



STATE OF CALIFORNIA  
**FRANCHISE TAX BOARD**  
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October 23, 2001

Chief Counsel Ruling  
 201257

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Re: \*\*\*\*\*

Dear \*\*\*\*\*:

This chief counsel ruling is issued in response to your \*\*\*\*\* request, on behalf of your client, \*\*\*\*\* for \*\* to be able to make an Internal Revenue Code ("IRC") section 59(e) election for California franchise tax purposes when it is not making that same election for federal income tax purposes.

**FACTS**

During the income year ended \*\*\*\*\* a California taxpayer, incurred significant research and experimental expenditures. For federal income tax purposes, \*\* will deduct the research and experimental expenditures pursuant to Internal Revenue Code section 174(a). For California franchise tax purposes, \*\* intends to make a different election (a separate California only election) to capitalize and amortize the research and experimental expenditures over a 10-year period in accordance with Revenue and Taxation Code sections 23051.5, 23400 and 23459 and Internal Revenue Code section 59(e).

**ISSUE**

Can \*\* make an election for California franchise tax purposes to capitalize and amortize research and experimental expenditures over a 10-year period pursuant to Revenue and Taxation Code sections 23051.5, 23400 and 23459 even though it is not making the same election for federal income tax purposes?

## HOLDING

Yes, \*\* can make an election for California franchise tax purposes to capitalize and amortize research and experimental expenditures over a 10-year period pursuant to Revenue and Taxation Code sections 23051.5, 23400 and 23459 assuming that such election is valid and properly made, even though it is not making the same election for federal income tax purposes.

## DISCUSSION

Revenue and Taxation Code section 23051.5(e) states that the following rules apply whenever Part 11, Bank and Corporation Tax Law,<sup>1</sup> allows a taxpayer to make an election:

(1) A proper election filed with the Internal Revenue Service in accordance with the Internal Revenue Code or regulations issued by "the secretary" shall be deemed to be a proper election for purposes of this part, unless otherwise expressly provided in this part or in regulations issued by the Franchise Tax Board.

(2) A copy of that election shall be furnished to the Franchise Tax Board upon request.

(3) To obtain treatment other than that elected for federal purposes, a separate election shall be filed with the Franchise Tax Board at the time and in the manner which may be required by the Franchise Tax Board.

Revenue and Taxation Code section 23400 incorporates by reference Part VI of Subchapter A of Chapter 1 of Subtitle A of the Internal Revenue Code, except as otherwise provided. Included within Part VI of Subchapter A of Chapter 1 of Subtitle A of the Internal Revenue Code is Internal Revenue Code section 59.

Internal Revenue Code section 59(e) allows taxpayers to make an election to deduct certain qualified expenditures ratably over a 10-year period.<sup>2</sup> Expenditures paid or

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<sup>1</sup> The title of Chapter 11 has been amended effective January 1, 2002 to "Corporation Tax Law."

<sup>2</sup> It should be noted that an election under Internal Revenue Code section 59(e) applies for all purposes of the Internal Revenue Code and the Revenue and Taxation Code. Therefore, the election applies not only for the computation of alternative minimum taxable income, but for purposes of computing the regular corporate income or franchise tax.

incurred under Internal Revenue Code section 174(a) are included in the list of qualified expenditures under Internal Revenue Code section 59(e)(2)(B).

Revenue and Taxation Code section 23459(c) modifies section 59(e)(2) of the Internal Revenue Code and states that "[s]ubparagraphs (A), (B), and (C) of Section 59(e)(2) of the Internal Revenue Code, relating to qualified expenditures, are modified . . . ." Paragraphs (c)(1) and (c)(2) of Revenue and Taxation Code section 23459 then set forth modifications for 59(e)(2)(A) and 59(e)(2)(C), but not 59(e)(2)(B). A review of the legislative history of Revenue and Taxation Code section 23459 reveals that former paragraph (c)(2) modified 59(e)(2)(B), but a 1991 amendment to this section deleted that paragraph. The amendment, however, failed to strike out the reference to subparagraph (B) of Internal Revenue Code section 59(e)(2) in the opening sentence of Revenue and Taxation Code section 23459(c). The reason for the amendment was that Revenue and Taxation Code 24365 incorporated by reference Internal Revenue Code section 174 with certain modifications.<sup>3</sup> Previously, the Revenue and Taxation Code had stand-alone provisions pertaining to research and experimental expenditures. The failure of the amendment to strike out the reference to Internal Revenue Code section 59(e)(2)(B) does not have any bearing on this ruling.

FTB Notice 95-1 states that, generally, taxpayers may "make a different election for California purposes than for federal purposes, unless otherwise provided in the RTC [Revenue and Taxation Code] or FTB regulations." There is nothing in the Revenue and Taxation Code or the FTB regulations that overrides the general rules of Revenue and Taxation Code section 23051.5 as it pertains to a separate California election under Revenue and Taxation Code sections 23400 and 23459 and Internal Revenue Code section 59(e) election.

Please be advised that the tax consequences expressed in this letter are applicable to the named taxpayer only and are based upon and limited to the facts submitted. In the event of a change in relevant statutory, judicial, or administrative law, a change in federal interpretation of federal law in cases where our ruling is based upon such interpretation, or a change in the material facts or circumstances relating to your request upon which this ruling is based, this ruling may no longer be applicable. It is your responsibility to be aware of these changes should they occur.

This chief counsel ruling does not address whether an election under Internal Revenue Code section 59(e)(2) is valid under the facts given, nor the time and manner for making such election. This ruling does not address whether this taxpayer has met the

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<sup>3</sup> It should be noted that even though Revenue and Taxation Code section 23459 does not reference Revenue and Taxation Code section 24365 with its modifications to Internal Revenue Code section 174, Revenue and Taxation Code section 23051.5(i) specifies that "[a]ny reference to a specific provision of the Internal Revenue Code shall include modifications of that provision, if any, in this part." Therefore, the modifications contained within Revenue and Taxation Code section 24365 must still be taken into account when applying Revenue and Taxation Code section 23459.

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requirements under Internal Revenue Code section 174 and Revenue and Taxation Code section 24635 in order to make an election under Internal Revenue Code section 59(e)(2). This ruling merely provides that if the election is appropriate and validly made, a different election than what is made for federal income tax purposes is permitted to be made for California franchise tax purposes.

This letter is a legal ruling by the Franchise Tax Board's Chief Counsel within the meaning of Revenue and Taxation Code section 21012, subdivision (a)(1). Please attach a copy of this letter and your request to the back of the appropriate return(s) (if any) when filed or any notices or inquiries which might be issued.

Very truly yours,

Debra S. Petersen  
Tax Counsel IV