



BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
SOUTH BAY BOARD OF REALTORS, INC.)

Appearances:

For Appellant: George V. Hall
Attorney at Law

For Respondent: Lawrence M. Counts
Junior 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 protests of South Bay Board of Realtors, Inc., against proposed assessments of additional franchise tax and penalties in the total amounts of \$996.21, \$996.21 and \$2,394.92 for the taxable years 1958 through 1960, respectively, based on income for the years 1958 and 1959. The penalties, which equal 5 percent of the taxes, were imposed for failure to file returns within the due date as extended by the Franchise Tax Board. It is undisputed that the penalties apply if the taxes are due,

The issue is whether, for the years in question, appellant is entitled to be classified as an exempt corporation.

Appellant was incorporated as a nonprofit corporation in 1948. Its members include: (1) Active Class A Members, who are licensed real estate brokers actively engaged in real estate business; (2) Active Class B Members, who are licensed real estate brokers affiliated with an organization having a Class A member; and (3) Salesmen Members, who are associated with Class A members as real estate salesmen,

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Total membership, including categories not mentioned above (affiliate, property owner, **honorary**, and nonresident members) was 545 in 1958, 616 in S-959 and 712 in 1960.

The objectives of appellant include: **uniting** those in the real estate business in order to exert a beneficial influence upon matters affecting that business; providing a unified medium whereby the collective and individual interests of those engaged in the real estate business may be advanced; **promoting** high ethical standards; protecting the welfare of real estate owners; and promoting the objectives of organized real estate men (Appellant's Constitution, Article XI).

Among appellant's activities are: maintaining a multiple listing service; producing a weekly publication for members; indoctrinating new members; regulating, and disciplining members; arbitrating member disputes; maintaining a public **relations** program; and forming other committees to insure professional operation and safeguard the interests of the members and the community.

Appellant has an office and secretarial staff of four **full-time** and two **part-time** employees,

Appellant expressly declared in **its** franchise tax returns filed at respondent's request for the years under consideration that its principal business activity was to "Maintain Office for Realtors Multiple Listings and **Trans-actions.**" It began operation of the multiple listing service in 1949. Pursuant to the **official** written policies of its multiple listing service, the Executive Committee of Multiple Listing, appointed by **appellant's president** with **the** approval of its board of directors, is the governing body of the multiple listing service. Changes in the official written policies of the service may be made by this committee subject to board approval.

The service affords **all** members and **certain** non-members the opportunity to sell property placed on multiple Listing, Exclusive listings of designated property acquired by the listing broker become **exclusive** listings of the service. **Appellant** receives as a fee on multiple listing sales, **.002** per cent of the selling price, After deduction of appellant's fee, the balance of tire sales commission is divided, in the usual instance, 60 percent to the selling broker and 40 percent to **the** listing broker.

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While appellant asserts that the multiple listing service was not intended to make a profit, the following table show that appellant's income resulted largely from the service:

<u>Income Year</u>	<u>1958</u>	<u>%</u>	<u>1959</u>	<u>%</u>
<u>Income :</u>				
Multiple Listing Service	\$47,004.95	68%	\$72,012.89	71%
Other	<u>21,977.48</u>	<u>32%</u>	<u>29,019.48</u>	<u>29%</u>
Total	\$68,982.43	100%	\$101,032.37	100%
<u>Expenses</u>	<u>45,263.21</u>		<u>59,490.10</u>	
Net Income	<u>\$23,719.22</u>		<u>\$ 41,542.27</u>	

Examination of appellant's franchise tax returns discloses that during the years in question its net income accumulated, its cash on hand increasing in an amount approximately equal to its total net income for the two-year period.

Appellant's elective officers include three vice\ presidents, one in charge of multiple listings, one in charge of public relations, and one in charge of ethics and professional standards, The vice president in charge of multiple listings is designated to succeed to appellant's presidency in the event of a vacancy and to fulfill the president's functions in the latter's absence.

Respondent Franchise Tax Board contends that the operation of the multiple listing service deprived appellant of its exempt status. Appellant maintains that this service is an exempt activity because it improves real estate conditions generally. It claims that because of this service, not only is maximum exposure provided to sellers and buyers but this is done within a framework of control to insure professional and ethical representation by agents. Appellant also urges that even if the multiple listing service is not itself an exempt activity it is incidental to exempt purposes*

The relevant statutes provide that business leagues, chambers of commerce, realestate boards, or boards of trade, not organized for profit and no part of the net earnings of

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which inures to the benefit of any individual, are exempt from the franchise tax except for the tax on "unrelated business net income," (Rev. & Tax. Code, §§ 23701, 23701e, 23732.)

Respondent's regulations provide that:

A business league is an association of persons having some common business interest, the purpose of which is to promote such common interest and not to engage in a regular business of a kind ordinarily carried on for profit. It is an organization of the same general class as a chamber of commerce or board of trade. Thus, its activities should be directed to the improvement of business conditions of one *or* more lines of business as distinguished from the performance of particular services for individual persons.... Astock exchange is not a business league ...and is not exempt from tax. (Cal. Admin. Code, tit. 18, reg. 23701e.)

The above provisions are substantially the same as those found in the federal code and regulations. (Xnt. Rev. Code of 1954, § 501(c)(6); Treas. Reg, § 1,501(d)(6)-1.)

Although the above quoted language of the regulation refers only to business leagues it applies to real estate boards as well. (Evanston -North Shore Board of Realtors v. United States, 320 F.2d 375, 377 [footnote], cert. denied, 376 U.S.931 [11L. Ed.2d 650].) In the cited case, a multiple listing service substantially similar to appellant's was held to operate primarily for the benefit of individual realtors rather than for the benefit of the real estate business generally, The court recognized that the interests of the real estate business generally and the interests of the public were benefited by the service because a broader and more active market for real estate resulted under controlled ethical conditions, Nevertheless, the court concluded that the most immediate benefit was to the individual participating realtors,

The court reached its conclusion for a number of reasons that apply also to the case before us, The court pointed out that the fees charged for the listing service were in approximate proportion to the benefits received by each realtor, The court also stated that the listing service was a "sales tool" at the disposal of the individual realtors and

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that there was a -compelling analogy between the operation of a multiple listing service and of a stock or commodity exchange.

The court recognized that if the principal purpose and activity of a real estate board is such as to justify exemption it does not lose its exempt status by engaging in an incidental activity which, standing alone., would be subject to taxation. The court held, however, that the multiple listing service activity was more than incidental and exemption was denied. In that case it was estimated that about 61 percent of the board's gross income was derived from the listing service and that more than half of the board's expenses were attributable to that activity. The court found that an increase in personnel, from one employee to five full-time employees and one part-time employee was largely due to the operation of the listing service. The court commented:

We do not say that financial. data of the type here present is the only relevant criterion of the importance of one of an organization's many activities. But we do hold that the relative contribution to plaintiff's receipts and expenditures of its listing service, and the amount of personnel which the service requires are sufficiently substantial that the listing service cannot be regarded as an incidental activity of the Board.

On the record before us here, there is no basis for holding that the operation of the multiple listing service is incidental. The wide majority of appellant's gross income is derived from the service and there is no evidence that the amount spent for exempt activities exceeded the expense of operating the service. The relative importance of the multiple listing service is evidenced by the relative importance of the officer in charge of it. As contrasted with the vice, presidents in charge of other activities, the vice president in charge of the service is the one designated to act for the president and to succeed him.'

Appellant further contends that if respondent prevails, appellant will be unconstitutionally deprived of property because it was not notified until 1960 that it was required to

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pay franchise tax based on income for the years 1953 and 1959. Appellant has not cited judicial authority in support of its contention of unconstitutionality and we are not aware of any. Moreover, there is reason to believe that appellant knew or should have known, well before the notice from respondent was given, that the operation of the multiple listing service placed its exempt status in jeopardy. The issue had become of sufficient importance by 1959 that the Internal Revenue Service in that year issued a ruling that real estate boards whose primary purpose or activity is the operation of a multiple listing system are not entitled to exemption. (Rev. Rul. 59-234, 1959-2 Cum. Bull. 149.)

We conclude that on the particular facts of this case and for the particular years in question, appellant is not entitled to be classified as an exempt corporation.

ORDER

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

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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 South Bay Board of Realtors, Inc., against proposed assessments of additional franchise tax and penalties in the total amounts of \$996.21, \$996.21 and \$2,392. for the taxable years 1958 through 3.960, respectively, be and the same is hereby sustained.

Done at Sacramento, California, this 21st day of April, 1966, by the State Board of Equalization.

Geo. Kelly, Chairman
Richard Mori, Member
Paul R. Leake, Member
_____, Member
_____, Member

ATTEST: W. H. Brown, Secretary