BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of) No. 85A-0455-DB
CHRISTIE ELECTRIC CORP.)

Appearances:

For Appellant: Robert C. Summers
Attorney at Law

For Respondent: Karl F. Munz
Counsel

O P I N I O N

This appeal is made pursuant to section 25666[1] of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Christie Electric Corp. against proposed assessments of additional franchise tax in the amounts of $10,417, $8,967, and $4,898 for the income years ended February 28, 1978, February 28, 1979, and February 29, 1980, respectively.

1/ Unless otherwise specified, all section references are to sections of the Revenue and Taxation Code as in effect for the income years in issue.

The question presented is whether, in computing the sales factor of appellant's apportionment formula, respondent Franchise Tax Board properly applied the "throw back" rule to appellant's sales in foreign countries.

Appellant manufactures and sells electrical products and equipment and does business both within and without California. During the appeal years, appellant apportioned its income among the various states in which it did business, using the standard three-factor apportionment formula. On each return, appellant excluded from the numerator of its sales factor all sales made to customers located in foreign countries. In auditing the returns, respondent determined that appellant was not taxable in any of the foreign countries, and it therefore "threw back" the sales to California and increased the numerator of appellant's sales factor accordingly. Appellant protested the resulting deficiency assessments, contending that, under our decision in the Appeal of Dresser Industries, Inc., originially decided by this board on June 29, 1982, and affirmed on denial of petition for rehearing on October 26, 1983, its foreign sales should have been assigned to their foreign destinations because appellant was taxable in all of those countries.

A taxpayer which derives income from sources both within and without California is required to measure its franchise tax liability by its net income derived from or attributable to California sources in accordance with the Uniform Division of Income for Tax Purposes Act (UDITPA) contained in sections 25120-25139. (Rev; & Tax. Code, § 25101.) As required by section 25128, a taxpayer's business income must be apportioned to this state by means of an equally-weighted, three-factor formula composed of the property factor, the payroll factor, and the sales factor.

Section 25134 defines the sales factor as "a fraction, the numerator of which is the total sales of the taxpayer in this state during the income year, and the denominator of which is the total sales of the taxpayer everywhere during the income year." For purposes of determining whether sales of tangible personal property are in this state, section 25135 sets forth the following rules:

Sales of tangible personal property are in this state if:

> (a) The property is delivered or shipped to a purchaser, other than the United States government, within this state regardless of the f.o.b. point or other conditions of the sale: or
>
> (b) The property is shipped from an office, store, warehouse, factory, or other place of storage in this state and (1) the purchaser is the United States government or (2) the taxpayer is not taxable in the state of the purchaser. (Emphasis added.)

The underscored language in subdivision (b) contains the "throw back" rule whose application is at issue in this appeal.

Under UDITPA, the term "state" includes any foreign country (Rev. & Tax. Code, § 25120, subd. (f)), and a taxpayer is "taxable" in another "state" if:

> (a) in that state it is subject to a net income tax, a franchise tax measured by net income, a franchise tax for the privilege of doing business, or a corporate stock tax, or (b) that state has jurisdiction to subject the taxpayer to a net income tax regardless of whether, in fact, the state does or does not. (Emphasis added.)

(Rev. & Code, § 25122.)

The parties agree that the only question is whether any of the foreign countries had jurisdiction to subject appellant to a net income tax, appellant having conceded that it did not actually pay any taxes to the countries in question.

While both parties apparently agree that United States jurisdictional standards, rather than the actual standards of the foreign countries, should be used to determine taxability (see Appeal of Dresser Industries, Inc., supra), appellant's failure to file returns and to pay taxes in any foreign countries does not have the same damaging implications for appellant's position as similar failures to file and pay have in the purely interstate commerce arena, where United States standards of taxability apply in fact as well as in theory. (Cf. Appeal of the Olga Company, Cal. St. Bd. of Equal., June 27, 1984, where we held that the taxpayer's failure to file

returns in states other than California was tantamount to a representation that it was not taxable in those states.). Nevertheless, it is certainly incumbent upon appellant to provide sufficient evidence of its activities to establish taxable nexus in the foreign countries. What appellant must prove is something akin to "continuous local solicitation," (Scripto, Inc. v. Carson, 362 U.S. 207, 211 [4 L.Ed.2d 660] (1960)), or to "a regular and systematic pattern of local sales solicitation" on appellant's behalf in the foreign countries in question. (Appeal of Dresser Industries, Inc., supra.)

With the exception of the documents produced with respect to sales activity in Israel, appellant's evidence falls well short of establishing the required nexus in any foreign country. Appellant has submitted a few documents reflecting sales trips abroad by some of its employees, but these reports contain insufficient data of the requisite sales activity on appellant's behalf in any particular country. In addition, appellant has been unable to substantiate the amount of its sales in any country except Israel. Consequently, even if appellant had taxable nexus in other countries, it would be impossible to determine the quantity of foreign sales properly excludible from the numerator of the sales factor.

For the above reasons, respondent's action in this matter will be sustained, subject to respondent's concession regarding appellant's sales in Israel.

Appeal of Christie Electric Corp.

O R D E R

Pu-rsuant 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 Christie Electric Corp. against proposed assessments of additional franchise tax in the amounts of $10,417, $8,967, and $4,898 for the income years ended February 28, 1978, February 28, 1979, and February 29, 1980, respectively, be and the same is hereby modified in accordance with respondent's concession regarding the sales in Israel. In all other respects, the action of the Franchise Tax Board is sustained.

Done at Sacramento, California, this 18th day of August, 1987, by the State Board of Equalization, with Board Members Mr. Collis, Mr. Dronenburg, Mr. Bennett and Mr. Carpenter present.

Conway H. Collis, Chairman

Ernest J. Dronenburg, Jr., Member

William M. Bennett, Member

Paul Carpenter, Member

_____, Member