

AMENDED IN ASSEMBLY APRIL 8, 2013

CALIFORNIA LEGISLATURE—2013–14 REGULAR SESSION

ASSEMBLY BILL

No. 769

Introduced by Assembly Member Skinner

February 21, 2013

An act to amend Sections 17276.20, 17276.21, 17276.22, 24416.20, 24416.21, and 24416.22 of, *and to add Sections 41, 42, and 43 to*, the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.

LEGISLATIVE COUNSEL'S DIGEST

AB 769, as amended, Skinner. Taxation: *tax expenditures: operative dates: deductions: net operating loss carrybacks.*

Existing law imposes various taxes and allows specified credits, deductions, exclusions, and exemptions in computing those taxes. The Franchise Tax Board administers the Personal Income Tax Law and the Corporation Tax Law, the State Board of Equalization administers the Sales and Use Tax Law, and various other tax laws.

This bill would require any measure, introduced on or after January 1, 2014, that would allow a personal income or corporation tax credit to contain, among other provisions, (1) specified goals, purposes, and objectives that the tax credit will achieve, (2) detailed performance indicators to measure whether the tax credit is meeting those goals, purposes, and objectives, and (3) a requirement that the tax credit cease to be operative no later than 3 years after its effective date, as specified. This bill would also require for passage of a measure that allows a new credit, the approval of $\frac{2}{3}$ of the membership of each house of the Legislature.

This bill would also require the State Board of Equalization and the Franchise Tax Board to adopt, for tax expenditures, as defined, enacted before January 1, 2014, specified goals, purposes, and objectives that the tax expenditure will achieve, detailed performance indicators and data collection requirements for the Legislature to measure or determine whether the tax expenditures are meeting, failing to meet, or exceeding those goals, purposes, and objectives. This bill would also make those specified tax expenditures inoperative on June 20, 2017, unless the inoperative date is extended, as specified.

The Personal Income Tax Law and the Corporation Tax Law allow individual and corporate taxpayers to utilize net operating losses and carryovers and carrybacks of those losses for purposes of offsetting their individual and corporate tax liabilities. Existing law allows net operating losses attributable to taxable years beginning on or after January 1, 2013, to be carrybacks to each of the preceding 2 taxable years, as provided.

This bill would disallow the use of net operating loss carrybacks by individual and corporate taxpayers.

This bill would include a change in state statute that would result in a taxpayer paying a higher tax within the meaning of Section 3 of Article XIII A of the California Constitution, and thus would require for passage the approval of $\frac{2}{3}$ of the membership of each house of the Legislature.

This bill would take effect immediately as a tax levy.

Vote: $\frac{2}{3}$. Appropriation: no. Fiscal committee: yes.
State-mandated local program: no.

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

- 1 SECTION 1. *The Legislature finds and declares the following:*
- 2 (a) *Government at all levels enacts tax preferences to promote*
- 3 *equity among taxpayers and enhance economic growth in a way*
- 4 *that is inexpensive to administer and provides direct benefits to*
- 5 *taxpayers.*
- 6 (b) *National and state public finance experts recommend that*
- 7 *tax preferences be evaluated alongside direct spending programs,*
- 8 *as both are public initiatives meant to accomplish specified goals.*
- 9 (c) *California foregoes more than \$49 billion in revenue from*
- 10 *tax preferences, according to the Department of Finance.*

1 (d) Many current tax preferences contain neither sunset
2 provisions nor goals and objectives to measure the performance
3 of the tax preference.

4 (e) Many current tax preferences neither require taxpayers to
5 submit data demonstrating the tax incentive's effectiveness nor
6 for state agencies to collect and send data to the Legislature to
7 evaluate the tax incentive.

8 (f) The Legislature should apply the same level of review and
9 performance measure that it applies to spending programs to tax
10 incentive programs, including tax credits.

11 SEC. 2. Section 41 is added to the Revenue and Taxation Code,
12 to read:

13 41. Notwithstanding any other law, any bill, introduced on or
14 after January 1, 2014, that would allow a new credit against the
15 "net tax," as defined in Section 17039, or against the "tax," as
16 defined in Section 23036, or both, shall contain all of the following:

17 (a) Specific goals, purposes, and objectives that the tax credit
18 will achieve.

19 (b) Detailed performance indicators for the Legislature to use
20 when measuring whether the tax credit meets the goals, purposes,
21 and objectives stated in the bill.

22 (c) Data collection requirements to enable the Legislature to
23 determine whether the tax credit is meeting, failing to meet, or
24 exceeding those specific goals, purposes, and objectives. The
25 requirements shall include the specific data and baseline
26 measurements to be collected and remitted in each year the credit
27 is in effect, in order for the Legislature to measure the change in
28 performance indicators, and the specific taxpayers, state agencies,
29 or other entities required to collect and remit data.

30 (d) A requirement that the tax credit shall cease to be operative
31 no later than three years after its effective date, and as of
32 December 1 of that year is repealed.

33 (e) The enactment of a measure that allows a credit shall require
34 for its passage a two-thirds vote of the membership of both houses
35 of the Legislature.

36 SEC. 3. Section 42 is added to the Revenue and Taxation Code,
37 to read:

38 42. (a) Notwithstanding any other law, the board shall adopt
39 the following for tax expenditures enacted prior to January 1,
40 2014:

1 (1) *Specific goals, purposes, and objectives that the tax*
2 *expenditure will achieve.*

3 (2) *Detailed performance indicators for the Legislature to use*
4 *when measuring whether the tax expenditure meets the goals,*
5 *purposes, and objectives.*

6 (3) *Data collection requirements to enable the Legislature to*
7 *determine whether the tax expenditure is meeting, failing to meet,*
8 *or exceeding those specific goals, purposes, and objectives. The*
9 *requirements shall include the specific data and baseline*
10 *measurements to be collected and remitted in each year the tax*
11 *expenditure is in effect, in order for the Legislature to measure*
12 *the change in performance indicators, and the specific taxpayers,*
13 *state agencies, or other entities required to collect and remit data.*

14 (b) *For the purposes of this section, “tax expenditure” means*
15 *an exclusion, exemption, or other tax benefit established in the*
16 *following provisions:*

17 (1) *Sections 995, 6010.6, 6010.9, 6356.5, 6357.1, 6357.5, 6358,*
18 *6359, 6362.7, 6366, 6378, 6379.5, and 6385.*

19 (2) *Section 6010.8 of this code and Division 16 (commencing*
20 *with Section 26000) of the Public Resources Code.*

21 (c) *A tax expenditure subject to this section shall cease to be*
22 *operative on June 20, 2017, unless a later enacted statute in a bill*
23 *related to the budget extends that date.*

24 SEC. 4. *Section 43 is added to the Revenue and Taxation Code,*
25 *to read:*

26 43. (a) *Notwithstanding any other law, the Franchise Tax*
27 *Board shall adopt the following for tax expenditures enacted prior*
28 *to January 1, 2014:*

29 (1) *Specific goals, purposes, and objectives that the tax*
30 *expenditure will achieve.*

31 (2) *Detailed performance indicators for the Legislature to use*
32 *when measuring whether the tax expenditure meets the goals,*
33 *purposes, and objectives.*

34 (3) *Data collection requirements to enable the Legislature to*
35 *determine whether the tax expenditure is meeting, failing to meet,*
36 *or exceeding those specific goals, purposes, and objectives. The*
37 *requirements shall include the specific data and baseline*
38 *measurements to be collected and remitted in each year the tax*
39 *expenditure is in effect, in order for the Legislature to measure*

1 *the change in performance indicators, and the specific taxpayers,*
2 *state agencies, or other entities required to collect and remit data.*

3 (b) *For the purposes of this section, “tax expenditure” means*
4 *an exclusion, credit, deduction, or other tax benefit established in*
5 *Sections 17052.12, 17053.80, 17087, 17087.5, 17201, 17681,*
6 *17955, 18006, 18031, 18035.6, 18036.6, 18152.5, 23609, 23623,*
7 *23800, 23800.5, 23801, 23802, 23802.5, 23803, 23804, 23806,*
8 *23807, 23808, 23809, 23811, 23813, 24365, 24831, 24941, 25110,*
9 *25111, 25111.1, 25112, and 25113.*

10 (c) *A tax expenditure subject to this section shall cease to be*
11 *operative on June 20, 2017, unless a later enacted statute in a bill*
12 *related to the budget extends that date.*

SECTION 1.

14 SEC. 5. Section 17276.20 of the Revenue and Taxation Code
15 is amended to read:

16 17276.20. Except as provided in Sections 17276.1, 17276.2,
17 17276.4, 17276.5, 17276.6, and 17276.7, the deduction provided
18 by Section 172 of the Internal Revenue Code, relating to net
19 operating loss deduction, shall be modified as follows:

20 (a) (1) Net operating losses attributable to taxable years
21 beginning before January 1, 1987, shall not be allowed.

22 (2) A net operating loss shall not be carried forward to any
23 taxable year beginning before January 1, 1987.

24 (b) (1) Except as provided in paragraphs (2) and (3), the
25 provisions of Section 172(b)(2) of the Internal Revenue Code,
26 relating to amount of carrybacks and carryovers, shall be modified
27 so that the applicable percentage of the entire amount of the net
28 operating loss for any taxable year shall be eligible for carryover
29 to any subsequent taxable year. For purposes of this subdivision,
30 the applicable percentage shall be:

31 (A) Fifty percent for any taxable year beginning before January
32 1, 2000.

33 (B) Fifty-five percent for any taxable year beginning on or after
34 January 1, 2000, and before January 1, 2002.

35 (C) Sixty percent for any taxable year beginning on or after
36 January 1, 2002, and before January 1, 2004.

37 (D) One hundred percent for any taxable year beginning on or
38 after January 1, 2004.

39 (2) In the case of a taxpayer who has a net operating loss in any
40 taxable year beginning on or after January 1, 1994, and who

1 operates a new business during that taxable year, each of the
2 following shall apply to each loss incurred during the first three
3 taxable years of operating the new business:

4 (A) If the net operating loss is equal to or less than the net loss
5 from the new business, 100 percent of the net operating loss shall
6 be carried forward as provided in subdivision (d).

7 (B) If the net operating loss is greater than the net loss from the
8 new business, the net operating loss shall be carried over as
9 follows:

10 (i) With respect to an amount equal to the net loss from the new
11 business, 100 percent of that amount shall be carried forward as
12 provided in subdivision (d).

13 (ii) With respect to the portion of the net operating loss that
14 exceeds the net loss from the new business, the applicable
15 percentage of that amount shall be carried forward as provided in
16 subdivision (d).

17 (C) For purposes of Section 172(b)(2) of the Internal Revenue
18 Code, the amount described in clause (ii) of subparagraph (B) shall
19 be absorbed before the amount described in clause (i) of
20 subparagraph (B).

21 (3) In the case of a taxpayer who has a net operating loss in any
22 taxable year beginning on or after January 1, 1994, and who
23 operates an eligible small business during that taxable year, each
24 of the following shall apply:

25 (A) If the net operating loss is equal to or less than the net loss
26 from the eligible small business, 100 percent of the net operating
27 loss shall be carried forward to the taxable years specified in
28 subdivision (d).

29 (B) If the net operating loss is greater than the net loss from the
30 eligible small business, the net operating loss shall be carried over
31 as follows:

32 (i) With respect to an amount equal to the net loss from the
33 eligible small business, 100 percent of that amount shall be carried
34 forward as provided in subdivision (d).

35 (ii) With respect to that portion of the net operating loss that
36 exceeds the net loss from the eligible small business, the applicable
37 percentage of that amount shall be carried forward as provided in
38 subdivision (d).

39 (C) For purposes of Section 172(b)(2) of the Internal Revenue
40 Code, the amount described in clause (ii) of subparagraph (B) shall

1 be absorbed before the amount described in clause (i) of
2 subparagraph (B).

3 (4) In the case of a taxpayer who has a net operating loss in a
4 taxable year beginning on or after January 1, 1994, and who
5 operates a business that qualifies as both a new business and an
6 eligible small business under this section, that business shall be
7 treated as a new business for the first three taxable years of the
8 new business.

9 (5) In the case of a taxpayer who has a net operating loss in a
10 taxable year beginning on or after January 1, 1994, and who
11 operates more than one business, and more than one of those
12 businesses qualifies as either a new business or an eligible small
13 business under this section, paragraph (2) shall be applied first,
14 except that if there is any remaining portion of the net operating
15 loss after application of clause (i) of subparagraph (B) of that
16 paragraph, paragraph (3) shall be applied to the remaining portion
17 of the net operating loss as though that remaining portion of the
18 net operating loss constituted the entire net operating loss.

19 (6) For purposes of this section, the term “net loss” means the
20 amount of net loss after application of Sections 465 and 469 of the
21 Internal Revenue Code.

22 (c) Net operating loss carrybacks shall not be allowed.

23 (d) (1) (A) For a net operating loss for any taxable year
24 beginning on or after January 1, 1987, and before January 1, 2000,
25 Section 172(b)(1)(A)(ii) of the Internal Revenue Code is modified
26 to substitute “five taxable years” in lieu of “20 taxable years”
27 except as otherwise provided in paragraphs (2) and (3).

28 (B) For a net operating loss for any taxable year beginning on
29 or after January 1, 2000, and before January 1, 2008, Section
30 172(b)(1)(A)(ii) of the Internal Revenue Code is modified to
31 substitute “10 taxable years” in lieu of “20 taxable years.”

32 (2) For any taxable year beginning before January 1, 2000, in
33 the case of a “new business,” the “five taxable years” in paragraph
34 (1) shall be modified to read as follows:

35 (A) “Eight taxable years” for a net operating loss attributable
36 to the first taxable year of that new business.

37 (B) “Seven taxable years” for a net operating loss attributable
38 to the second taxable year of that new business.

39 (C) “Six taxable years” for a net operating loss attributable to
40 the third taxable year of that new business.

(3) For any carryover of a net operating loss for which a deduction is denied by Section 17276.3, the carryover period specified in this subdivision shall be extended as follows:

(A) By one year for a net operating loss attributable to taxable years beginning in 1991.

(B) By two years for a net operating loss attributable to taxable years beginning prior to January 1, 1991.

(4) The net operating loss attributable to taxable years beginning on or after January 1, 1987, and before January 1, 1994, shall be a net operating loss carryover to each of the 10 taxable years following the year of the loss if it is incurred by a taxpayer that is under the jurisdiction of the court in a Title 11 or similar case at any time during the income year. The loss carryover provided in the preceding sentence shall not apply to any loss incurred after the date the taxpayer is no longer under the jurisdiction of the court in a Title 11 or similar case.

(e) For purposes of this section:

(1) "Eligible small business" means any trade or business that has gross receipts, less returns and allowances, of less than one million dollars (\$1,000,000) during the taxable year.

(2) Except as provided in subdivision (f), "new business" means any trade or business activity that is first commenced in this state on or after January 1, 1994.

(3) "Title 11 or similar case" shall have the same meaning as in Section 368(a)(3) of the Internal Revenue Code.

(4) In the case of any trade or business activity conducted by a partnership or "S" corporation paragraphs (1) and (2) shall be applied to the partnership or "S" corporation.

(f) For purposes of this section, in determining whether a trade or business activity qualifies as a new business under paragraph (2) of subdivision (e), the following rules shall apply:

(1) In any case where a taxpayer purchases or otherwise acquires all or any portion of the assets of an existing trade or business (irrespective of the form of entity) that is doing business in this state (within the meaning of Section 23101), the trade or business thereafter conducted by the taxpayer (or any related person) shall not be treated as a new business if the aggregate fair market value of the acquired assets (including real, personal, tangible, and intangible property) used by the taxpayer (or any related person) in the conduct of its trade or business exceeds 20 percent of the

1 aggregate fair market value of the total assets of the trade or
2 business being conducted by the taxpayer (or any related person).
3 For purposes of this paragraph only, the following rules shall apply:

4 (A) The determination of the relative fair market values of the
5 acquired assets and the total assets shall be made as of the last day
6 of the first taxable year in which the taxpayer (or any related
7 person) first uses any of the acquired trade or business assets in
8 its business activity.

9 (B) Any acquired assets that constituted property described in
10 Section 1221(1) of the Internal Revenue Code in the hands of the
11 transferor shall not be treated as assets acquired from an existing
12 trade or business, unless those assets also constitute property
13 described in Section 1221(1) of the Internal Revenue Code in the
14 hands of the acquiring taxpayer (or related person).

15 (2) In any case where a taxpayer (or any related person) is
16 engaged in one or more trade or business activities in this state, or
17 has been engaged in one or more trade or business activities in this
18 state within the preceding 36 months (“prior trade or business
19 activity”), and thereafter commences an additional trade or business
20 activity in this state, the additional trade or business activity shall
21 only be treated as a new business if the additional trade or business
22 activity is classified under a different division of the Standard
23 Industrial Classification (SIC) Manual published by the United
24 States Office of Management and Budget, 1987 edition, than are
25 any of the taxpayer’s (or any related person’s) current or prior
26 trade or business activities.

27 (3) In any case where a taxpayer, including all related persons,
28 is engaged in trade or business activities wholly outside of this
29 state and the taxpayer first commences doing business in this state
30 (within the meaning of Section 23101) after December 31, 1993
31 (other than by purchase or other acquisition described in paragraph
32 (1)), the trade or business activity shall be treated as a new business
33 under paragraph (2) of subdivision (e).

34 (4) In any case where the legal form under which a trade or
35 business activity is being conducted is changed, the change in form
36 shall be disregarded and the determination of whether the trade or
37 business activity is a new business shall be made by treating the
38 taxpayer as having purchased or otherwise acquired all or any
39 portion of the assets of an existing trade or business under the rules
40 of paragraph (1) of this subdivision.

1 (5) “Related person” shall mean any person that is related to
2 the taxpayer under either Section 267 or 318 of the Internal
3 Revenue Code.

4 (6) “Acquire” shall include any gift, inheritance, transfer incident
5 to divorce, or any other transfer, whether or not for consideration.

6 (7) (A) For taxable years beginning on or after January 1, 1997,
7 the term “new business” shall include any taxpayer that is engaged
8 in biopharmaceutical activities or other biotechnology activities
9 that are described in Codes 2833 to 2836, inclusive, of the Standard
10 Industrial Classification (SIC) Manual published by the United
11 States Office of Management and Budget, 1987 edition, and as
12 further amended, and that has not received regulatory approval for
13 any product from the United States Food and Drug Administration.

14 (B) For purposes of this paragraph:

15 (i) “Biopharmaceutical activities” means those activities that
16 use organisms or materials derived from organisms, and their
17 cellular, subcellular, or molecular components, in order to provide
18 pharmaceutical products for human or animal therapeutics and
19 diagnostics. Biopharmaceutical activities make use of living
20 organisms to make commercial products, as opposed to
21 pharmaceutical activities that make use of chemical compounds
22 to produce commercial products.

23 (ii) “Other biotechnology activities” means activities consisting
24 of the application of recombinant DNA technology to produce
25 commercial products, as well as activities regarding pharmaceutical
26 delivery systems designed to provide a measure of control over
27 the rate, duration, and site of pharmaceutical delivery.

28 (g) In computing the modifications under Section 172(d)(2) of
29 the Internal Revenue Code, relating to capital gains and losses of
30 taxpayers other than corporations, the exclusion provided by
31 Section 18152.5 shall not be allowed.

32 (h) Notwithstanding any provisions of this section to the
33 contrary, a deduction shall be allowed to a “qualified taxpayer” as
34 provided in Sections 17276.1, 17276.2, 17276.4, 17276.5, 17276.6,
35 and 17276.7.

36 (i) The Franchise Tax Board may prescribe appropriate
37 regulations to carry out the purposes of this section, including any
38 regulations necessary to prevent the avoidance of the purposes of
39 this section through split-ups, shell corporations, partnerships,
40 tiered ownership structures, or otherwise.

1 (j) The Franchise Tax Board may reclassify any net operating
2 loss carryover determined under either paragraph (2) or (3) of
3 subdivision (b) as a net operating loss carryover under paragraph
4 (1) of subdivision (b) upon a showing that the reclassification is
5 necessary to prevent evasion of the purposes of this section.

6 (k) Except as otherwise provided, the amendments made by
7 Chapter 107 of the Statutes of 2000 shall apply to net operating
8 losses for taxable years beginning on or after January 1, 2000.

9 ~~SEC. 2.~~

10 *SEC. 6.* Section 17276.21 of the Revenue and Taxation Code
11 is amended to read:

12 17276.21. (a) Notwithstanding Sections 17276, 17276.1,
13 17276.2, 17276.4, 17276.5, 17276.6, 17276.7, and 17276.20 of
14 this code and Section 172 of the Internal Revenue Code, no net
15 operating loss deduction shall be allowed for any taxable year
16 beginning on or after January 1, 2008, and before January 1, 2012.

17 (b) For any net operating loss or carryover of a net operating
18 loss for which a deduction is denied by subdivision (a), the
19 carryover period under Section 172 of the Internal Revenue Code
20 shall be extended as follows:

21 (1) By one year, for losses incurred in taxable years beginning
22 on or after January 1, 2010, and before January 1, 2011.

23 (2) By two years, for losses incurred in taxable years beginning
24 on or after January 1, 2009, and before January 1, 2010.

25 (3) By three years, for losses incurred in taxable years beginning
26 on or after January 1, 2008, and before January 1, 2009.

27 (4) By four years, for losses incurred in taxable years beginning
28 before January 1, 2008.

29 (c) The provisions of this section shall not apply to the following
30 taxpayers:

31 (1) For any taxable year beginning on or after January 1, 2008,
32 and before January 1, 2010, this section shall not apply to a
33 taxpayer with net business income of less than five hundred
34 thousand dollars (\$500,000) for the taxable year. For purposes of
35 this paragraph, business income means:

36 (A) Income from a trade or business, whether conducted by the
37 taxpayer or by a pass-thru entity owned directly or indirectly by
38 the taxpayer. For purposes of this paragraph, the term "pass-thru
39 entity" means a partnership or an "S" corporation.

40 (B) Income from rental activity.

1 (C) Income attributable to a farming business.

2 (2) For any taxable year beginning on or after January 1, 2010,
3 and before January 1, 2012, this section shall not apply to a
4 taxpayer with modified adjusted gross income of less than three
5 hundred thousand dollars (\$300,000) for the taxable year. For
6 purposes of this paragraph, “modified adjusted gross income”
7 means the amount described in paragraph (2) of subdivision (h)
8 of Section 17024.5, determined without regard to the deduction
9 allowed under Section 172 of the Internal Revenue Code, relating
10 to net operating loss deduction.

11 ~~SEC. 3.~~

12 *SEC. 7.* Section 17276.22 of the Revenue and Taxation Code
13 is amended to read:

14 17276.22. Notwithstanding Section 17276.1, 17276.2, 17276.4,
15 17276.5, 17276.6, or 17276.7 to the contrary, a net operating loss
16 attributable to a taxable year beginning on or after January 1, 2008,
17 shall be a net operating carryover to each of the 20 taxable years
18 following the year of the loss.

19 ~~SEC. 4.~~

20 *SEC. 8.* Section 24416.20 of the Revenue and Taxation Code
21 is amended to read:

22 24416.20. Except as provided in Sections 24416.1, 24416.2,
23 24416.4, 24416.5, 24416.6, and 24416.7, a net operating loss
24 deduction shall be allowed in computing net income under Section
25 24341 and shall be determined in accordance with Section 172 of
26 the Internal Revenue Code, except as otherwise provided.

27 (a) (1) Net operating losses attributable to taxable years
28 beginning before January 1, 1987, shall not be allowed.

29 (2) A net operating loss shall not be carried forward to any
30 taxable year beginning before January 1, 1987.

31 (b) (1) Except as provided in paragraphs (2) and (3), the
32 provisions of Section 172(b)(2) of the Internal Revenue Code,
33 relating to amount of carrybacks and carryovers, shall be modified
34 so that the applicable percentage of the entire amount of the net
35 operating loss for any taxable year shall be eligible for carryover
36 to any subsequent taxable year. For purposes of this subdivision,
37 the applicable percentage shall be:

38 (A) Fifty percent for any taxable year beginning before January
39 1, 2000.

1 (B) Fifty-five percent for any taxable year beginning on or after
2 January 1, 2000, and before January 1, 2002.

3 (C) Sixty percent for any taxable year beginning on or after
4 January 1, 2002, and before January 1, 2004.

5 (D) One hundred percent for any taxable year beginning on or
6 after January 1, 2004.

7 (2) In the case of a taxpayer who has a net operating loss in any
8 taxable year beginning on or after January 1, 1994, and who
9 operates a new business during that taxable year, each of the
10 following shall apply to each loss incurred during the first three
11 taxable years of operating the new business:

12 (A) If the net operating loss is equal to or less than the net loss
13 from the new business, 100 percent of the net operating loss shall
14 be carried forward as provided in subdivision (e).

15 (B) If the net operating loss is greater than the net loss from the
16 new business, the net operating loss shall be carried over as
17 follows:

18 (i) With respect to an amount equal to the net loss from the new
19 business, 100 percent of that amount shall be carried forward as
20 provided in subdivision (e).

21 (ii) With respect to the portion of the net operating loss that
22 exceeds the net loss from the new business, the applicable
23 percentage of that amount shall be carried forward as provided in
24 subdivision (d).

25 (C) For purposes of Section 172(b)(2) of the Internal Revenue
26 Code, the amount described in clause (ii) of subparagraph (B) shall
27 be absorbed before the amount described in clause (i) of
28 subparagraph (B).

29 (3) In the case of a taxpayer who has a net operating loss in any
30 taxable year beginning on or after January 1, 1994, and who
31 operates an eligible small business during that taxable year, each
32 of the following shall apply:

33 (A) If the net operating loss is equal to or less than the net loss
34 from the eligible small business, 100 percent of the net operating
35 loss shall be carried forward to the taxable years specified in
36 paragraph (1) of subdivision (e).

37 (B) If the net operating loss is greater than the net loss from the
38 eligible small business, the net operating loss shall be carried over
39 as follows:

1 (i) With respect to an amount equal to the net loss from the
2 eligible small business, 100 percent of that amount shall be carried
3 forward as provided in subdivision (e).

4 (ii) With respect to that portion of the net operating loss that
5 exceeds the net loss from the eligible small business, the applicable
6 percentage of that amount shall be carried forward as provided in
7 subdivision (e).

8 (C) For purposes of Section 172(b)(2) of the Internal Revenue
9 Code, the amount described in clause (ii) of subparagraph (B) shall
10 be absorbed before the amount described in clause (i) of
11 subparagraph (B).

12 (4) In the case of a taxpayer who has a net operating loss in a
13 taxable year beginning on or after January 1, 1994, and who
14 operates a business that qualifies as both a new business and an
15 eligible small business under this section, that business shall be
16 treated as a new business for the first three taxable years of the
17 new business.

18 (5) In the case of a taxpayer who has a net operating loss in a
19 taxable year beginning on or after January 1, 1994, and who
20 operates more than one business, and more than one of those
21 businesses qualifies as either a new business or an eligible small
22 business under this section, paragraph (2) shall be applied first,
23 except that if there is any remaining portion of the net operating
24 loss after application of clause (i) of subparagraph (B) of paragraph
25 (2), paragraph (3) shall be applied to the remaining portion of the
26 net operating loss as though that remaining portion of the net
27 operating loss constituted the entire net operating loss.

28 (6) For purposes of this section, “net loss” means the amount
29 of net loss after application of Sections 465 and 469 of the Internal
30 Revenue Code.

31 (c) For any taxable year in which the taxpayer has in effect a
32 water’s-edge election under Section 25110, the deduction of a net
33 operating loss carryover shall be denied to the extent that the net
34 operating loss carryover was determined by taking into account
35 the income and factors of an affiliated corporation in a combined
36 report whose income and apportionment factors would not have
37 been taken into account if a water’s-edge election under Section
38 25110 had been in effect for the taxable year in which the loss was
39 incurred.

40 (d) Net operating loss carrybacks shall not be allowed.

(e) (1) (A) For a net operating loss for any taxable year beginning on or after January 1, 1987, and before January 1, 2000, Section 172(b)(1)(A)(ii) of the Internal Revenue Code is modified to substitute “five taxable years” in lieu of “20 years” except as otherwise provided in paragraphs (2), (3), and (4).

(B) For a net operating loss for any income year beginning on or after January 1, 2000, and before January 1, 2008, Section 172(b)(1)(A)(ii) of the Internal Revenue Code is modified to substitute “10 taxable years” in lieu of “20 taxable years.”

(2) For any income year beginning before January 1, 2000, in the case of a “new business,” the “five taxable years” referred to in paragraph (1) shall be modified to read as follows:

(A) “Eight taxable years” for a net operating loss attributable to the first taxable year of that new business.

(B) “Seven taxable years” for a net operating loss attributable to the second taxable year of that new business.

(C) “Six taxable years” for a net operating loss attributable to the third taxable year of that new business.

(3) For any carryover of a net operating loss for which a deduction is denied by Section 24416.3, the carryover period specified in this subdivision shall be extended as follows:

(A) By one year for a net operating loss attributable to taxable years beginning in 1991.

(B) By two years for a net operating loss attributable to taxable years beginning prior to January 1, 1991.

(4) The net operating loss attributable to taxable years beginning on or after January 1, 1987, and before January 1, 1994, shall be a net operating loss carryover to each of the 10 taxable years following the year of the loss if it is incurred by a corporation that was either of the following:

(A) Under the jurisdiction of the court in a Title 11 or similar case at any time prior to January 1, 1994. The loss carryover provided in the preceding sentence shall not apply to any loss incurred in an income year after the taxable year during which the corporation is no longer under the jurisdiction of the court in a Title 11 or similar case.

(B) In receipt of assets acquired in a transaction that qualifies as a tax-free reorganization under Section 368(a)(1)(G) of the Internal Revenue Code.

(f) For purposes of this section:

1 (1) “Eligible small business” means any trade or business that
2 has gross receipts, less returns and allowances, of less than one
3 million dollars (\$1,000,000) during the income year.

4 (2) Except as provided in subdivision (g), “new business” means
5 any trade or business activity that is first commenced in this state
6 on or after January 1, 1994.

7 (3) “Title 11 or similar case” shall have the same meaning as
8 in Section 368(a)(3) of the Internal Revenue Code.

9 (4) In the case of any trade or business activity conducted by a
10 partnership or an “S” corporation, paragraphs (1) and (2) shall be
11 applied to the partnership or “S” corporation.

12 (g) For purposes of this section, in determining whether a trade
13 or business activity qualifies as a new business under paragraph
14 (2) of subdivision (e), the following rules shall apply:

15 (1) In any case where a taxpayer purchases or otherwise acquires
16 all or any portion of the assets of an existing trade or business
17 (irrespective of the form of entity) that is doing business in this
18 state (within the meaning of Section 23101), the trade or business
19 thereafter conducted by the taxpayer (or any related person) shall
20 not be treated as a new business if the aggregate fair market value
21 of the acquired assets (including real, personal, tangible, and
22 intangible property) used by the taxpayer (or any related person)
23 in the conduct of its trade or business exceeds 20 percent of the
24 aggregate fair market value of the total assets of the trade or
25 business being conducted by the taxpayer (or any related person).
26 For purposes of this paragraph only, the following rules shall apply:

27 (A) The determination of the relative fair market values of the
28 acquired assets and the total assets shall be made as of the last day
29 of the first taxable year in which the taxpayer (or any related
30 person) first uses any of the acquired trade or business assets in
31 its business activity.

32 (B) Any acquired assets that constituted property described in
33 Section 1221(1) of the Internal Revenue Code in the hands of the
34 transferor shall not be treated as assets acquired from an existing
35 trade or business, unless those assets also constitute property
36 described in Section 1221(1) of the Internal Revenue Code in the
37 hands of the acquiring taxpayer (or related person).

38 (2) In any case where a taxpayer (or any related person) is
39 engaged in one or more trade or business activities in this state, or
40 has been engaged in one or more trade or business activities in this

1 state within the preceding 36 months (“prior trade or business
2 activity”), and thereafter commences an additional trade or business
3 activity in this state, the additional trade or business activity shall
4 only be treated as a new business if the additional trade or business
5 activity is classified under a different division of the Standard
6 Industrial Classification (SIC) Manual published by the United
7 States Office of Management and Budget, 1987 edition, than are
8 any of the taxpayer’s (or any related person’s) current or prior
9 trade or business activities.

10 (3) In any case where a taxpayer, including all related persons,
11 is engaged in trade or business activities wholly outside of this
12 state and the taxpayer first commences doing business in this state
13 (within the meaning of Section 23101) after December 31, 1993
14 (other than by purchase or other acquisition described in paragraph
15 (1)), the trade or business activity shall be treated as a new business
16 under paragraph (2) of subdivision (e).

17 (4) In any case where the legal form under which a trade or
18 business activity is being conducted is changed, the change in form
19 shall be disregarded and the determination of whether the trade or
20 business activity is a new business shall be made by treating the
21 taxpayer as having purchased or otherwise acquired all or any
22 portion of the assets of an existing trade or business under the rules
23 of paragraph (1) of this subdivision.

24 (5) “Related person” shall mean any person that is related to
25 the taxpayer under either Section 267 or 318 of the Internal
26 Revenue Code.

27 (6) “Acquire” shall include any transfer, whether or not for
28 consideration.

29 (7) (A) For taxable years beginning on or after January 1, 1997,
30 the term “new business” shall include any taxpayer that is engaged
31 in biopharmaceutical activities or other biotechnology activities
32 that are described in Codes 2833 to 2836, inclusive, of the Standard
33 Industrial Classification (SIC) Manual published by the United
34 States Office of Management and Budget, 1987 edition, and as
35 further amended, and that has not received regulatory approval for
36 any product from the United States Food and Drug Administration.

37 (B) For purposes of this paragraph:

38 (i) “Biopharmaceutical activities” means those activities that
39 use organisms or materials derived from organisms, and their
40 cellular, subcellular, or molecular components, in order to provide

1 pharmaceutical products for human or animal therapeutics and
2 diagnostics. Biopharmaceutical activities make use of living
3 organisms to make commercial products, as opposed to
4 pharmaceutical activities that make use of chemical compounds
5 to produce commercial products.

6 (ii) “Other biotechnology activities” means activities consisting
7 of the application of recombinant DNA technology to produce
8 commercial products, as well as activities regarding pharmaceutical
9 delivery systems designed to provide a measure of control over
10 the rate, duration, and site of pharmaceutical delivery.

11 (h) For purposes of corporations whose net income is determined
12 under Chapter 17 (commencing with Section 25101), Section
13 25108 shall apply to each of the following:

14 (1) The amount of net operating loss incurred in any taxable
15 year that may be carried forward to another taxable year.

16 (2) The amount of any loss carry forward that may be deducted
17 in any taxable year.

18 (i) The provisions of Section 172(b)(1)(D) of the Internal
19 Revenue Code, relating to bad debt losses of commercial banks,
20 shall not be applicable.

21 (j) The Franchise Tax Board may prescribe appropriate
22 regulations to carry out the purposes of this section, including any
23 regulations necessary to prevent the avoidance of the purposes of
24 this section through split-ups, shell corporations, partnerships,
25 tiered ownership structures, or otherwise.

26 (k) The Franchise Tax Board may reclassify any net operating
27 loss carryover determined under either paragraph (2) or (3) of
28 subdivision (b) as a net operating loss carryover under paragraph
29 (1) of subdivision (b) upon a showing that the reclassification is
30 necessary to prevent evasion of the purposes of this section.

31 (l) Except as otherwise provided, the amendments made by
32 Chapter 107 of the Statutes of 2000 shall apply to net operating
33 losses for taxable years beginning on or after January 1, 2000.

34 ~~SEC. 5.~~

35 *SEC. 9.* Section 24416.21 of the Revenue and Taxation Code
36 is amended to read:

37 24416.21. (a) Notwithstanding Sections 24416, 24416.1,
38 24416.2, 24416.4, 24416.5, 24416.6, 24416.7, and 24416.20 of
39 this code and Section 172 of the Internal Revenue Code, no net

operating loss deduction shall be allowed for any taxable year beginning on or after January 1, 2008, and before January 1, 2012.

(b) For any net operating loss or carryover of a net operating loss for which a deduction is denied by subdivision (a), the carryover period under Section 172 of the Internal Revenue Code shall be extended as follows:

(1) By one year, for losses incurred in taxable years beginning on or after January 1, 2010, and before January 1, 2011.

(2) By two years, for losses incurred in taxable years beginning on or after January 1, 2009, and before January 1, 2010.

(3) By three years, for losses incurred in taxable years beginning on or after January 1, 2008, and before January 1, 2009.

(4) By four years, for losses incurred in taxable years beginning before January 1, 2008.

(c) The disallowance of any net operating loss deduction for any taxable year beginning on or after January 1, 2008, and before January 1, 2010, pursuant to subdivision (a) shall not apply to a taxpayer with income subject to tax under this part of less than five hundred thousand dollars (\$500,000) for the taxable year.

(d) (1) The disallowance of any net operating loss deduction for any taxable year beginning on or after January 1, 2010, and before January 1, 2012, pursuant to subdivision (a) shall not apply to a taxpayer with preapportioned income of less than three hundred thousand dollars (\$300,000) for the taxable year.

(2) For purposes of this subdivision, "preapportioned income" means net income after state adjustments, before the application of the apportionment and allocation provisions of this part.

(3) For taxpayers that are required to be included in a combined report under Section 25101 or authorized to be included in a combined report under Section 25101.15, the amount prescribed in paragraph (1) shall apply to the aggregate amount of preapportioned income for all members included in a combined report.

(e) Notwithstanding subdivision (a), this section shall not apply to a taxpayer that ceased to do business or has a final taxable year ending prior to August 28, 2008, that sold or transferred substantially all of its assets resulting in a gain on sale during a taxable year ending prior to August 28, 2008, for which the gain could be offset with existing net operating loss deductions and the sale or transfer occurred pursuant to a plan of reorganization under

Chapter 11 of Title 11 of the United States Code. An amended tax return claiming net operating loss deductions allowed pursuant to this subdivision shall be treated as a timely filed original return.

(f) The Legislature finds and declares that the addition of subdivision (e) to this section by the act adding this subdivision fulfills a statewide public purpose by providing necessary tax relief for a taxpayer that ceased to do business or has a final taxable year ending prior to August 28, 2008, that sold or transferred substantially all of its assets resulting in a gain or sale during a taxable year prior to August 28, 2008, for which the gain could be offset with existing net operating loss deductions and the sale or transfer occurred pursuant to a plan of reorganization under Chapter 11 of Title 11 of the United States Code, in order to ensure that these taxpayers are not permanently denied the net operating loss deduction.

~~SEC. 6.~~

SEC. 10. Section 24416.22 of the Revenue and Taxation Code is amended to read:

24416.22. Notwithstanding Section 24416.1, 24416.2, 24416.4, 24416.5, 24416.6, or 24416.7 to the contrary, a net operating loss attributable to a taxable year beginning on or after January 1, 2008, shall be a net operating carryover to each of the 20 taxable years following the year of the loss.

~~SEC. 7.~~

SEC. 11. This act provides for a tax levy within the meaning of Article IV of the Constitution and shall go into immediate effect.