

AMENDED IN ASSEMBLY SEPTEMBER 10, 1999

AMENDED IN ASSEMBLY SEPTEMBER 10, 1999

AMENDED IN ASSEMBLY JULY 7, 1999

AMENDED IN SENATE MAY 28, 1999

AMENDED IN SENATE APRIL 29, 1999

AMENDED IN SENATE APRIL 14, 1999

AMENDED IN SENATE APRIL 6, 1999

SENATE BILL

No. 1038

Introduced by Senator Burton

February 26, 1999

An act to amend Section 15700 of, ~~and to add Sections 15606.7 and 15705 to,~~ the Government Code, and to amend Section 23040.1 of the Revenue and Taxation Code, relating to taxation.

LEGISLATIVE COUNSEL'S DIGEST

SB 1038, as amended, Burton. FTB membership: partnership investment income: ~~regulations.~~

The Bank and Corporation Tax Law provides that income from sources in this state is generally taxable. The law exempts from taxation the distributive share of interest, dividends, and gains from the sale or exchange of qualifying investment securities derived by a corporation that is a partner in a partnership that qualifies as an investment partnership, if the income from the partnership is the only income of the

corporation derived from sources in this state. This exemption does not apply if the corporation participates in the management of investment activities or is engaged in a unitary business with another corporation that meets specified qualifications.

This bill would provide that the exemption shall also apply to income, gain, or loss from stocks or securities received by an alien corporation whose sole activities in this state involve trading in those stocks or securities for the corporation’s own account, with specified exceptions.

Existing law provides that the Franchise Tax Board consists of the State Controller, the Director of Finance, and the Chairman of the State Board of Equalization, ~~and specifies the regulatory authority of the State Board of Equalization and the Franchise Tax Board.~~

This bill would add the Treasurer and a public member to the Franchise Tax Board. The bill would provide for the Chair of the Franchise Tax Board to be selected on a rotating basis. ~~This bill would also revise the regulatory authority of the State Board of Equalization and Franchise Tax Board.~~

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

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

1 ~~SECTION 1. Section 15606.7 is added to the~~
 2 ~~Government Code, to read:~~
 3 ~~15606.7. In addition to any other procedural~~
 4 ~~requirement related to the adoption of regulations, the~~
 5 ~~State Board of Equalization may not adopt a regulation~~
 6 ~~sooner than 30 days after notification in writing of the~~
 7 ~~necessity therefor, including the specific statutory~~
 8 ~~authority for its adoption, to the chairperson of the~~
 9 ~~committee in each house of the Legislature that considers~~
 10 ~~revenue and taxation, the chairpersons in each house that~~
 11 ~~consider appropriations, the chairpersons of the~~
 12 ~~committees, and the appropriate subcommittees, in each~~
 13 ~~house that consider the State Budget, and the~~
 14 ~~Chairperson of the Joint Legislative Budget Committee.~~



1 ~~With regard to the proposed regulation, the~~
2 ~~notification shall include an estimate prepared by the~~
3 ~~Director of Finance of the net effect on state revenues of~~
4 ~~the proposed regulation. The Director of Finance shall~~
5 ~~indicate in that notification whether the net effect on~~
6 ~~state revenues was identified or contemplated by the~~
7 ~~Department of Finance at the time the Legislature~~
8 ~~passed the bill that added or last amended the specific~~
9 ~~statute authorizing the regulation. If the Director of~~
10 ~~Finance estimates that the net increase or decrease in~~
11 ~~state revenues resulting from the proposed regulation,~~
12 ~~that had not been so identified or contemplated as~~
13 ~~described in the previous sentence, will exceed one~~
14 ~~million dollars (\$1,000,000) in the current or any of the~~
15 ~~three subsequent fiscal years, it shall be deemed that the~~
16 ~~proposed regulation goes substantially beyond necessary~~
17 ~~statutory interpretation and that regulation may not be~~
18 ~~adopted by the board.~~

19 ~~SEC. 2.—~~

20 *SECTION 1.* Section 15700 of the Government Code
21 is amended to read:

22 15700. There is in the state government, in the
23 Agriculture and Services Agency, a Franchise Tax Board
24 consisting of the State Controller, the Director of
25 Finance, the Chairman of the State Board of
26 Equalization, the Treasurer, and one public member
27 appointed by the Governor and confirmed by the Senate.
28 The public member shall receive a per diem of one
29 hundred dollars (\$100) for each day actually spent in the
30 discharge of official duties and shall be reimbursed for
31 traveling and other expenses necessarily incurred in the
32 performance of official duties. Commencing with the
33 2000 calendar year, the Chair of the Franchise Tax Board
34 shall be rotated on an annual basis in a manner that
35 ensures that no chair shall serve as the chair for more than
36 one consecutive calendar year at a time. The Franchise
37 Tax Board is the successor to, and is vested with, all of the
38 duties, powers, purposes, responsibilities, and jurisdiction
39 of the Franchise Tax Commissioner, but the statutes and
40 laws under which that office existed and all laws



1 prescribing the duties, powers, purposes, responsibilities
2 and jurisdiction of that office, together with all lawful
3 rules and regulations established thereunder, are
4 expressly continued in force. “Franchise Tax
5 Commissioner” when used in any statute, law, rule or
6 regulation now in force, or that may hereafter be enacted
7 or adopted, means the Franchise Tax Board. No action to
8 which the Franchise Tax Commissioner is a party shall
9 abate by reason hereof but shall continue in the name of
10 the Franchise Tax Board, and the Franchise Tax Board
11 shall be substituted for the Franchise Tax Commissioner
12 by the court wherein the action is pending. The
13 substitution shall not in any way affect the rights of the
14 parties to the action.

15 Notwithstanding any other provision of the law to the
16 contrary, any directive or regulation adopted by the
17 Franchise Tax Board shall take precedence over any
18 directive or regulation adopted by its executive officer.

19 ~~SEC. 3. Section 15705 is added to the Government~~
20 ~~Code, to read:~~

21 ~~15705. In addition to any other procedural~~
22 ~~requirement related to the adoption of regulations, the~~
23 ~~Franchise Tax Board may not adopt a regulation sooner~~
24 ~~than 30 days after notification in writing of the necessity~~
25 ~~therefor, including the specific statutory authority for its~~
26 ~~adoption, to the chairperson of the committee in each~~
27 ~~house of the Legislature that considers revenue and~~
28 ~~taxation, the chairpersons in each house that consider~~
29 ~~appropriations, the chairpersons of the committees, and~~
30 ~~the appropriate subcommittees, in each house of the~~
31 ~~Legislature that consider the State Budget, and the~~
32 ~~Chairperson of the Joint Legislative Budget Committee.~~

33 ~~With regard to the proposed regulation, the~~
34 ~~notification shall include an estimate prepared by the~~
35 ~~Director of Finance of the net effect on state revenues of~~
36 ~~the proposed regulation. The Director of Finance shall~~
37 ~~indicate in that notification whether the net effect on~~
38 ~~state revenues was identified or contemplated by the~~
39 ~~Department of Finance at the time the Legislature~~
40 ~~passed the bill that added or last amended the specific~~



1 ~~statute authorizing the regulation. If the Director of~~
2 ~~Finance estimates that the net increase or decrease in~~
3 ~~state revenues resulting from the proposed regulation,~~
4 ~~that had not been so identified or contemplated as~~
5 ~~described in the previous sentence, will exceed one~~
6 ~~million dollars (\$1,000,000) in the current or any of the~~
7 ~~three subsequent fiscal years, it shall be deemed that the~~
8 ~~proposed regulation goes substantially beyond necessary~~
9 ~~statutory interpretation and that regulation may not be~~
10 ~~adopted by the board.~~

11 ~~SEC. 4.—~~

12 *SEC. 2.* Section 23040.1 of the Revenue and Taxation
13 Code is amended to read:

14 23040.1. (a) Notwithstanding Sections 23040 and
15 25101, income derived from or attributable to sources
16 within this state shall not include:

17 (1) The distributive share of interest, dividends, and
18 gains from the sale or exchange of qualifying investment
19 securities derived by a corporation that is a partner in a
20 partnership that qualifies as an investment partnership
21 under Section 17955, whether or not the partnership has
22 a usual place of business in this state, if the income from
23 the partnership is the corporation's only income derived
24 from or attributable to sources within this state.

25 (2) Income, gain, or loss from stocks or securities
26 received by an alien corporation whose sole activities in
27 this state involve trading in those stocks or securities for
28 the corporation's own account within the meaning of
29 Section 864(b)(2)(A)(ii) of the Internal Revenue Code,
30 whether the trading is done by the corporation or its
31 employees or through a resident broker, commission
32 agent, custodian, or other agent, and whether or not any
33 such employee or agent has discretionary authority to
34 make decisions in effecting the transactions. This
35 paragraph shall not apply in the case of a dealer in stocks
36 or securities.

37 (b) (1) Paragraph (1) of subdivision (a) shall not
38 apply to a corporation that participates in the
39 management of the investment activities of the
40 investment partnership or that is engaged in a unitary



1 business with another corporation or partnership that
2 participates in the management of the investment
3 activities of the partnership or has income derived from
4 or attributable to sources within this state other than
5 income described in paragraph (1) of subdivision (a).

6 (2) Paragraph (2) of subdivision (a) shall not apply to
7 an alien corporation that itself has, or that is engaged in
8 a unitary business with another corporation that has,
9 income derived from or attributable to sources within this
10 state other than income described in paragraph (2) of
11 subdivision (a).

12 (c) An alien corporation (other than a dealer in stocks
13 or securities) trading in stocks or securities for its own
14 account, as described in paragraph (2) of subdivision (a),
15 is not doing business in this state for purposes of Chapter
16 2 of this part.

17 (d) For purposes of this section:

18 (1) "Alien corporation" means a corporation
19 organized under the laws of a country, or any political
20 subdivision thereof, other than the United States.

21 (2) "Dealer in stocks or securities" means a dealer in
22 stocks or securities for purposes of Section
23 864(b)(2)(A)(ii) of the Internal Revenue Code.

24 (3) "Investment partnership" means a partnership
25 that meets both of the following requirements:

26 (A) No less than 90 percent of the partnership's cost of
27 its total assets consist of qualifying investment securities,
28 deposits at banks or other financial institutions, and office
29 space and equipment reasonably necessary to carry on its
30 activities as an investment partnership.

31 (B) No less than 90 percent of its gross income consists
32 of interest, dividends, and gains from the sale or exchange
33 of qualifying investment securities.

34 (4) (A) "Qualifying investment securities" include all
35 of the following:

36 (i) Common stock, including preferred or debt
37 securities convertible into common stock, and preferred
38 stock.

39 (ii) Bonds, debentures, and other debt securities.



1 (iii) Foreign and domestic currency deposits or
2 equivalents and securities convertible into foreign
3 securities.

4 (iv) Mortgage- or asset-backed securities secured by
5 federal, state, or local governmental agencies.

6 (v) Repurchase agreements and loan participations.

7 (vi) Foreign currency exchange contracts and
8 forward and futures contracts on foreign currencies.

9 (vii) Stock and bond index securities and futures
10 contracts, and other similar financial securities and
11 futures contracts on those securities.

12 (viii) Options for the purchase or sale of any of the
13 securities, currencies, contracts, or financial instruments
14 described in clauses (i) to (vii), inclusive.

15 (ix) Regulated futures contracts.

16 (B) “Qualifying investment securities” does not
17 include an interest in a partnership unless that
18 partnership is itself an investment partnership.

19 (5) “Stocks or securities” has the same meaning as
20 applies to that phrase as used in Section 864(b)(2)(A)(ii)
21 of the Internal Revenue Code.

22 (e) The amendments made to this section by the act
23 adding this subdivision shall apply to income years
24 beginning on or after January 1, 1999.

