BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
THE WESTERN PACIFIC RAILROAD)
COMPANY AND AFFILIATED COMPANIES)

Appearances:

For Appellant: Louis A., Starr
Tax Manager

For Respondent: A. Ben Jacobson
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 The Western Pacific Railroad Company and Affiliated Companies against proposed assessments of additional franchise tax in the amounts of $35,667.58, $12,726.54, $23,219.79, and $12,939.27 for the income years 1962, 1963, 1964, and 1965, respectively.

The question presented is whether the gains and losses appellant Western Pacific realized from several sales of unimproved real estate constitute unitary or nonunitary income. This issue relates entirely to the years 1962 and 1963. The additional assessments for 1964 and 1965 have been conceded by appellant.

Appellant is a California corporation which has its head office and commercial domicile in this state. In conjunction with several wholly owned subsidiaries, it is engaged in a unitary railroad business. From time to time appellant and its subsidiaries make sales of land which they own. Several such sales made during 1962 and 1963 are the subject of this appeal.

In 1962 four parcels of land in San Francisco were sold for a total gain of $1,155,502, and one parcel in Reno, Nevada, was sold at a gain of $7,922. In 1963 a large bloc of waterfront property in Oakland, California, was sold at a loss of $386,256, and a small parcel of land in Yuba City, California, was sold at a gain of $18,612. Respondent determined that these gains and losses were nonunitary and allocated each gain and loss to the state in which the land giving rise to it was located. Appellant's position is that the gains and losses were unitary income subject to formula apportionment among the various states in which the unitary railroad business was conducted.

Respondent contends that gain or loss from the sale of property is unitary or nonunitary depending on whether the property was used in the unitary business operation up to the time of sale. In respondent's opinion the properties in question were not so used in the unitary business. Consequently, respondent concluded that the gains and the loss were nonunitary. Appellant contends that they should be treated as unitary because the sales were made to present or prospective shippers in order to promote and increase rail traffic for the benefit of the unitary business.

The test used by respondent is supported by regulation 25101, subdivision (d)(1), of title 18 of the California Administrative Code, which provides in part:

> Income from property, which is not a part of or connected with the unitary business, is excluded from the income of the unitary business which is allocated by formula.

It is also supported by our prior decisions. (Appeal of Chris-Craft Industries, Inc., Cal St. Bd. of Equal., March 26, 1968; Appeal of American President Lines, Ltd., Cal. St, Bd. of Equal,, Jan. 5,1961.) In Chris-Craft we held that the gain from the sale of a parcel of California real estate was nonunitary, and therefore allocable in full to California, because the land had never become a part of the unitary business and had never contributed to the unitary income. We believe that Chris-Craft controls the present appeal. The record clearly establishes that the properties in question were not being used in the unitary business at the times they were sold. And it also appears that they were never employed in the unitary business, although some or all of them may have been acquired with the intent to use them in the railroad business.

We cannot agree with appellant that, because it intended to benefit the rail business by making the sales, the income therefrom was unitary income. In Chris-Craft we held that income from the sale of property acquired for a specific unitary purpose was not unitary income because the property had never, in fact, been put to a unitary use. We see no reason why the motive behind the sale of such property should have any greater impact on the character of the gain or loss thereby realized, The Appeal of American Snuff Co., decided by us on April 20, 1960, does not require a different result since it did not involve a sale of property, In addition, the income-producing assets which we-re involved in that case -- loans to the taxpayer's employees -- were actually used in the unitary business.

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 protest of The Western Pacific Railroad Company and Affiliated Companies against proposed assessments of additional franchise tax in the amounts of $35,667.58, $12,726.54, $23,219.79, and $12,989.27 for the income years 1962, 1963, 1964, and 1965, respectively, be and the same is hereby sustained,

Done at Sacramento, California, this 31st day of July, 1972, by the State Board of Equalization.

_____, Chairman

_____, Member

_____, Member

_____, Member

_____, Member

ATTEST: _____, Secretary