BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
J. BRAMDENSTEIN INVESTMENT CO.)

Appearances:

For Appellant: Mr. H. U. Brandenstein, President, and Mr. R. McCleod, Auditor, of Appellant corporation

For Respondent: Hon. Chas. J. McColgan Franchise Tax Commissioner

O P I N I O N

This is an appeal pursuant to section 25 of the Bank and Corporation Franchise Tax Act (Stats. 1929, Chapter 13, as amended) from the action of the Franchise Tax Commissioner in overruling the protest of J. Brandenstein Investment co., a corporation, to a proposed assessment of additional tax in the amount of $114.01, based upon the return of appellant corporation for the taxable year ended December 31, 1930.

It is contended by appellant that the Commissioner erred in that he disallowed as a deduction from appellant's net income for the year 1930, an item of $241.26 representing a refund of local taxes received during that year but alleged by appellant to have been an outstdnding claim receivable as of January 1, 1928.

Apparently, the item of $241.26 accrued either during, or prior to, the year 1927. If appellant were reporting on the accrual basis, this item unquestionably could not be considered as income for the year 1930, the year in which received, but would be considered as income for the year in which accrued, and consequently, no tax under the Act should be measured thereby since the Act was passed and became effective during the year 1929 and has not at any time provided for imposing a tax measured by income of any year prior to the year 1928. We assume, however, although the point does not definitely appear from the record, that appellant has been reporting on the cash receipts and disbursements basis. Ordinarily, taxpayer reporting on this basis must report items as income in the year received, and not in the year in which they accrue. Application of this rule in the instant case would lead to the conclusion that the item in question should be considered as income for the year 1930, and should be included in the income to be used as a measure for computing a tax on appellant for the year 1931. We are of the opinion, however, that the rule should not be applied in the instant case.

In the appeal of Institute of Musical Education, Ltd.

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(decided by this board on April 21, 1932), we held that a corporation reporting on a cash receipts and disbursements basis could not deduct from income for the year 1929 amounts paid out during that year on account of expenses incurred during years prior to January 1, 1928. In the course of the opinion rendered in the above appeal, we expressed ourselves at page 5 as follows:

> "... it is to be noted that only corporations reporting on a cash receipts and disbursements basis could claim as a deduction amounts for expenses incurred in years prior to January 1, 1928. Corporations reporting on an accrual basis could not deduct amounts paid out subsequent to this time for expenses previously incurred. Such corporations could deduct expenses only when incurred, not when paid. To hold that a corporation reporting on the cash receipts and disbursements basis could deduct amounts paid out after January 1, 1928 for expenses incurred prior thereto, would result in giving a distinct advantage to the cash receipts and disbursements basis of accounting. This, we do not believe was intended. Rather, we believe it was intended that over a period of years, a corporation would be allowed the same deductions for expenses regardless of whether it reported on the cash receipts and disbursements basis or on the accrual basis, the only difference being that under the first mentioned basis, expenses would be deducted when paid, whereas under the second method, they would be deducted when incurred."

If amounts paid out by a corporation after the effective date of the Act on account of expenses incurred prior to January 1, 1928 cannot be deducted from the income of the year in which paid, although the corporation reports on a cash receipts and disbursements basis, then conversely, and for similar reasons, it would seem that amounts received by a corporation after the effective date of the Act but accruing prior to January 1, 1928, should not be considered as income for the year in which received, notwithstanding the fact that the corporation reports on a cash receipts and disbursements basis. Consequently, we hold that the item of $241.26 representing a refund of local taxes received during the year 1930, should not be included in the income of appellant to be used as a measure of a tax on appellant for the year 1931.

Appellant also contends that it is not taxable under the Act for the reason that it is not doing business. It appears that appellant is a closely held corporation, the activities of which are limited to receiving and distributing to its stockholders rental income from propery leased by it. Although there are cases holding that such activities do not constitute "doing business" (see Del Norte Company v. Wilkinson, 28 Fed. (2d) 876, Rose v. Nunnally Investment Company, 22 Fed. (2d) 102), we held in the appeal of Union Oil Associates (decided by this

Board on October 10, 1932) that a corporation was "doing business" within the meaning of the definition of that term contained in the Act, although it engaged in no other activities than the holding of stock in another corporation and receiving and distributing dividends thereon to its stockholders. This decision was relied upon in holding, in the appeals of Killefer Manufacturing Company and Merryman Estate Company (decided by this Board on October 10, 1932), that corporations engaging in activities similar to those engaged in by appellant were "doing business" as that term is defined in the Act. These decisions, we think, are controlling in the instant appeal, and necessitate our holding that the appellant is to be considered under the terms of the Bank and Corporation Franchise Tax Act as a business corporation "doing business" in this state, and, consequently, is required to pay a tax for the privilege of "doing business" during the year 1931, measured by its net income for the next preceding year.

O R D E R

Pursuant to the views expressed in the opinion of the Board on file in this proceeding, and good cause appearing therefor,

IT Is HEREBY ORDERED, ADJUDGED AND DECREED, that the action of the Franchise Tax Commissioner in overruling the protest of J. Brandenstein Investment Company, a corporation, against a proposed assessment of an additional tax in the amount of $114.01, based upon the return of said corporation for the period ended December 31, 1930, be and the same is hereby modified. Said action is reversed insofar as the Commissioner disallowed as a deduction the sum of $241.26 representing a refund of local taxes received during the year 1930. In all other respects, said action is sustained. The correct amount of tax to be assessed to the J. Brandenstein Investment Co. is hereby determined as the amount produced by means of a computation which will include the allowance as a deduction of the above amount in the calculation thereof. The Commissioner is hereby directed to proceed in conformity with this order and to send the said J. Brandenstein Investment Co. a notice of assessments revised in accordance therewith.

Done at Sacramento, California, this 2nd day of February, 1933, by the State Board of Equalization.

R. E. Collins, Chairman
Fred E. Stewart, Member
Jno C. Corbett, Member
H. G. Cattell, Member

Attest: Dixwell L. Pierce, Secretary