BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
ATLAS ACCEPTANCE CORPORATION)

Appearances:

For Appellant: Robert H. Solomon
Attorney at Law

For Respondent: Claudia K. Land
Counsel

O P I N ION

This appeal is made pursuant to section 25666 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Atlas Acceptance Corporation against proposed assessments of additional franchise tax in the amounts of $4,699.40 and $3,141.12 for the income years 1974 and 1975, respectively.

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The question presented by this appeal is whether the Franchise Tax Board (hereinafter referred to as "respondent") properly classified appellant as a financial corporation within the meaning of section 23183 of the Revenue and Taxation Code, thereby making it taxable at the rate applicable to banks and financial corporations, rather than at the lesser rate applicable to general corporations.

Appellant, a California corporation located in Dublin, California, was incorporated on July 1, 1971. Its articles of incorporation state, in pertinent part:

> (a) THE SPECIFIC BUSINESS IN WHICH THE CORPORATION IS PRIMARILY TO ENGAGE IS: Purchasing at a discount membership contracts generated by health spa operations, the factoring of accounts receivable, and similar financing transactions.

Appellant purchases health spa membership contracts in an amount equal to 70 percent of their face value, including interest charges. The accounts are unsecured and, typically, are turned over to appellant for collection within a very short period of time. Appellant is furnished lists of contracts by health spas and runs credit checks upon their clientele. On the basis of these credit checks, appellant determines which health spa membership contracts to purchase. The contracts are purchased without recourse against the health spa operators.

In 1974, appellant reported $1,305,945 in receivables; $90,532 was charged against the reserve for bad debts. In 1975, $1,179,017 in receivables was reported, and $61,357 was charged against the bad debt reserve. For the years indicated below, appellant's gross income, derived from its purchase of health spa membership contracts, was as follows:

	Income Years Ended		
Source	12/31/74	12/31/75	Total
Gross Receipts	$452,727	$384,827	$837,554
Interest	6,717	12,428	19,145
Late Charges and Collection Fees	23,127	32,214	55,341
	$482,571	$429,469	$912,040

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In computing its California franchise tax liability for the years inquestion, appellant used the rate applicable to general corporations. Respondent determined that appellant was a financial corporation and, therefore, was taxable at the same rate as banks. Appellant protested the resulting proposed assessments of additional tax issued by respondent, and respondent's denial of that protest gave rise to this appeal.

The "financial corporation" classification (Rev. & Tax. Code, § 23183 et seq.) was created by the Legislature to comply with the federal statute (12 U.S.C.A. § 548) prohibiting discrimination between national banks and other financial corporations. (Crown Finance Corp. v. McColgan, 23 Cal.2d 280 [144 P.2d 331] (1943); Marble Mortgage Co. v. Franchise Tax Board, 241 Cal.App.2d 26 [50 Cal.Rptr. 345] (1966).) While the term is not defined in the statute, the courts have developed a two-part test which must be met before a corporation may be classified as a financial corporation under section 23183: (i) it must deal in money or moneyed capital as distinguished from other commodities (The Morris Plan Co. v. Johnson, 37 Cal.App.2d 621 [100 P.2d 493] (1540); and (ii) it must be in substantial competition with national banks. (Crown Finance Corp. v. McColgan, supra.) Respondent's determination that a corporation is a financial corporation is presumed correct, and the burden is upon appellant to show that it is not a financial corporation. (Appeals of The Diners' Club, Inc., Cal. St. Bd. of Equal., Sept. 1, 1967; Todd v. McColgan, 89 Cal.App.2d 509 [201 P.2d 414] (1949).)

In the instant appeal, since appellant concedes that it is dealing in money, this board is only called upon to determine if appellant's business is in substantial competition with national banks. If appellant's operations are found to constitute substantial competition with national banks, then we are required to sustain respondent's determination that appellant is a financial corporation taxable at the same rate applicable to banks.

Appellant argues that banks are unwilling to purchase health spa contracts, with or without recourse against health spa owners, because of the tenuous financial status of health spas generally and because of problems in enforcing and collecting on the contracts. We are satisfied with the showing of appellant that, in fact, California national banks have a general policy

against purchasing membership contracts from health spas. This determination, however, is not dispositive in ascertaining whether appellant's business operations place it in substantial competition with national banks.

It is not necessary to find that national banks would engage in precisely the same transactions as appellant in order to find that appellant is in substantial competition with national banks. Competition may arise from the employment of capital invested by individuals or institutions in those classes of investments engaged in by national banks, (First Nat. Bank v. Louisiana Tax Commission, 289 U.S. 60 [77 L.Ed. 1030] (1933); First Nat. Bank v. Hartford, 273 U.S. 548 [71 L.Ed. 767] (1927); Minnesota v. First Nat. Bank, 273 U.S. 561 [71 L.Ed. 774] (1927).) After a careful review of the record on appeal, and for the specific reasons set forth below, we conclude that appellant is involved in substantial competition with national banks and that respondent's action in this matter must be sustained.

Whenever capital is employed either by a business or by private investors in the same type of transactions as those in which national banks engage and in the same locality in which they do business, those businesses or private investors are acting in competition with national banks. (See First Nat. Bank v. Louisiana Tax Commission, supra; First Nat. Bank v. Hartford, supra.) One such type or class of investment in which national banks engage is the business of discounting commercial paper. (Talbott v. Silver Bow County Commissioners, 139 U.S. 438 [35 L.Ed. 2101 (1891); First Nat. Bank v. Anderson, 269 U.S. 341 [70 L.Ed. 295] (1926).) While appellant, as noted above, argues that it is not in competition with national banks because such, banks, within the locality of appellant's operations, have a policy against discounting the precise sort of commercial paper which appellant discounts, it is undisputed that appellant is involved in an activity engaged in by national banks (i.e., the discounting of commercial paper). In order to establish competition, it is not necessary to show that national banks and competing investors solicit the same customers for the same loans or investments. It is sufficient if both engage in seeking and securing, in the same locality, capital investments of the class now under consideration which are substantial in amount. (First Nat. Bank v. Hartford, supra.) Accordingly, since appellant is involved in the business of discounting

commercial paper, an activity engaged in by national banks, we must find that appellant is in competition with national banks. That appellant's operations were significant enough to find that it was in substantial competition with national banks is evidenced by the fact that, in both of the years in issue, it purchased more than one million dollars in health spa membership contracts.

Appellant relies heavily upon the decision of this board in Appeals of Arc Investment Co., decided February 18, 1964, to support its position that it is not in competition with national banks. In that appeal, it was decided that the taxpayer, a corporation in the business of purchasing contracts similar to those in question here, was not a financial corporation in substantial competition with national banks. In that case, respondent conceded that the taxpayer purchased a particular type of commercial paper not purchased by any national bank', but nevertheless argued that the taxpayer was in competition with such banks because it was engaged in the "field" of making unsecured loans, an activity engaged in by national banks. To support its conclusion that the taxpayer was in competition with national banks, respondent cited only Crown Finance Corp. . McColgan, supra. No mention was made of the United States Supreme Court decisions in First Nat. Bank v. Hartford, supra, and Minnesota v. First Nat. Bank, supra. As we observed in Appeals of Arc Investment Co., Crown Finance Corp. did not require a finding that Arc Investment Co. was in competition with national banks because it was dealing with a class of persons none of whom had sufficiently high credit standings to interest such banks. However, the above cited United States Supreme Court decisions stand for the proposition that it is not necessary to show that national banks and competing investors solicit the same customers for the same loans or investments, but merely that competing investors make the same type of investments made by national banks, e.g., the discounting of commercial paper. Thus, by focusing on the lack of competition with respect to the particular type of commercial paper purchased by Arc Investment Co., as opposed to commercial paper generally, the opinion in Appeals of Arc Investment Co. was in error.

For the reasons stated above, we will sustain respondent's determination that appellant is taxable as a financial corporation.

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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 Atlas Acceptance Corporation against proposed assessments of additional franchise tax in the amounts of $4,699.40 and $3,141.12 for the income years 1974 and 1975, respectively, be and the same is hereby sustained.

Done at Sacramento, California, this 29th day Of July , 1980, by the State Board of Equalization, with Board Members Mr. Dronenburg, Mr. Reilly, Mr. Bennett and Mr. Nevins present.

Ernest J. Dronenburg, Jr., Chairman

George R. Reilly, Member

William M. Bennett, Member

Richard Nevins, Member

, Member