisdictions:*

(i) Anguilla.

(ii) Antigua and Barbuda.

(iii) Aruba.

(iv) Bahamas.

(v) Belize.

(vi) Bermuda.

(vii) British Virgin Islands.

(viii) Cayman Islands.

(ix) Cook Islands.

(x) Cyprus.

(xi) Dominica.

(xii) Gibraltar.

(xiii) Grenada.

(xiv) Guernsey.

(xv) Isle of Man.

(xvi) Jersey.

(xvii) Liechtenstein.

(xviii) Malta.

(xix) Nauru.

(xx) Netherlands Antilles.

(xxi) Panama.
(xxii) Samoa.
(xxiii) St. Kitts and Nevis.
(xxiv) St. Lucia.
(xxv) St. Vincent and the Grenadines.
(xxvi) Turks and Caicos Islands.
(xxvii) Vanuatu.

(B) An additional jurisdiction shall be considered a "tax haven" for purposes of this section if the Secretary of the Treasury of the United States issues notice after January 1, 2011, declaring that the jurisdiction is recognized as a tax haven by the United States. A jurisdiction shall not be considered a "tax haven" for purposes of this section if the Secretary of the Treasury of the United States issues notice after January 1, 2011, declaring the jurisdiction is no longer recognized as a tax haven by the United States.

(C) The Franchise Tax Board shall annually issue a notice identifying the jurisdictions that are tax havens for purposes of this section for that tax year.

(c) All references in this part to income determined pursuant to Section 25101 shall also mean income determined pursuant to this section.

(d) This section shall remain in effect only until June 1, 2015, and as of that date is repealed.

SEC. 4. Section 25110 is added to the Revenue and Taxation Code, to read:

25110. (a) Notwithstanding Section 25101, a qualified taxpayer, as defined in paragraph (2) of subdivision (b), that is subject to the tax imposed under this part, may elect to determine its income derived from or attributable to sources within this state pursuant to a water's-edge election in accordance with the provisions of this part, as modified by this article. A taxpayer that makes a water's-edge election on or after January 1, 2006, shall take into account that portion of its own income and apportionment factors and the income and apportionment factors of its affiliated entities to the extent provided below:

(1) The entire income and apportionment factors of any of the following corporations:

(A) Domestic international sales corporations, as described in Sections 991 to 994, inclusive, of the Internal Revenue Code and foreign sales corporations as described in Sections 921 to 927, inclusive, of the Internal Revenue Code.

(B) Any corporation (other than a bank), regardless of the place where it is incorporated if the average of its property, payroll, and sales factors within the United States is 20 percent or more.

(C) Corporations that are incorporated in the United States, excluding corporations making an election pursuant to Sections 931 to 936, inclusive, of the Internal Revenue Code.

(D) Export trade corporations, as described in Sections 970 to 972, inclusive, of the Internal Revenue Code.

(2) (A) With respect to a corporation that is not described in subparagraphs (A), (B), (C), and (D) of paragraph (1), as provided in either one or both of the following clauses:

(i) The income and apportionment factors of that corporation to the extent of its income derived from or attributable to sources within the United States and its factors assignable to a location within the United States in accordance with paragraph (3) of subdivision (b). Income of that corporation derived from or attributable to sources within the United States as determined by federal income tax laws shall be limited to, and determined from, the books of account maintained by the corporation with respect to its activities conducted within the United States.

(ii) The income and apportionment factors of that corporation that is a "controlled foreign corporation," as defined in Section 957 of the Internal Revenue Code, to the extent determined by multiplying the income and apportionment factors of that corporation without application of this subparagraph by a fraction not to exceed one, the numerator of which is the "Subpart F income" of that corporation for that taxable year and the denominator of which is the "earnings and profits" of that corporation for that taxable year.

(B) For purposes of this paragraph, both of the following apply:

(i) "Subpart F income" means "Subpart F income" as defined in Section 952 of the Internal Revenue Code.

(ii) "Earnings and profits" means "earnings and profits" as described in Section 964 of the Internal Revenue Code.

(3) The income and apportionment factors of the corporations described in this subdivision shall be taken into account only to the extent that they would have been taken into account had no election under this section been made.

(4) The Franchise Tax Board shall prescribe regulations to coordinate implementation of subparagraph (A) of paragraph (2) to prevent multiple inclusion or exclusion of income and factors in situations where the same item of income is described in clauses.

(b) For purposes of this article and Section 24411, all of the following definitions apply:

(1) An "affiliated corporation" means a corporation that is a member of a commonly controlled group as defined in Section 25105.

(2) A "qualified taxpayer" means a corporation that does both of the following:

(A) Files with the state tax return, on which the water's-edge election is made, a consent to the taking of depositions, at the time and place most reasonably convenient to all parties, from key domestic corporate individuals and to the acceptance of subpoenas duces tecum requiring reasonable production of documents to the Franchise Tax Board, as provided in Section 19504, by the State Board of Equalization, as provided in Section 5005 of Title 18 of the California Code of Regulations, or by the courts of this state, as provided in Chapter 2 (commencing with Section 1985) of Title 3 of Part 4 of, and Chapter 9 (commencing with Section 2025.010) of Title 4 of Part 4 of, the Code of Civil Procedure. The consent relates to issues of jurisdiction and service and does not waive any defenses that a taxpayer may otherwise have. The consent shall remain in effect as long as the water's-edge election is in effect, and shall be limited to providing that information necessary to review or adjust income or deductions in a manner authorized by Section 482, 861, Subpart F of Part III of Subchapter N, or similar provisions, of the Internal Revenue Code, together with the regulations adopted pursuant to those provisions, and for the conduct of an investigation with respect to any unitary business in which the taxpayer may be involved.

(B) Agrees that, for purposes of this article, dividends received by any corporation whose income and apportionment factors are taken into account pursuant to subdivision (a) from either of the following are functionally related dividends and shall be presumed to be business income:

(i) A corporation of which more than 50 percent of the voting stock is owned, directly or indirectly, by members of the unitary group and which is engaged in the same general line of business.

(ii) Any corporation that is either a significant source of supply for the unitary business or a significant purchaser of the output of the unitary business, or that sells a significant part of its output or obtains a significant part of its raw materials or input from the unitary business. "Significant," as used in this subparagraph, means an amount of 15 percent or more of either input or output.

All other dividends shall be classified as business or nonbusiness income without regard to this subparagraph.

(3) The definitions and locations of property, payroll, and sales shall be determined under the laws and regulations that set forth the apportionment formulas used by the individual states to assign net income subject to taxes on, or measured by, net income in that state. If a state does not impose a tax on, or measured by, net income or does not have laws or regulations with respect to the assignment of property, payroll, and sales, the laws and regulations provided in Article 2 (commencing with Section 25120) shall apply.

Sales shall be considered to be made to a state only if the corporation making the sale may otherwise be subject to a tax on, or measured by, net income under the Constitution or laws of the United States, and shall not include sales made to a corporation whose income and apportionment factors are taken into account pursuant to subdivision (a) in determining the amount of income of the taxpayer derived from or attributable to sources within this state.

(4) "The United States" means the 50 states of the United States and the District of Columbia.

(c) All references in this part to income determined pursuant to Section 25101 shall also mean income determined pursuant to this section.

(d) This section shall become operative on July 1, 2014, and apply to taxable years beginning on or after July 1, 2014.

SEC. 5. This act provides for a tax levy within the meaning of Article IV of the Constitution and shall go into immediate effect.

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