

Wright Ford Young & Co.

Certified Public Accountants and Consultants, Inc.

CALIFORNIA SINGLE SALES FACTOR

Dear Clients and Friends:

Beginning with the 2011 tax year, businesses other than those that are primarily engaged in agriculture, extractive business, savings and loans, or banking and financial activities, may make an irrevocable annual election to apportion income to California using a single sales factor apportionment formula.

Prior to 2011, California tax law states that a taxpayer doing business in more than one state must apportion its business income to California by applying an apportionment factor to its net income. The apportionment factor is based on a three-factor formula consisting of property, payroll and sales. Each factor is derived by taking the ratio of the amount in California to the amount everywhere. The sales factor is double weighted, and the sum of all of the ratios is divided by four to determine an average combined ratio or apportionment percentage.

For tax years beginning on or after January 1, 2011, taxpayers may make a California annual irrevocable election to apportion their California business income using the single sales factor or they can continue to use the standard three-factor formula.

For businesses that elect to use a single sales factor apportionment formula, all business income is apportioned to California by multiplying the business income by the sales factor only. The election must be made on a timely filed original return and is irrevocable in the year for which it is made.

The fact that the election is made on an annual basis provides substantial opportunities for both in-state and out-of-state corporations.

So which apportionment formula should you choose?

For example, a California-based company with relatively high payroll and property may be able to substantially reduce its income apportioned to California by using a single sales factor in years they are profitable. For a loss year, it may maximize its loss apportioned to California by electing the standard apportionment formula. The reverse would generally be true for businesses based outside the state which have minimal property and payroll within California but have substantial sales to California.

According to the Franchise Tax Board, the new apportionment rules are expected to make California a more competitive place to do business, especially for businesses with significant out-of-state sales and substantial in-state payroll and property.

Please give us a call if you would like to discuss which method is advantageous for your company.

Very truly yours,

WRIGHT FORD YOUNG & CO.

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