

**OFFICE OF TAX APPEALS
STATE OF CALIFORNIA**

In the Matter of the Appeal of:
A GIRL’S EMPIRE

) OTA Case No. 19105409
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OPINION

Representing the Parties:

For Appellant:

Roland Biegler, CPA

For Respondent:

Paul L. Kim, Tax Counsel
Christopher Casselman, Tax Counsel IV

C. AKIN, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19324, A Girl’s Empire (appellant) appeals actions by Franchise Tax Board (FTB) denying appellant’s claims for refund of \$216, plus applicable interest, for the 2016 taxable year, and \$829, plus applicable interest, for the 2017 taxable year.

Office of Tax Appeals Administrative Law Judges Cheryl L. Akin, Amanda Vassigh, and Keith T. Long held an oral hearing telephonically for this matter in Sacramento, California, on May 28, 2020. At the conclusion of the hearing, the record was closed and this matter was submitted for decision.

ISSUES

1. Whether the late-filing penalty was properly imposed for the 2016 taxable year.
2. Whether appellant owed the \$800 minimum franchise tax for the 2017 taxable year.¹

FACTUAL FINDINGS

1. On December 16, 2016, appellant filed its articles of incorporation with the California Secretary of State (SOS).
2. The SOS took six days to process and approve appellant's articles of incorporation and a certified copy of the articles of incorporation was prepared and first made available for pickup by appellant's corporate officer on December 22, 2016.
3. The Internal Revenue Service (IRS) assigned appellant a federal employer identification number (FEIN) on December 27, 2016.
4. For the tax years at issue, appellant was taxed as a Subchapter S corporation for federal and California income tax purposes.

2016 Taxable Year

5. On October 24, 2018, appellant untimely filed its 2016 Form 100S, S Corporation Franchise or Income Tax Return, reporting \$0 California net income and \$0 total tax for the year. Page 3 of the tax return indicates that appellant incorporated on December 16, 2016, began business in California on January 1, 2017, and had a single shareholder during the 2016 taxable year.
6. FTB subsequently assessed a late-filing penalty of \$216.
7. Appellant paid the balance due and filed a Form 2924 "Reasonable Cause – Business Entity Claim for Refund."
8. FTB denied appellant's claim for refund for the 2016 taxable year and this timely appeal followed.

¹ In addition to the \$800 minimum tax, FTB also assessed an underpayment of estimated tax penalty (estimated tax penalty) of \$29 and interest for the 2017 taxable year. While appellant states that it is appealing "the minimum tax, interest, and penalties," appellant does not present any argument for the abatement of the estimated tax penalty or interest. As such, it is our understanding that appellant is only contesting the estimated tax penalty and interest as they pertain to the minimum tax, such that if it does not owe the minimum tax, it will not owe the estimated tax penalty or interest. Therefore, because we conclude below that appellant is liable for the minimum tax, it is also liable for the estimated tax penalty and interest for the 2017 taxable year.

2017 Taxable Year

9. Appellant filed a timely 2017 Form 100S, S Corporation Franchise or Income Tax Return, reporting \$0 California net income and \$0 total tax for the year. The return was designated as appellant's final return and indicated that appellant dissolved on December 31, 2017.
10. FTB subsequently revised appellant's total tax from \$0 as reported on its 2017 return to \$800 in order to reflect the \$800 minimum franchise tax and assessed an estimated tax penalty of \$29.
11. Appellant subsequently paid the balance due and filed a Form 2924 "Reasonable Cause – Business Entity Claim for Refund."
12. FTB denied appellant's claim for refund for the 2017 taxable year and this timely appeal followed.

SOS Letter Provided During this Appeal

13. Appellant provides a letter from the SOS dated December 5, 2019. In this letter, the SOS states that it "cannot change the date of formation" and explains, in relevant part, that "California Corporations Code section 110(a) provides that upon receipt of any instrument by the [SOS] for filing pursuant to this division, if it conforms to law, it shall be filed by, and in the office of, the [SOS] and the date of filing endorsed thereon. Except for instruments filed pursuant to Section 1502, the date of filing shall be the date the instrument is received by the [SOS] unless the instrument provides that it is to be withheld from filing until a future date . . ." (Emphasis in original.) The letter further notes that because a future filing date was not requested in appellant's articles of incorporation, the date of filing for appellant's articles of incorporation was December 16, 2016, which is the date of receipt of the document by the SOS.

DISCUSSIONIssue 1. Whether the late-filing penalty was properly imposed for the 2016 taxable year.

R&TC section 19172.5(a) imposes a penalty if an S corporation that is required to file a return under R&TC section 18601 for any taxable year fails to file the return at the time prescribed therefor, unless that failure is due to reasonable cause. The penalty is not measured

by the tax amount due but is instead imposed based on the number of shareholders and lateness of the return. For each month the return is late, the penalty is computed by multiplying \$18 times the number of persons who were shareholders in the S corporation during any part of the taxable year, for a maximum of 12 months. (R&TC, §19172.5(a), (b).)

Here, the penalty was computed by multiplying \$18 by appellant's one shareholder, and the maximum of 12 months. For the 2016 taxable year, appellant's tax return was due on or before the 15th day of the third month following the close of appellant's taxable year. (R&TC, § 18601(d)(1).) Appellant neither filed by March 15, 2017, nor did it file within the automatic sixth-month extension period allowed by R&TC section 18604(a) and FTB Notice 2016-04 (Nov. 4, 2016). Instead, appellant filed its return on October 24, 2018, more than 19 months after the original due date. Appellant does not dispute the computation of the penalty or argue that there is reasonable cause for the abatement of the penalty. Instead, appellant asserts that the penalty is improper because it did not have any business operations or a tax liability during the 2016 taxable year. We disagree.

R&TC section 18601(a) provides that every taxpayer subject to the tax imposed by Part 11 (i.e., the Corporation Tax Law), commencing with R&TC section 23001, shall file a return with FTB. Under R&TC section 23151, with the exception of banks and financial corporations, every corporation doing business within the limits of this state and not expressly exempted from taxation by the provisions of the Constitution of this state or this part, shall annually pay to the state, for the privilege of exercising its corporate franchises within this state, a tax according to or measured by its net income. For purposes of the franchise tax imposed by R&TC section 23151, a corporation is "doing business" in California if, among other things, it is organized in the state. (R&TC, § 23101(b)(1).) Appellant was organized in this state during the 2016 taxable year because it filed its articles of incorporation with the SOS on December 16, 2016. Because appellant was organized in California during 2016, it was doing business in this state and was required to file a return with FTB for the short period that constitutes its 2016 taxable year in accordance with R&TC sections 18601(a) and 24634(a)(2), (a)(4), and (c). Although appellant was not subject to the minimum franchise tax under R&TC section 23153 for the 2016 taxable year as 2016 was appellant's first taxable year,²

² See R&TC section 23153(f)(1), which provides that every corporation that incorporates or qualifies to do business in California on or after January 1, 2000, shall not be subject to the minimum franchise tax for its first taxable year.

appellant remained subject to the franchise tax calculated by multiplying its state net income by the appropriate tax rate. (See R&TC, §§ 23151(a), 23802(b)(1), 23113.)

While appellant states (and we assume, for purposes of our analysis) that it did not conduct any business operations and did not have any income during the 2016 taxable year and therefore did not have a resulting tax liability based on its net income for this year, R&TC section 18601(a) requires a taxpayer to file a return if the taxpayer is *subject* to the tax imposed by the Corporation Tax Law. Because appellant was *subject* to the franchise tax measured by its net income for the 2016 taxable year, it is immaterial that appellant's ultimate tax liability was zero for that year.

However, as potentially applicable here, R&TC section 23114(a) provides a statutory exception to this rule where the corporation did no business in this state during the taxable year, and the taxable year was 15 days or less. If these requirements are satisfied, R&TC section 23114(a) provides that the corporation shall not be “subject” to the taxes imposed by this chapter (i.e., Chapter 2, which imposes the corporation franchise tax). Because the corporation is not *subject* to the franchise tax if the requirements of R&TC section 23114(a) are met, the corporation would not have a filing requirement under R&TC section 18601(a) and thus would not be subject to the late-filing penalty under R&TC section 19172.5(a).

Appellant asserts that the provisions of R&TC section 23114(a) should apply to its 2016 taxable year. Appellant notes that even though it filed its articles of incorporation with the SOS on December 16, 2016, the SOS took six days to process the form before returning it to the corporate officer on December 22, 2016. Appellant contends that because it did not conduct any business operations during the 2016 taxable year and because the 2016 taxable year was less than 15 days from the date its corporate officer received the approved articles of incorporation back from the SOS on December 22, 2016, it meets the requirements of R&TC section 23114(a) and therefore was not subject to tax or required to file a return for its 2016 taxable year.³

Appellant further explains that prior to 2010, the SOS completed and approved articles of incorporation within one hour; however, beginning on January 1, 2010, the SOS began charging for expedited services and SOS approval of articles of incorporation can now take seven to

³ FTB does not argue, and we therefore do not consider, whether appellant failed to meet R&TC section 23114(a)'s requirement that the corporation “did no business in the state during the taxable year” as a result of its incorporation in California during the 2016 taxable year and the interplay of the bright-line “doing business” rule provided in R&TC section 23101(b)(1). As such, we only address whether appellant's taxable year was 15 days or less.

10 days to process without expedited service. During the busiest time of year, appellant asserts that SOS approval of articles of incorporation can sometimes take up to a month. Appellant contends that while it used to be true that if you filed on December 16, you received the approved articles of incorporation that same day, this is no longer the case. Appellant further asserts that this is problematic for California corporations because filing the articles of incorporation is only the first step for these corporations. Appellant states that a corporation needs the approved articles of incorporation in order to do the following chronological steps: first, it must request a FEIN from the IRS; second, it must have the approved articles of incorporation and a FEIN from the IRS to open a bank account; and lastly, it needs a bank account in order to obtain a California resale license from the California Department of Tax and Fee Administration. Appellant notes that because it planned to sell apparel, it needed a resale license before it could become operational. Given these many organizational steps, appellant asserts that its 2016 taxable year should be deemed to start on the date its corporate officer received the approved articles of incorporation back from the SOS (i.e., December 22, 2016), not on the date the articles of incorporation were delivered to the SOS (i.e., December 16, 2016).

While we understand appellant's argument and the many steps a corporation must undertake before it can become fully operational, both the starting date of appellant's corporate existence and the filing date of the appellant's articles of incorporation are controlled and governed by the California Corporations Code (Cal. Corp. Code). Cal. Corp. Code section 200(c) provides that a corporation's corporate existence begins upon the filing of the articles of incorporation. (See also *Appeal of Edward M. Ornitz & Co., Inc.* (50-SBE-006) 1950 WL 332 [the privilege of exercising a corporate franchise begins on the date that the taxpayer files its articles of incorporation].) The filing date of a corporation's articles of incorporation is governed by Cal. Corp. Code section 110(a), which provides that upon receipt of any instrument by the SOS for filing pursuant to this division, if it conforms to law, it shall be filed by, and in the office of, the SOS and the date of filing endorsed thereon. Cal. Corp. Code section 110(a) further provides that the date of filing shall be the date the instrument is received by the SOS unless the instrument provides that it is to be withheld from filing until a future date.

The date of filing endorsed on appellant's articles of incorporation is December 16, 2016. This is the date of receipt of the articles of incorporation by the SOS. In its letter dated December 5, 2019, the SOS specifically notes that a future filing date was not requested in

appellant's articles of incorporation and confirms December 16, 2016, as the date of receipt and filing of appellant's articles of incorporation. Because Cal. Corp. Code section 110(a) specifies that the filing date is the date of receipt of the instrument by the SOS, it is inconsequential that appellant and/or its corporate officer did not receive a copy of the approved articles of incorporation back from the SOS until six days later, on December 22, 2016. Further, as appellant's corporate existence began upon the filing of its articles of incorporation on December 16, 2016, appellant's 2016 taxable year also began on this date. (See Cal. Corp. Code, § 200(c); *Appeal of Edward M. Ornitz & Co., Inc.*, *supra*.) This makes appellant's 2016 taxable year 16 days (inclusive of both December 16 and December 31), not 15 days or less as required by R&TC section 23114(a).⁴

Although appellant failed to meet the requirements of R&TC section 23114(a) by a single day, we do not have the authority to extend the applicability of R&TC section 23114(a). Ordinarily, the plain meaning of statutory language is conclusive. (*Appeal of Kishner* (99-SBE-007) 1999 WL 1080250.) The plain language of R&TC section 23114(a) is explicit and does not provide exceptions. Because appellant's taxable year was 16 days, not 15 days or less as required by R&TC section 23114(a), the narrow exception to taxation provided in R&TC section 23114(a) is inapplicable to appellant's 2016 taxable year. Accordingly, appellant had a filing obligation for the 2016 taxable year, and because it undisputedly filed that return late, the late-filing penalty under R&TC section 19172.5 was properly imposed.

Issue 2. Whether appellant owed the \$800 minimum franchise tax for the 2017 taxable year.

R&TC section 23153(a) and (b) provide that every corporation that is incorporated under the laws of this state shall be subject to the minimum franchise tax from the earlier of the date of incorporation, qualification, or commencing to do business within this state, until the effective date of dissolution. For the 2016 and 2017 taxable years, the annual minimum franchise tax was \$800. (R&TC, § 23153(d).) However, R&TC section 23153(f)(1) provides that every corporation that incorporates or qualifies to do business in California on or after January 1, 2000,

⁴ California Code of Regulations, title 18, section 23222 provides a relevant example which notes that no return will be required and no tax will be due where a calendar year corporation files its article of incorporation on December 17 and does no business during the period from December 17 to December 31; however, the example further notes that if the same corporation files its articles of incorporation on December 16, it will be required to file a return and pay tax for the period from December 16 to December 31, regardless of whether it was inactive and received no income during that period.

shall not be subject to the minimum franchise tax for its first taxable year. Appellant asserts that because it was not subject to tax in 2016 as a result of the application of the exception contained in R&TC section 23114(a), the 2017 taxable year was appellant's first taxable year and therefore it was not subject to the minimum tax for its 2017 taxable year pursuant to R&TC section 23153(f)(1).⁵

However, because we find R&TC section 23114(a) to be inapplicable to appellant's 2016 taxable year, the 2016 taxable year was appellant's first taxable year. Thus, the exception to the imposition of minimum franchise tax for a taxpayer's first taxable year provided in R&TC section 23153(f)(1) was applied to appellant's 2016 taxable year and cannot also be applied to appellant's 2017 taxable year.⁶ Because 2017 was appellant's second taxable year and because appellant continued to be incorporated with the SOS in California during the 2017 taxable year, appellant is subject to the \$800 minimum franchise tax for the 2017 taxable year pursuant to R&TC section 23153(a) and (b).

⁵ R&TC section 23114(b) specifically provides that the period of time for which a corporation is not subject to taxes imposed by this chapter as provided in R&TC section 23114(a) may not be considered a taxable year for purposes of R&TC section 23153(f)(1).


⁶ Absent the exception provided in R&TC section 23153(f)(1), appellant would have been subject to the \$800 minimum tax for its 2016 taxable year under R&TC section 23153(a) and (b) since it was incorporated in California during 2016.

HOLDINGS


1. The late-payment penalty was properly imposed for the 2016 taxable year.
2. Appellant owed the \$800 minimum franchise tax for the 2017 taxable year.


DISPOSITION

FTB’s actions denying appellant’s claims for refund for the 2016 and 2017 taxable years are sustained.

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 Cheryl L. Akin
 Administrative Law Judge

We concur:

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 Administrative Law Judge

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 Keith T. Long
 Administrative Law Judge

Date Issued: 7/16/2020