

**ASSEMBLY BILL**

**No. 2998**

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**Introduced by Assembly Member Frommer**

February 24, 2006

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An act to amend Sections 24307 and 24451 of the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.

LEGISLATIVE COUNSEL'S DIGEST

AB 2998, as introduced, Frommer. The Corporation Tax Law: cancellation of indebtedness: limitations on net operating losses and tax credits.

The Corporation Tax Law, in modified conformity with the federal income tax laws, limits the amount of net operating losses (NOLs) and tax credits, acquired by a corporate taxpayer from other corporations, that may be used by the taxpayer each year in calculating its taxable income apportioned to California, as provided.

This bill would specify that the amount of NOLs and tax credits acquired by a corporate taxpayer from other corporations, as a result of the acquisition of those corporations by the taxpayer, must be calculated by multiplying the amount of NOLs or tax credits allowable to the taxpayer for federal income tax purposes, after applying the federal limitation rules, by the average apportionment percentage of the acquired corporation for the year of the acquisition and the 2 immediately preceding taxable years.

The Corporation Tax Law, in conformity with, and by reference to, specified federal statutes, requires a borrower to include in its income the amount of debt canceled or discharged; however, it allows a corporate taxpayer, instead of including that amount in its income, to reduce the taxpayer's tax attributes, such as net operating losses, tax

credits, capital losses, and depreciable basis of property, that could otherwise have been used by the taxpayer to reduce its tax liability in the future, as provided.

This bill would require the apportionment and allocation rules to apply for purposes of determining the amount of tax attributes that a taxpayer is required to reduce, as provided.

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:*

1 SECTION 1. Section 24307 of the Revenue and Taxation  
2 Code is amended to read:

3 24307. (a) Section 108 of the Internal Revenue Code,  
4 relating to income from discharge of indebtedness, shall apply,  
5 except as otherwise provided.

6 (b) (1) Section 108(b)(2)(B) of the Internal Revenue Code,  
7 relating to general business credit, is modified by substituting  
8 “this part” in lieu of “Section 38 (relating to general business  
9 credit).”

10 (e)  
11 (2) Section 108(b)(2)(G) of the Internal Revenue Code,  
12 relating to foreign tax credit carryovers, shall not apply.

13 (d)  
14 (3) Section 108(b)(3)(B) of the Internal Revenue Code,  
15 relating to credit carryover reduction, is modified by substituting  
16 “11.1 cents” in lieu of “33 1/3 cents” in each place in which it  
17 appears. In the case where more than one credit is allowable  
18 under this part, the credits shall be reduced on a pro rata basis.

19 (4) (A) *Except as provided in paragraph (2), for purposes of*  
20 *reducing tax attributes under Section 108(b) of the Internal*  
21 *Revenue Code, as modified by this section, the amount excluded*  
22 *from gross income shall be the amount determined after the*  
23 *application of the apportionment and allocation provisions of*  
24 *Article 2 (commencing with Section 25120) of Chapter 17.*

25 (B) *For purposes of reducing the basis of property pursuant to*  
26 *Section 108(b)(2)(E) of the Internal Revenue Code, the amount*  
27 *excluded from gross income shall not be reduced by the*  
28 *application of the apportionment and allocation provisions of*

1 Article 2 (commencing with Section 25120) of Chapter 17, if  
2 income from discharge of indebtedness is business income or  
3 nonbusiness income allocable to this state.

4 (5) (A) If a taxpayer makes an election, for federal income tax  
5 purposes, under Section 108(b)(5) of the Internal Revenue Code,  
6 relating to the reduction of tax attributes against depreciable  
7 property, a separate election shall not be allowed under  
8 paragraph (3) of subdivision (e) of Section 23051.5 and the  
9 federal election shall be binding for purposes of this part.

10 (B) If a taxpayer has not made an election for federal income  
11 tax purposes under Section 108(b)(5) of the Internal Revenue  
12 Code, then the taxpayer shall not be allowed to make that  
13 election for purposes of this part.

14 (6) In lieu of the order of reduction of tax attributes prescribed  
15 by Section 108(b) of the Internal Revenue Code, the reduction in  
16 tax attributes shall be made in the following order:

17 (A) To the extent the basis of property of a taxpayer is reduced  
18 for federal tax purposes by application of Section 108(b)(2)(E),  
19 the basis of that property shall be reduced by the same amount  
20 for purposes of this part.

21 (B) The reduction in tax attributes required by Section  
22 108(b)(1) of the Internal Revenue Code shall be made as  
23 described in Sections 108(b)(2)(A), 108(b)(2)(B), as modified by  
24 this section, Section 108(b)(2)(C), and Section 108(b)(2)(D) of  
25 the Internal Revenue Code, in the order prescribed therein.

26 (C) Any amount remaining after the application of  
27 subparagraphs (A) and (B) shall be applied to reduce the basis of  
28 property in accordance with Section 108(b)(2)(E) of the Internal  
29 Revenue Code. To the extent an amount remaining after the  
30 application of subparagraphs (A) and (B) consists of an amount  
31 from the discharge of indebtedness that would give rise to  
32 business income, that amount shall be increased to an amount  
33 determined by dividing that amount by the fraction determined  
34 under Section 25128 for apportioning business income to this  
35 state.

36 ~~(e)~~

37 (7) Section 108(g)(3)(B) of the Internal Revenue Code,  
38 relating to adjusted tax attributes, is modified by substituting  
39 “\$9” in lieu of “\$3.”

40 ~~(f)~~

1 (c) (1) The amendments to Section 108 of the Internal  
2 Revenue Code made by Section 13150 of the Revenue  
3 Reconciliation Act of 1993 (Public Law 103-66), relating to  
4 exclusion from gross income for income from discharge of  
5 qualified real property business indebtedness, shall apply to  
6 discharges occurring on or after January 1, 1996, in taxable years  
7 beginning on or after January 1, 1996.

8 (2) If a taxpayer makes an election for federal income tax  
9 purposes under Section 108(c) of the Internal Revenue Code,  
10 relating to treatment of discharge of qualified real property  
11 business indebtedness, a separate election shall not be allowed  
12 under paragraph (3) of subdivision (e) of Section 23051.5 and the  
13 federal election shall be binding for purposes of this part.

14 (3) If a taxpayer has not made an election for federal income  
15 tax purposes under Section 108(c) of the Internal Revenue Code,  
16 relating to treatment of discharge of qualified real property  
17 business indebtedness, then the taxpayer shall not be allowed to  
18 make that election for purposes of this part.

19 ~~(g)~~

20 (d) The amendments to Section 108 of the Internal Revenue  
21 Code made by Section 13226 of the Revenue Reconciliation Act  
22 of 1993 (Public Law 103-66), relating to modifications of  
23 discharge of indebtedness provisions, shall apply to discharges  
24 occurring on or after January 1, 1996, in taxable years beginning  
25 on or after January 1, 1996.

26 ~~(h)~~

27 (e) The amendments made to Section 108(d)(7)(A) of the  
28 Internal Revenue Code, relating to certain provisions to be  
29 applied at the corporate level by Section 402 of the Job Creation  
30 and Worker Assistance Act of 2002 (Public Law 107-147), shall  
31 apply to discharges of indebtedness after December 31, 2001, in  
32 taxable years ending after that date. This subdivision shall not  
33 apply to any discharge of indebtedness made before March 1,  
34 2002, pursuant to a plan of reorganization filed with a bankruptcy  
35 court on or before October 11, 2001.

36 SEC. 2. Section 24451 of the Revenue and Taxation Code is  
37 amended to read:

38 24451. (a) Subchapter C of Chapter 1 of Subtitle A of the  
39 Internal Revenue Code, relating to corporate distributions and  
40 adjustments, shall apply, except as otherwise provided.

1     **(b) (1)** *The allocation and apportionment provisions of Article*  
2 *2 (commencing with Section 25120) of Chapter 17 shall apply to*  
3 *any adjustment required to be made under Sections 382 and 383*  
4 *of the Internal Revenue Code.*

5     **(2)** *The limitations described in Sections 382 and 383 of the*  
6 *Internal Revenue Code shall be determined by applying the*  
7 *average apportionment percentage, utilizing the proper*  
8 *apportionment formula, as described in paragraph (1), of the*  
9 *acquired corporation for the year of acquisition and the two*  
10 *immediately preceding taxable years, if applicable.*

11     **SEC. 3.** This act provides for a tax levy within the meaning of  
12 Article IV of the Constitution and shall go into immediate effect.

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