

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of }
MODERN BARBER COLLEGES; INC. }

Appearances:

For Appellant: William Pinney and William Conklin,
Attorneys at Law

For Respondent: A. Ben Jacobson, Associate Tax Counsel

O P I N I O N

This appeal is made pursuant to section 25667 of, the Revenue. and Taxation Code from the action of the Franchise Tax Board on the protest of Modern Barber Colleges, Inc., against a proposed assessment of additional franchise tax in the amount of \$3,560.47 for the income year.1959.

The question presented by this appeal is whether appellant's failure to file a timely franchise tax return for the income year 1959 precluded its using the installment method of reporting the gain realized on the sale of its assets in that year.

Appellant, a California corporation, was engaged in operating a barber school in San Francisco. Its president and sole stockholder was E. M. Robinson, now deceased.

On December 12, 1959, appellant sold all its assets for \$65,000, under an installment sale agreement. E. M. Robinson's son was a practicing attorney. He was named escrow holder for the sale and all the corporate assets, including its cash on hand, were turned over to him. He was to transfer the corporate assets to the buyer, receive the payments from the buyer, and pay the existing liabilities of the corporation,, A payment of \$18,000 was received in 1959.

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111 feelings developed between E. M. Robinson and his son subsequent to the sale of the business. In early March 1960, an accountant prepared appellant's California franchise tax and federal income tax returns for the income year 1959 and mailed them to the son, requesting him to write checks on the escrow funds by March 15, 1960, in payment of the 'computed taxes. Though he raised some questions about the accuracy of the returns, the son nevertheless agreed to write the checks and file the returns as requested. On March 15, 1960, the date the tax returns were due, he telephoned his father and told him that he had **changed his mind**, and was not going to file the returns or pay the taxes shown thereon to be due. E. M. Robinson asked him to at least put the returns in the mail that day and, nothing further being heard, assumed that this was done.

The dispute between E. M. Robinson and his son over the business and the escrow resulted in litigation later in 1960. During the latter part of that year respondent mailed several notices to appellant, which stated that no return had been received and demanded the filing of a delinquent return. On January 3, 1961, after settlement of the difficulties which had arisen between father and son, appellant filed a California franchise tax return for the income year 1959. In that return appellant reported its gain from the sale of the business on the installment basis. Respondent denied appellant **the right to use the installment method, treating the entire gain on the sale as taxable in the income year 1959.**

The installment method provides a means whereby a taxpayer may report as income in any one income year a portion only of the total gain realized from an installment sale. (See Rev. & Tax. Code, §§ 24667 and 24668.) It is not disputed that the sale in question meets all the requirements for treatment under the installment method which are set forth in the above-cited sections of the Revenue and Taxation Code and the related regulations. (See Cal. Admin. Code, tit. 18, reg. 25291-25293(a) to 25291-25293(c), inclusive.) Respondent contends, however, that appellant's failure to elect to use the installment method in a timely filed return for the income year 1959 resulted in a forfeiture of its right to report gain from the sale of its property on the installment basis.-

Appellant contends that it at all times acted 'in good faith in its attempts to file a timely tax return with respondent; and that the failure to do so was through no fault of its own but was due to the actions of a recalcitrant escrow holder. Appellant urges that, under these circumstances, the fact that it failed to make its election in a timely filed return was excusable and should not preclude its subsequently reporting the gain realized from the sale of its business on the installment basis.

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Earlier interpretations by the United States Tax Court of federal income tax provisions substantially similar to those sections of the Revenue and Taxation Code with which we are here concerned, did establish the rule that a taxpayer's right to report gain from an installment sale on the installment basis was conditioned on his making an election to do so on a timely filed tax return for the year of sale. (See, e.g., Sarah Briarly, 29 B.T.A. 256; W. T. Thrift, Sr., 15 T.C. 366; W. A. Ireland, 32 T.C. 994.) This strict rule has been changed, however, by more recent decisions of the Tax Court and other federal courts, which have held that where the facts and circumstances of the case warrant a deviation, a taxpayer's failure to make an election in a timely filed return for the year of sale is not fatal to his right to use the installment method of reporting gain.

Some of the cases which have allowed the use of the installment method in spite of the taxpayer's failure to make an election in a timely return for the year of the sale have based their decisions on grounds such as the existence of good faith (Scales v. Commissioner, 211 F.2d 133; United States v. Eversman, 133 F.2d 261; John F. Bayley, 35 T.C. 288), someone's inadvertent omission (Hornberger v. Commissioner, 289 F.2d 602), or an honest error (John P. Reaver, 42 T.C. 72). In 1964 the Court of Appeals for the Fifth Circuit held in Baca v. Commissioner, 326 F.2d 189, that the privilege of installment reporting will not be denied a taxpayer even though he negligently failed to file a timely return for the year of sale. This same position has recently been adopted by the Tax Court in F. E. McGillick Co., 42 T.C. 1059.

Basing our decision upon these most recent authorities, and recognizing the liberalizing trend which is evidenced therein, we conclude that appellant's failure to file a timely franchise tax return for the income year 1959 did not bar it from later utilizing the installment methods of reporting the gain realized from the sale of its business in 1959.

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,

