

BEFORE THE STATE BOARD OF EQUALIZATION  
OF THE STATE OF CALIFORNIA

In the Matter of the Appeals of )  
MONTGOMERY WARD & CC., INCORPORATED)

Appearances:

For Appellant: G. R. Richards, Attorney at Law

For Respondent: Israel Rogers, Assistant Counsel

O P I N I O N

These appeals are made pursuant to Section 25667 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protests of Montgomery Ward & Co., Incorporated, against proposed assessments of additional franchise tax in the amounts of \$69,266.69, \$52,228.47, \$42,458.28, \$34,918.55, \$26,802.53, \$34,332.03 and \$40,324.39 for the income years ended January 31, 1951, 1952, 1953, 1954, 1955, 1956 and 1957, respectively.

Appellant, an Illinois corporation with its headquarters in Chicago, conducts a general merchandising business and has stores located in all states except Massachusetts and Delaware. In addition to its retail stores, it operates mail order houses in nine major cities, one of which is in California. Appellant manufactures some products in three factories which it owns, but approximately 98 percent of the goods handled by its outlets are purchased from other manufacturers.

The instant dispute revolves about the treatment of certain merchandise owned by Appellant which had been placed in transit to its California outlets but which had not yet reached this state. This merchandise included goods sent from Appellant's warehouses outside this State and goods shipped directly to California stores from out-of-state manufacturers.

Appellant's operation constitutes a unitary business and it therefore used a formula to determine the amount of net income attributable to California sources for franchise tax purposes. The formula consisted of property, payroll and sales factors. Only the property factor is in question here.

Appellant included merchandise in transit to California at the end of each of the years in question in the computation of the denominator of its property factor. The Franchise Tax Board

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determined that merchandise in transit to California should be assigned to this state for purposes of allocating the income attributable to California sources. Accordingly it included the value of such merchandise in both the numerator and the denominator of Appellant's property factor.

The income years in question were the subject of Federal audits conducted under protection of waivers, executed by Appellant, extending the period during which assessments for deficiencies in Federal income tax could be made. A portion of the assessments on appeal resulted from the adoption of adjustments made to Appellant's unitary business income by the Federal authorities.

The statutory provision governing the allocation of income during the period in question is section 25101 of the Revenue and Taxation Code (Section 24301 during the years 1951 to 1955) which reads in part:

When the income of a taxpayer subject to the tax imposed under this part is derived from or attributable to sources both within and without the State, the tax shall be measured by the net income derived from or attributable to sources within this State. Such income shall be determined by an allocation upon the basis of sales, purchases, expenses of manufacture, pay roll, value and **situs** of tangible property or by reference to any of these or other factors or by such other method of allocation as if fairly calculated to determine the net income derived from or attributable to sources within this State; . . .

Appellant urges that the words "**value and situs** of tangible **property**" limit Respondent's discretion with respect to the use of property as a factor in the allocation of income. It contends that if property is used as a factor, it must be assigned according to its **situs**, as that term is generally understood in property law. This is substantially the same issue decided by us in the Appeal of Ames Harris Neville Co., Cal. St. Bd. of Equal., Nov. 21, 1957, 2 CCH Cal. Tax Cas. Par. 200-753, 2 P-H State & Local Tax Serv. Cal. Par. 13171, wherein we said:

To thus narrow the issue presumes that the assignment to California for purposes of the property factor of property not physically within the State is barred by the statute. A fair reading of the language of Section 10 [now section 25101] of the Act, however, clearly refutes the existence of any such restriction. To the contrary, the Franchise Tax Board is granted broad discretion in determining the proper method of

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allocating income. (El Dorado Oil Works v. McColgan, ... [34 Cal, 2d 731, 737]; Pacific Fruit Express Co. v. McColgan, 67 Cal. App. 2d 93.)

Appellant seeks to distinguish our decision in the Appeal of Ames Harris Neville Co., supra, on the grounds that there the taxpayer was a domestic corporation and that the property there in question was purchased in India and had no contact with any taxing jurisdiction other than California. We do not, however, regard these differences as controlling.

As Respondent points out, once goods have been placed in transit, the economic benefit to be derived from them is most closely connected with the point of destination. For the purposes of allocating income, the point of origin or points along the journey which goods in transit must travel are of little significance, as compared to the place where such **goods** will actually be put in use in the unitary business.

Appellant attempts to draw an analogy between its situation and that of transportation companies, whose transportation equipment is included in the property factor according to the miles traveled within and without the state. The argument is then made that if only a portion of such equipment is assigned to California when it has actually been in this state, there is no logical basis for assigning to California the entire value of merchandise in transit to this state when it has never been here.

Appellant's argument is difficult to follow, since if the analogy existed, consistency would demand apportioning the merchandise on a mileage basis, which Appellant does not advocate. Suffice it to say, however, that we see no relevant analogy between transportation equipment, the very movement of which is the source of income, and Appellant's inventory, which produces income because it is sold and which is moved only to facilitate its sale.

Appellant has not shown by clear and cogent evidence that the application of Respondent's formula is manifestly unreasonable or that it results in extraterritorial values being taxed. Accordingly, the Franchise Tax Board's action must be sustained. (Butler Bros. v. McColgan 315, II. 501, 507 [86 L. Ed. 9913, affirming 17 Cal. 2d 664 [111 P.2d 334].)

As a procedural matter, Appellant contends that the assessments for the income years ended January 31, 1951, 1952 and 1953 and portions of the assessments for later years were barred by the **four year** statute of limitations. Section 25663a of the Revenue and Taxation Code, however, provides that where the taxpayer agrees with the United States Commissioner of Internal

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Revenue for an extension of the period during which deficiencies in Federal income tax may be assessed "the period for mailing notices of proposed deficiency tax for such year shall be ...six months after the date of the expiration of the agreed period for assessing deficiencies in Federal income tax, ..." Appellant argues that this provision is not applicable here because the disputed assessments were not based upon Federal adjustments.

This question was decided by us in the Appeal of RKO Radio Pictures, Inc., Cal. St. Bd. of Equal., Dec. 17, 1957, 2 CCH Cal. Tax Cas. Par. 200-767, 2 P-H State & Local Tax Serv. Cal. Par. 13173. We held that the clear and unambiguous language of Section 25663a would not permit our restricting its application solely to proposed assessments which are based upon adjustments to income made by the Federal authorities.

Appellant contends that our decision is no longer valid in view of the reasoning used by the court to uphold the constitutional validity of Section 25663a in Richfield Oil Corp. v. Franchise Tax Board (1959) 169 Cal. App. 2d 331 [337 P.2d 237]. The court, however, expressly declined to consider the question now before us and did not, therefore, overrule our earlier holding.

It is settled law that where the language of an enactment is clear there is no room or justification for interpretation, (Caminetti v. Pacific Mutual Life Ins. Co., 22 Cal. 2d 344, 353 [139 P.2d 908] cert. denied, 320 U.S. 802 [88 L. Ed. 484]; Riley v. Robbins, 1 Cal. 2d 285, 287 [34 P.2d 715].) Not only is the language of Section 25663a clear by itself; the lack of any intended restriction is emphasized by its relation to Section 26073a, which allows the taxpayer to file a claim for refund, without reservation as to grounds, within the same period that a state assessment may be issued in a case where there has been an extension of time for assessing Federal deficiencies. Together, the sections comprise an uncomplicated Legislative plan to extend the statute of limitations for both the taxpayer and the state regardless of the basis for the assessment or the refund claim.

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, pursuant to Section 25667 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protests of Montgomery Ward & Co., Incorporated, against proposed assessments of additional franchise tax in the amounts of \$69,266.69, \$52,228.47,

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\$42,458.28, \$34,918.55, \$26,802.53, \$34,332.03 and \$40,324.39 for the income years ended January 31, 1951, 1952, 1953, 1954, 1955, 1956 and 1957, respectively, be and the same is hereby sustained.

Done at Sacramento, California this 20th day of March, 1963, by the State Board of Equalization.

John W. Lynch \_\_\_\_\_, Chairman  
Geo. R. Reilly \_\_\_\_\_, Member  
Alan Cranston \_\_\_\_\_, Member  
Paul R. Leake \_\_\_\_\_, Member  
\_\_\_\_\_, Member

ATTEST: Dixwell L. Pierce \_\_\_\_\_, Secretary