

BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal)

of

AMERICAN HOME SUPPLY, INC.

Appearances:

| For | Appellant: | Waldbaum, | Rockower & Company | |
|-----|-------------|-----------|--|-------|
| For | Respondent: | | ack, Chief Counsel Smith, Associate Cou | unsel |

NOINIGN

This appeal is made pursuant to Section 25667 of the Revenue and Tazation Code from the action of the Franchise Tax Board on the protest of American Home Supply, Inc. to a proposed assessment of additional franchise tax in the amount of \$2,382.37 for the income year ended April 30, 1949, taxable year ended April 30, 1950.

Appellant was incorporated in California on November 11, 1947, and commenced doing business in this State about November.29, 1947. It was engaged in selling household furnishings, primarily upon the installment plan. Upon filing its return under the Bank and Corporation Franchise Taz Act for the sim months period ended April 30, 1948, it elected to report its income from installment sales under the deferred or installment basis as provided in Section 19(e) of the Act (now Sections 25291-25295a of the Revenue and Taxation Code), i.e., it included in income that proportion of the payments actually received during the income year which the gross profit realized when payment was completed bore to the total contract price.

As a commencing corporation Appellant's return for the siz months period, as provided in Section 13(c) of the Act (now Section 23222 of the Code), was the basis for its tax for that period. Under that section its return for the income year ended April 30, 1949, was the basis for its tax for that year and also for the taxable year ended April 30, 1950. Since Appellant had reported a loss in each return, however, it paid only the minimum tax for each taxable period. As of April 30, 1949, its unrealized and unreported income from installment sales was \$96,352.16.

During March and April of 1950 Appellant sold its installment accounts and at the close of business on April 30, 1950, it ceased operations. Thereafter Appellant filed a return and paid a tax in the amount of \$75.03 for the year ended April 30, 1950. The return reported sales of \$155,735.91, gross income from sales of \$122,258.60 and a net income from operations of \$1,875.79. Disposition of the balance remaining in the "unrealized profits" from installment sales account was shown as follows:

| Balance - May 1, 1949 | \$ 96,352.16 |
|---|---------------------------------|
| Add - Gross Profit on Reserve for Bad Debts at May 1, 1949 Total | <u>4,055.48</u> \$100,407.64 |
| | |

Disposition

| Bad debt write-off Portion collected | | \$ 3;742.96 51,489.27 |
|---|-------|--------------------------------------|
| Loss on Sale of Accounts ceivable Cancelled Sales | Re- | 29,721.01 15,140.12 |
| Adjustment | Total | <u>314.28</u> \$100,407.64 |

The Franchise Tax Board adjusted Appellant's income for the income year ended April 30, 1949, by including therein the sum of \$92,352.16, the balance remaining as of April 30, 1949, in Appellant's "unrealized profits from installment sales," and issued the proposed assessment of additional tax which'is the subject of this appeal. In computing the proposed assessment the Franchise Tax Board allowed a credit of \$50.03 of the \$75.03 which had been remitted by Appellant with its return for the year ended April 30, 1950, on the ground that Appellant was liable for only the minimum tax of \$25.00 for the period beginning May 1, 1950.

Section 19(e)(5) of the Bank and Corporation Franchise Tax Act (now Sections 25295 and 25295a of the Revenue and Taxation Code, as it read during the period in question, provided in part as follows:

> "(5) Where a bank or corporation elects to report income from the sale or other disposition of property in the manner provided in this subsection and the entire income therefrom has not been reported prior to the year of dissolution or withdrawal of the bank or corporation, or cessation of business by the corporation, the remainder of the income therefrom shall

be included in the computation of the measure of the tax for the last year in which the bank was located or the corporation did business in this State; no abatement shall be allowed under the provisions-of Section 13(k) of this act for any tax measured by such ` income ...

'Cessation of business' as herein used means the failure to do business during an entire taxable year."

Appellant states that, since it continued its business activity through April 30, 1950, the last day of its fiscal year, the cessation of its business occurred in the year following April 30, 1950, according to the terms of the statute. It contends, accordingly, that its last income year is the year ended April 30, 1950, and that under Section 19(e)(5) it properly included all unrealized income from installment sales, not previously reported, in a tax return for that income year.

The Franchise tax is imposed for the privilege of doing business in this State and for any taxable year the tax is measured by the income of the preceding income year (except for commencing corporations). Sections 4(3) and 13(c) of the Bank and Corporation Franchise Tax Act; <u>Spring Valley Co</u>. <u>Ltd.v. Johnson</u>, 7 Cal, App. 2d 258.

Thus, without the application of Section 19(e)(5), the measure of the tax for the last year in which Appellant did business would have been its income for the next preceding income year. As we construe Section 19(e)(5), a corporation which has reported its income from installment sales on a deferred basis, as permitted by Section 19(e), is required, upon cessation of business, to include in the measure of the tax for the last year in which it does business in this State the unreported income from such sales which, except for the operation of Section 19(e), would have been included in the measure of its/either for that year or previous years. As so interpreted Section 19(e)(5) is in accord with and gives effect to Sections 4(3) and 13(c).

Upon the admitted facts, the "last year that the corporation (Appellant) did business in this State" is the year ended April 30, 1950. The "measure of the tax" for that year as provided in Section 13(c), is its income for the year ended April 30, 1949. In the computation of income for the year ended April 30, 1949, however, Section 19(e)(5) requires the inclusion of unreported income from installment sales. We conclude, accordingly, that the action of the Franchise Tax Board must be sustained.

ORDER

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, pursuant to Section 25667 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of American Home Supply, Inc., to a proposed assessment of additional franchise tax in the amount of \$2,382.37 for the income year ended April 30, 1949, be and the same is hereby sustained;

-Done at Sacramento, California, t-his 19th day of May, 1954, by the State Board of Equalization.

Geo. R. Reilly ____, Chairman

Member

Paul R. Leake ____, Member

____Wm. G. Bonelli____, Member /

_____ Robert C. Kirkwood, Member

ATTEST: <u>Dixwell L. Pierce</u>, Secretary