

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeals of)
JOHN AND DOLORES LACEY, AND ELIZABETH LACEY }

For Appellants: Curtis Darling
Attorney at Law

For Respondent: Carl G. Knopke
Counsel

O P I N I O N

These appeals are made pursuant to section 18593 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of John and Dolores Lacey against a proposed assessment of additional personal income tax in the amount of \$12,481.82 for the year 1975, and on the protest of Elizabeth Lacey against a-proposed assessment of additional personal income tax in the amount of \$5,987.57 for the year 1975.

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The issue presented by this appeal is whether appellants' distributive shares of partnership income were properly included in their California taxable income for 1975.

Appellants are partners in a family partnership which owned and operated a ranch in Montana. The partnership sold the ranch operations on August 15, 1975. At that time, appellants were residents of Montana. On October 1, 1975, they moved to California as full-time residents. The partnership is on a calendar year; its 1975 taxable year ended on December 31, 1975, after appellants became California residents.

On their California personal income tax returns for 1975, appellants reported their distributive shares of only those partnership items of income and deductions which accrued after appellants became California residents. Upon audit respondent determined that appellants' distributive shares of the partnership's gains and losses should have been included in their California income. It issued proposed assessments reflecting this determination. After considering appellants' protests, respondent affirmed the proposed assessments, and these appeals followed. We note that the gain on the sale of the partnership assets located in Montana was taxed by that state on a source basis. California, which taxed the **gain** on the basis of appellants' residency, has allowed a tax credit for the taxes paid to Montana.

Appellants' argument is that only the items of income and deductions which accrued to the partnership after appellants became California residents should be included in their 1975 California taxable income on the basis of section 17596 of the Revenue and Taxation Code. **That** section states:

When the status of a taxpayer changes from resident to nonresident, or from nonresident to resident, there shall be included in determining income from sources within or without this State, as the case may be, income and deductions accrued prior to the change of status even though not otherwise **includible** in respect of the period prior to such change, **but the taxation** or deduction of items accrued prior to the change of status shall not be affected by the change.

Our initial inquiry must be whether section **17596** is applicable to this appeal;

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This board has recently examined the purpose of section 17596 and limited its application. (Appeal of Virgil M. and Jeanne P. Money, Cal. St. Bd. of Equal., Dec. 13, 1983.) We concluded that "section 17596 was designed merely to prevent California from treating accrual and cash basis taxpayers differently when they changed residency and were subject to taxation by California on the basis of their residency." In light of this limited purpose, we held that section 17596 applies only when two conditions are met: (1) when California's only basis for taxation is the taxpayer's residency, and (2) when California's taxation would differ depending on whether the taxpayer used the accrual or cash method of accounting.

With regard to appellants' partnership income, only the first condition is satisfied. The second condition is not satisfied since section 17861 of the Revenue and Taxation Code, which **sets** forth when a partner's distributive share of partnership income is included in the partner's taxable income, makes no distinction between cash and accrual basis taxpayers and treats all taxpayers **identically**. Since a specific statute treats all partners as if they are on the same method of accounting, we need **not use** section 17596 to obtain the same outcome. (Appeal of Virgil M. and Jeanne P. Money, supra.)

Under California law, a partner's distributive share of partnership income **or loss** is fixed at the end of the partnership's taxable year and includes all of the partnership's **items** of income and deductions for that taxable year. (Rev. & Tax. Code, § 17861; Appeal of Jerald L. and Joan Ratleman, Cal. St. Bd. of Equal., Dec. 15, 1976; see also Estate of Levine, 72 T.C. 780 (1979) affd., 634 F.2d 12 (2d Cir. 1980).) In the instant appeal, the partnership's taxable year ended December 31, 1975. Therefore, appellants' entire distributive shares of the partnership's 1975 income are **includible** in computing appellants' 1975 taxable income.

For the foregoing reasons, respondent's action must be sustained.

