



Appeal of Stanley K. and Beatrice L. Wong

The issue for determination is whether certain interest and dividend income received by appellants was from Hawaiian sources, entitling them to a credit against their California personal income tax for taxes paid on those amounts to Hawaii.

Appellants, who were born in Hawaii, are domiciliaries and residents of California. In 1969 they purchased a condominium unit located in Hawaii as a rental property. The unit was sold in 1970, and appellants elected to use the installment method of reporting their gain on the transaction. Appellants' attorney in Honolulu **had been** their rental agent and also handled the details of the sale of the condominium, pursuant to a power of attorney which they had executed. The attorney in Honolulu retained possession of the buyer's installment note, collected the Payments of principal and interest, and **forwarded** the **proceeds** to appellants in California.

Appellants paid Hawaiian income tax on both the capital gain and interest portions of each installment, treating them as income from Hawaiian sources. As California residents, appellants also paid tax to California on the same amounts and claimed a credit against their California tax for the tax paid to Hawaii. Respondent disallowed the credit for taxes paid to Hawaii on the interest portion of the installment payments.

During 1972 appellants also received dividend income from stock which they owned in Leong Brothers, **Ltd.**, a closely held family corporation with its headquarters in Honolulu. The stock certificates were held in the name of Mrs. Wong at the corporate offices in Honolulu, and, presumably, the dividends were mailed to her in California. Appellants reported the dividends as income from Hawaiian sources and paid income taxes on them to both Hawaii and California. Respondent disallowed the credit which appellants claimed against their California tax for the tax paid to Hawaii on the dividend income.

Under certain circumstances, a credit for net income taxes paid by residents of California to other states is authorized by section 18001 of the Revenue and Taxation Code. That section limits the availability of the credit as follows:

- (a) The credit shall be allowed only for taxes paid to the other state on income derived from sources within that state. ... (Emphasis added.)

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It is respondent's position that both the interest portion of the installment payments and the dividend income received by appellants constituted income from intangible property which had its source at the residence of the owner of the property, under the rule of mobilia sequuntur personam. Since appellants were domiciliaries and residents of California, respondent concluded the interest and dividend income was derived from California sources and no credit was allowable for income taxes paid to Hawaii.

Appellants, on the other hand, contend that the intangibles in question had acquired a business situs in Hawaii. In support of this contention they argue that the condominium was business property located in Hawaii prior to its sale, and that the interest received in connection with that sale retained its business characteristics throughout the term of the installment contract. They also point out that the installment note itself remained in Hawaii in the hands of their attorney who was authorized to act on their behalf. Appellants also contend that the stock certificates were physically located in Hawaii and were associated with the operation of the family corporation.

The issue presented in this appeal is controlled by the California Supreme Court's decision in Miller v. McColgan, 17 Cal. 2d 432 [110 P.2d 4191 (1941)]. (See also Christman v. Franchise Tax Board, 64 Cal. App. 3d 751 [134 Cal. Rptr. 725] (1976); Appeal of Hallie L. Bills, Cal. St. Bd. of Equal., April 5, 1965; Appeal of Anne Bachrach, Cal. St. Bd. of Equal., July 22, 1958.) The question before the court in Miller was whether a credit was allowable for a Philippine income tax paid on dividends and gains received by a California resident from his stock in a corporation located in the Philippine Islands. In applying the predecessor of section 18001, the court determined that no credit was available. The reasoning of the court was that the dividends and gains had their source in the stock itself, and that the situs of the stock was the residence of its owner. In reaching this conclusion the court applied the common law doctrine often followed in determining the taxable situs of intangible assets, mobilia sequuntur personam, meaning "movables follow the person." We have consistently followed the view set forth in Miller v. McColgan. (See, e.g., Appeal of John K. and Patricia J. Withers, Cal. St. Bd. of Equal., Sept. 1 1966; Appeal of Hugh S. and Nina J. Livie, Cal. St. Bd. of Equal., Oct. 28, 1964.)

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The business **situs** exception to the mobilieria rule, urged by appellants as controlling in this appeal, was recognized in the Miller case. In order to establish a business **situs**, however, the intangibles must be so tied in with the business activities of the owner in the foreign state that they have become integral parts of the local business. (See Southern Pacific Co. v. McColgan, 68 Cal. App. 2d 48, 71-72 [156 P.2d 81] (1945); see also Appeal of Anne Bachrach, supra.)

In support of their position, appellants first argue that the condominium was a business property located in Hawaii prior to its sale, and that the interest received in connection with that sale retained its business characteristics throughout the term of the installment contract. This argument has been rejected previously in the Appeal of Hallie L. Bills, supra, where we held that the immediate source of interest income on a debt is the debt itself. Since the debt instrument is an intangible asset with its **situs** at the residence of its owner, the creditor, the interest has its source at the same place under the mobilieria rule.

Next, relying on Appeal of Estate of Douglas C. Alexander, Deceased, decided by this board, January 4, 1966, appellants argue that the installment note remained in Hawaii in the hands of their attorney, a fiduciary authorized to act on their behalf pursuant to a power of attorney. We do not find appellants' argument persuasive. The mere fact that the physical evidence of the intangible remained in Hawaii is not sufficient to create a business **situs**. (See Miller v. McColgan, supra.) Furthermore, the Alexander appeal is distinguishable. In Alexander we refused to apply the mobilieria rule to intangibles held in trust by a trustee who had legal title, possession and control of the securities in question, and held that the **situs** of the securities was at the residence of the trustee, not the beneficiary. Here, although appellants' attorney was a fiduciary, he was merely their agent, not a trustee. (Warner Bros. Records, Inc. v. Golden West Music Sales, 36 Cal. App. 3d 1012 [112 Cal. Rptr. 71] (1974), New York v. New, 148 Cal. App. 2d 372 [306 P.2d 987] (1957).)

Finally, in their attempt to establish a Hawaiian business **situs**, appellants allege that the stock certificates, which were physically located in Honolulu, were associated with the operation of the family corporation. With reference to this argument, it is sufficient

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to point out that appellants have offered absolutely no evidence to support this allegation. Accordingly, their argument must be rejected.

We conclude that the interest and dividend income received by appellants was from a California source. Therefore, they were not entitled to a credit against their California tax for taxes paid to Hawaii on those amounts.

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 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of Stanley K. and Beatrice L. Wong against a proposed assessment of additional personal income tax in the amount of \$110.73 for the year 1972, be and the same is hereby sustained.

Done at Sacramento, California, this 4th day of May , 1978, by the State Board of Equalization.

Geoff Peilly , Chairman  
Paul Lee , Member  
Iris Sawyer , Member  
Sullivan B. B... Member  
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