

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
RICHARD R. AND DIANE K. SMITH) No. 90R-0282-ES

For Appellants: Richard R. Smith
Diane K. Smith

For Respondent: John A. Stilwell, Jr.
Counsel

OPINION

This appeal is made pursuant to section 19057, subdivision (a),^{1/} of the Revenue and Taxation Code from the action of the Franchise Tax Board in denying the claim of Richard R. and Diane K. Smith for refund of personal income tax in the amount of \$135.45 for the year 1987.

The issue presented by this appeal is whether the full amount of appellants' interest dividends is exempt from taxation where only a portion of the dividends is attributable to qualifying government obligations.

On their 1987 California personal income tax return, appellants reported interest

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

dividends which had been paid them by Fidelity U. S. Government Reserves Fund (Fidelity), a mutual fund. Appellants filed an amended return for 1987 on February 7, 1989, and claimed a refund in the amount of \$346.45, asserting that the previously reported interest dividends were exempt from taxation. The Franchise Tax Board (FTB) granted a refund to appellants in the amount of \$211. This appeal followed wherein appellants seek to be granted the \$135.45 disallowed by respondent.

Appellants assert that the full amount of the dividends they received from Fidelity is exempt pursuant to section 17145 as dividends derived from exempt government obligations. They further argue that they should get the full refund because the FTB's own written instructions and an employee of the State Board of Equalization^{2/} told them that such dividends are exempt.

California allows the exemption of interest dividends derived from exempt state, local, or U. S. government obligations pursuant to section 17145. The exempt status of dividends derived from such obligations is allowed to pass through to the individual shareholder of a mutual fund. (Brown v. Franchise Tax Board, 197 Cal.App.3d 300 [242 Cal.Rptr. 810] (1987).)

Section 17145, subdivision (a), for 1987 provided that where "at least 50 percent of the value of the total assets of a management company or series thereof, consists of obligations, interest on which is exempt from taxation under the Constitution or laws of this state, that company or series of that company shall be qualified to pay exempt-interest dividends to its shareholders." To claim the exemption, the shareholder must have received a written notice from the issuing company, designating the dividends as exempt. (Rev. & Tax. Code, § 17145, subd. (b)(1).)

Fidelity, in accord with the statute, issued a notice advising its shareholders that 60.31 percent of its interest dividends came from "U.S. Government Reserves." Respondent allowed appellants' claim for refund to the extent the notice indicated the interest dividends were derived from exempt government obligations, for a total of \$211.

Appellants argue the statute entitled them to exempt all of their interest dividends once Fidelity met the threshold criterion of section 17145, that the company's assets consist of at least 50 percent in government obligations. However, they have not taken into consideration the limitation on exemption which is also found in section 17145.

Section 17145, subdivision (b)(1), defines exempt-interest dividends as: "any dividend or part thereof paid by a management company or series thereof in an amount not exceeding the interest received by it during the taxable year on obligations, interest on which is exempt from taxation . . ." (Emphasis added.) The statute is clear that the exempt status of such dividends is proportionate only to the extent of the percentage shown to be from exempt government obligations. Accordingly, we rule in favor of the respondent on this issue.

Appellants' assertion they are nevertheless entitled to a full refund because they relied on

^{2/} The number appellants called for advice regarding their dividends is in fact for the Franchise Tax Board, not the Board of Equalization as indicated in appellants' brief.

information supplied by the FTB, sounds in the nature of an estoppel argument. As a general rule, government action will not be estopped unless the facts establish that a grave injustice would otherwise result. (California Cigarette Concessions v. City of Los Angeles, 53 Cal.2d 865 [3 Cal.Rptr. 675] (1960); Appeal of BalDar Industries, Inc., Cal. St. Bd. of Equal., Mar. 3, 1987.) Appellants have not shown they suffered any grave injustice as a result of the FTB's information. No injustice can be inferred when in fact the FTB allowed their claim for refund to the appropriate extent.

Accordingly, for the reasons set forth above, the respondent's action in this matter will be sustained.

ORDER

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 19060 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the claim of Richard R. and Diane K. Smith for refund of personal income tax in the amount of \$135.45 for the year 1987 be and the same is hereby sustained.

Done at Sacramento, California, this 9th day of October, 1991, by the State Board of Equalization, with Board Members Mr. Sherman, Mr. Dronenburg, Mr. Bennett, Mr. Fong, and Mr. Davies present.

_____, Chairman

Ernest J. Dronenburg, Jr., Member

William M. Bennett, Member

Matthew K. Fong, Member

John Davies*, Member

*For Gray Davis, per Government Code section 7.9
smith.es