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**Subject: Microsoft Corp. v. Franchise Tax Board; General Motors Corp. v. Franchise Tax Board**

**Date: August 20, 2006**

To Our Clients and Friends:

The California Supreme Court has just decided a pair of cases involving the controversial issue of whether gross or net proceeds from securities/investment transactions are includible in the receipts factor for apportionment purposes. By way of background, taxpayers in various businesses commonly invest excess cash in short-term financial instruments such as United States Treasury obligations and commercial paper issued by corporations. The income generated by the investments generally constitutes business income, and the transactions giving rise to such income are reflected in the receipts factor.

When the excess cash investments are frequent and/or the size of the investments is large, the impact on the receipts factor can be significant (even when the aggregate net profit is small). The impact often turns on whether the receipts factor should include the gross receipts, or only the net gain, from the sale of the excess cash investments (or whether the receipts should be thrown out of the factor entirely).

In Microsoft Corp. v. Franchise Tax Board, Dkt. No. S133343, Aug. 17, 2006, the taxpayer was unable to include the gross amounts received from the redemption of marketable securities at maturity in the receipts factor of the apportionment formula. Although the court acknowledged that the relevant statute called for the inclusion of gross receipts in the apportionment factor, the court also found that the inclusion of the full redemption price of the securities did not fairly reflect business activity in the state.

In General Motors Corp. v. Franchise Tax Board, Dkt. No. S127086, Aug. 17, 2006, the taxpayer was only able to include the interest received from repurchase agreements in the receipts factor of the apportionment formula, since the court viewed the repurchase agreements as analogous to secured loans. The court again acknowledged that the relevant statute provided for the inclusion of gross receipts received from the redemption of marketable securities held to maturity in the apportionment factor.

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If you have any questions or would like a copy of either of these cases, please do not hesitate to contact me.

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