BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
AMERICAN EMPIRE MUTUAL FUND, INC.)

For Appellant.: Charles W. Cottle
President and Director

For Respondent: Crawford H. Thomas
Chief Counsel

James P. Corn
Counsel

O P I N I O N

This appeal is made pursuant to section 26077 of the Revenue and Taxation Code from the action of the Franchise Tax Board in denying the claim of American Empire Mutual Fund, Inc., for a refund of franchise tax in the amount of $100 for the income and taxable year 1970.

Before proceeding to the merits of this appeal, we must dispose of a procedural question. Appellant American Empire Mutual Fund, Inc., has moved to strike the Franchise Tax Board's supplemental memorandum on the grounds that it is not authorized by section 5027 of title 18 of the California Administrative Code. That section allows the Franchise Tax Board to file "a supplemental memorandum to deny allegations of fact in the reply of the appellant." Appellant's position appears to be that the supplemental memorandum was improper because there were no new allegations of fact in appellant's reply to trigger the operation of section 5027. In the view of appellant, respondent's supplemental memorandum is "a thinly veiled attempt to have the 'last word,'" in contravention of the basic principle of appellate procedure that the appellant is entitled to have the last word on the issues.

We agree that the "last word" belongs to the appellant, and our regulations governing both the filing of written memoranda and the conduct of oral hearings are predicated on that principle. We also agree that the primary purpose for allowing a supplemental memo-. randum by the Franchise Tax Board is to permit it to deny factual allegations. But in the nature of our. proceedings, the supplemental memorandum often must serve as a vehicle for the Franchise Tax Board's response to wholly new arguments raised for the first time in the appellant's reply. Here, appellant specifically raised new issues in its reply memorandum, and the Franchise Tax Board is therefore entitled to comment on those issues in a supplemental memorandum. (Appeal of Woodward Enterprises, Inc., Cal. St. Bd. of Equal., Aug. 4, 1971.) The supplemental memorandum does contain matter (the second paragraph on page 2) not constituting either a denial of factual allegations or comment on the new issues raised in appellant's reply, but a small amount of unnecessary and repetitious argument does not justify striking the entire memorandum from the record. Accordingly, appellant's motion to strike is denied.

On the merits this appeal involves the question whether appellant was liable for the minimum franchise tax (Rev. & Tax. Code, § 23153) in the year of its incorporation.

Appellant is a "diversified management company" registered with the Securities and Exchange Commission pursuant to section 8 of the Investment Company Act of 1940 (15 U.S.C.A. § 80a-8). Appellant filed its articles of incorporation with the California Secretary of State on June 18, 1970, and paid the $100 minimum franchise tax at that time. (Rev. & Tax. Code? § 23221.) On June 19, 1970, appellant filed for exemption from franchise taxes pursuant to Revenue and Taxation Code section 23701m. That section provides such an exemption for "Corporations classified as diversified management companies under Section 5 of the Federal Investment Company Act of 1940, and registered as provided in that act." After appellant registered with the Securities and Exchange Commission on July 1, 1970, respondent Franchise Tax Board granted the exemption to appellant, effective July 1, 1970. On November 17, 1970, appellant filed a claim for refund of the $100 minimum tax. Respondent denied the refund claim and appellant has taken this appeal.

Respondent's position is based on the following provisions contained in--Revenue and Taxation Code section 23153:

> Every corporation not otherwise taxed under this chapter and not expressly exempted by the provisions of this part or the Constitution of this state shall pay annually to the state a tax of one hundred dollars ($100),...
>
> * * *
>
> Every such domestic corporation taxable under this section shall be subject to the said tax from the date of incorporation until the effective date of dissolution as provided in Section 23331.

Respondent contends that the minimum tax applies because for a short period (June 18 to July 1, 1970) subsequent to its incorporation appellant was not exempt under section 23701m. As respondent has interpreted section 23153, the minimum tax is a privilege tax on the mere ownership of a corporate franchise , and 'there is no requirement that the taxpayer be doing business in order to be subject to it. In this respect the operation of section 23153 is to be distinguished from that of section 23151, which impose2 a franchise tax on corporations "doing business" in California .

We believe that the literal language of section 23153 compels the conclusion advanced by respondent, Appellant's reliance on the exemption provided by section 23701m is misplaced, since registration under the Investment Company Act of 1940 is a condition. precedent to the exemption. Appellant was granted the exemption effective the day it registered, but it was not exempt for the few days of its corporate existence prior to registration. We have not been cited to any authority supporting appellant's implicit contention that section 23701m exempts diversified management companies "in the process of registration" as well as those actually "registered" with the Securities and Exchange Commission. Of appellant 's other contentions, we need answer only the one suggesting that section 23153 should not apply because appellant's corporate franchise was essentially a nullity prior to July 1, 1970. The alleged nullity is said to result from the legal restrictions preventing investment companies from doing any inve stment busines s prior to registration. The short answer is that the very act of incorporation invokes the operation of section 23153, regardless of whether extrinsic rules of law may impose sanctions on the immediate doing of business by the corporation.

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 26077 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the claim of American Empire Mutual Fund, Inc., for refund of franchise tax in the amount of $100 for the income and taxable year 1970, be and the same is hereby sustained.

Done at Sacramento, California, this 11th day of May, 1972, by the State Board of Equalization.

John W. Lynch, Chairman

[signature], Member

[signature], Member

[signature], Member

, Member

ATTEST: [signature], Secretary