

^{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 single issue for determination is whether appellant's property factor can be modified to include appellant's coupon inventory.

During the years in issue, the main offices of appellant Retail Marketing Services, Inc., a California coupon processing corporation, were located in Sacramento, California. Appellant conducted its coupon business within and without California with its subsidiaries Organizacion De Cupones, a Mexican corporation, and R.M.S. Haiti S.A., a Haitian corporation. The coupons in question were issued by various manufacturers of food and other products, and their value to a shopper was in the discount received when redeemed by a participating merchant; a merchant could either submit the coupons to the manufacturer, and receive the value of the coupons in cash, or sell them to appellant, which then collated them and resold them to the respective manufacturer for cash.

Appellant purchased the coupons from independent grocery stores for an average premium of 6.5 cents per coupon, or about 14.5 percent over face value, and resold them to the manufacturer for a price in excess of appellant's cost. The coupons were insured against loss, damage, or destruction by appellant, and were recorded as inventory in appellant's accounting records at a nominal value. (Appeal Ltr. at 2.) Also, during the years in issue, appellant and its subsidiaries filed combined reports on a unitary basis utilizing the standard three-factor formula (sales/property/payroll) to apportion the group's unitary income to California.

Respondent Franchise Tax Board audited the books and records of appellant for the years in issue, and assessed additional taxes, unrelated to this appeal, which appellant paid. Appellant filed amended returns for the years in issue that included the coupon inventory in the numerator and denominator of appellant's property factor; appellant submitted the amended returns during the audit. After several months appellant was advised that respondent would not allow the coupons to be included in the property factor because it considered them to be intangible property. Respondent denied appellant's refund claims, and this timely appeal followed.

The numerator of the property factor is the average value of the taxpayer's real and tangible personal property owned or rented and used in this state during the income year, and the denominator is the average value of all the taxpayer's real and tangible personal property owned or rented and used during the income year. Intangible property is not specifically included in the property factor. (Rev. & Tax. Code, § 25129; see also Appeal of Texaco, Inc., Cal. St. Bd. of Equal., Jan. 11, 1978.)

Respondent's position is that the coupons in question had no inherent value in and of themselves, but only represented a value to a consumer in the amount of the discount which would be eventually exchanged for cash, and as such constituted intangible property. Respondent concluded that "[w]ith limited exceptions, not relevant here, the property factor of the apportionment formula cannot include intangible property." (Resp. Br. at 3.) Appellant's position is that the definition of "tangible" as contained in Funk and Wagnall's Standard College Dictionary (copyright 1963) clearly demonstrates that the coupons in question constituted tangible personal property because they are:

1. Perceptible by touch, also within reach by touch;
2. Capable of being apprehended by the mind; of definite shape; or
3. Perceptible to the senses; corporeal; material.

(Appeal Ltr. at 3.)

Appellant further believes that since the coupons in question have inherent value to the extent of appellant's investment in them, and because they were sold for an amount greater than appellant's investment, the coupons in question are tangible assets. (App. Reply Br. at 6.) We must, therefore, determine whether or not the coupons are in fact tangible personal property; if they are, then the matter ends there. However, if we find that the coupons in question are intangible property, then we must decide if this is a situation where they nevertheless properly belong in the numerator and denominator of appellant's property factor. The parties apparently agree that appellant's payroll and sales factors were properly reported. Therefore, we will limit our discussion to whether appellant's property factors for the years in issue should be modified to include appellant's coupon inventory. Further, it is not disputed by either party that if the coupons in question constitute tangible personal property, they are properly includable in the numerator and denominator of appellant's property factor.

Tangible personal property is not defined in either the Revenue and Taxation Code or the Internal Revenue Code (I.R.C.), and, therefore, we must look to a secondary source for its definition. Appellant is correct that the ordinary and customary meaning of "tangible" is that which can be felt by touch, having actual form and substance. (Webster's Ninth New Collegiate Dict. (1983) p. 1205; see also Black's Law Dict. (5th ed. 1979) p. 1305; Texas Instruments, Inc. v. United States, 551 F.2d 599, 611 (5th Cir. 1977).) However, we must agree with respondent that this definition is much too broad to be used to determine whether the coupons in question constituted tangible personal property. Here, the parties appear to agree that the coupons had no intrinsic value to a consumer apart from the discount received by the consumer upon presentation to the merchant. Thus, the coupons represented a customer's "right" to the discount, and property that is a right rather than a physical object is intangible. (City of Oakland v. Oakland Raiders, 32 Cal.3d 60, 67 [183 Cal.Rptr. 673] (1982).) Further, property is intangible if its intrinsic value is attributable to its intangible elements rather than to any of its specific tangible embodiments. (Texas Instruments, Inc. v. United States, supra, 551 F.2d at 609.) Applying the "intrinsic value" test, we conclude that the intrinsic value of the coupons is attributable to their intangible elements rather than to their tangible embodiments, and thus they are intangible rather than tangible property. (See Ronnen v. Commissioner, 90 T.C. 74, 99-100 (1988).)

We also reject the position urged upon us by appellant that its investment in the coupons, and subsequent resale at an amount greater than its initial investment, has somehow transformed the coupons from intangible to tangible personal property. Had appellant purchased and resold at a greater price a patent right, franchise, or other intangible asset, we fail to see how the

subsequent resale would change the item from an intangible to a tangible asset. Appellant has offered no explanation for why a different result should obtain in the case of its coupons. This matter does not end here, however, because while we conclude that the coupons were intangible property, we must now decide if this is a situation where in order to fairly represent the extent of appellant's business activity in this state, the coupons must be included in appellant's property factor.

Section 25137^{2/} permits a deviation from the statutory apportionment formula when the formula does not fairly represent the extent of a taxpayer's business activity in this state. (See Appeal of Donald M. Drake Company, Cal. St. Bd. of Equal., Feb. 3, 1977; Appeal of New York Football Giants, Inc., Cal. St. Bd. of Equal., Feb. 3, 1977; and Appeal of Lipps, Inc., 87-SBE-017, Mar. 3, 1987.) However, the party who seeks to deviate from the statutory formula bears the burden of proving that exceptional circumstances are present that require a deviation. (Appeal of Merrill, Lynch, Pierce, Fenner & Smith, Inc., 89-SBE-017, June 2, 1989.)

In the instant matter, appellant's sole argument for application of section 25137 is that its "business may be unique and require a separate method for determining an appropriate allocation of income." (Appeal Ltr. at 4.) While we agree that appellant's business may be "unique," the mere uniqueness of a business is not sufficient to establish that the statutory formula does not fairly represent the extent of a taxpayer's business activity in this state, and allow us to depart from use of the statutory formula. In Appeal of Merrill, Lynch, Pierce, Fenner & Smith, Inc., supra, we rejected respondent's argument as unavailing that a deviation under section 25137 was justified because the result was "better" than the result using the statutory formula. We rejected respondent's argument because, in our opinion, what must be shown is that the statutory formula distorts the extent of the taxpayer's business activities in this state. (See, e.g., Appeal of New York Football Giants, Inc., supra; Appeal of Oscar Enterprises, L.T.D., 87-SBE-069, Oct. 6, 1987.) Appellant's argument has not persuaded us that exclusion of the coupons from appellant's property factor distorts the extent of appellant's business activities in this state. Accordingly, appellant has not met its burden of proving that the statutory formula does not fairly represent the extent of appellant's business activities in this state.

^{2/} Section 25137 provides:

If the allocation and apportionment provisions of this act do not fairly represent the extent of the taxpayer's business activity in this state, the taxpayer may petition for or the Franchise Tax Board may require, in respect to all or any part of the taxpayer's business activity, if reasonable:

- (a) Separate accounting;
- (b) The exclusion of any one or more of the factors;
- (c) The inclusion of one or more additional factors which will fairly represent the taxpayer's business activity in this state; or
- (d) The employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

For the above reasons, respondent's action in this matter must be sustained.

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 26077 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the claims of Retail Marketing Services, Inc., for refund of franchise tax in the amounts of \$8,860, \$20,423, \$6,385, and \$3,977 for the income years ended April 30, 1983, April 30, 1984, April 30, 1985, and April 30, 1986, respectively, be and the same is hereby sustained.

Done at Sacramento, California, this 1st day of August, 1991, by the State Board of Equalization, with Board Members Mr. Sherman, Mr. Dronenburg, Mr. Bennett, and Ms. Scott present.

Brad Sherman _____, Chairman

Ernest J. Dronenburg, Jr. _____, Member

William M. Bennett _____, Member

Windie Scott* _____, Member

_____, Member

*For Gray Davis, per Government Code section 7.9
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