

California's Proposition 39 Mandates Use of Single-Sales Factor

By Michael J. Cataldo

Proposition 39 was passed by 60.1 percent of the California electorate on the November 6th, 2012 statewide ballot. As a result, most multistate businesses must apportion income to California using a single-sales factor method of apportionment for taxable years beginning on or after January 1, 2013.

In general, an apportioning trade or business must use a three-factor method of apportionment based on property, payroll, and double-weighted sales.¹ For taxable years beginning on or after January 1, 2011, an apportioning trade or business other than a financial, extractive or agricultural business may make an annual election to use a single-sales factor method of apportionment.² However, for taxable years beginning on or after January 1, 2013, Proposition 39 (1) eliminates this election and (2) mandates the use of the single-sales factor method of apportionment for most businesses.³

Mandatory Market-Based Sourcing

For taxable years beginning on or after January 1, 2011, but before January 1, 2013, taxpayers electing to use the single-sales factor method of apportionment must use market-based rules to source sales of other than tangible personal property for sales factor purposes.⁴ Taxpayers that either do not elect or are not eligible to elect to use the single-sales factor method of apportionment during these years must source such sales to the location where the income-producing activity occurs, based on costs of performance.⁵ For taxable years beginning on or after January 1, 2013, Proposition 39 requires the use of market-based sourcing rules for sales of other than tangible personal property for all taxpayers, including financial, extractive and agricultural businesses.⁶

¹ Section 25128(a). All statutory references are to the California Revenue and Taxation Code.

² Section 25128.5.

³ Section 25128.7. Financial, extractive, and agricultural businesses must apply an equally-weighted three-factor apportionment formula based on property, payroll, and sales. See Section 25128(b).

⁴ Section 25136(b).

⁵ Section 25136(a).

⁶ Section 26136. The special sourcing rules set forth in Regulation 25137-4.2 continue to apply to financial businesses except for those provisions relating to costs of performance and throwback sales. See Regulation 25136-2(g)(3)(D). All regulatory references are to Title 18 of the California Code of Regulations.

Special Sourcing Rules for Certain Cable Businesses

Proposition 39 also provides a modified sales factor sourcing rule for certain cable businesses that make at least \$250 million of annual expenditures in California.⁷ In such cases, 50 percent of the gross receipts derived from certain cable services that would otherwise be assigned to California under the market-based sourcing rules for sales of other than tangible personal property are excluded from the sales factor numerator.⁸

If you have any questions about the content of this alert, please contact the Pillsbury attorney with whom you regularly work, or the attorneys below.

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⁷ Section 25136.1.

⁸ Section 25136.1(a)(1).

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