

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of
KURBO CORPORATION

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No. 89R-1467-MC

For Appellant: Howard Gordon
 Certified Public Accountant

For Respondent: Douglas K. Powers
 Counsel

OPINION

This appeal is made pursuant to section 26075, subdivision (a),^{1/} of the Revenue and Taxation Code from the action of the Franchise Tax Board in denying the claim of Kurbo Corporation for refund of franchise tax in the amount of \$14,740 for the income year 1987.

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

The issue in this appeal is whether appellant is entitled to spread over four years payment of its tax liability for its short income year ended December 31, 1987, which short year is required by a change in its taxable year pursuant to the Tax Reform Act of 1986.

Appellant had elected to be a subchapter-S corporation (I.R.C. § 1361, et seq.) for federal income tax purposes. Prior to 1987, California had not conformed to subchapter S; consequently, corporations which were S corporations for federal purposes were taxed as "regular" corporations for state purposes. In 1987, after enactment of the Tax Reform Act of 1986 (P.L. 99-514) ("TRA 1986"), the California Legislature enacted provisions (Rev. & Tax. Code, § 23800, et seq.) recognizing subchapter-S status for California taxation purposes. (Stats. 1987, ch. 1139, § 55, p. 3991.) As part of TRA 1986, S corporations were required to adopt a calendar year for tax purposes.^{2/} (I.R.C. § 1378.) California also conformed to these provisions. (Rev. & Tax. Code, § 24633.5.)

Prior to 1987, appellant's income year ended on October 31 of each year. As a result of TRA 1986, appellant changed its income year end to December 31. In 1987, appellant thus had an income year of 12 months ended on October 31, 1987, and a short income year from November 1 to December 31, 1987. For its income year ended October 31, 1987, appellant paid tax as a "regular" corporation, and for its short year ended December 31, 1987, it paid tax as an S corporation. Appellant computed its tax for the short period as required by the statute, and then paid one-fourth of the liability. Appellant planned on paying one-fourth of its remaining liability in each of the three succeeding income years.

Section 24633.5 authorizes a corporate taxpayer to change its accounting period for state purposes when the change is required by TRA 1986. Section 24633.5 reads in its entirety as follows:

(a) In the case of any taxpayer required to change its accounting period by the federal Tax Reform Act of 1986 (Public Law 99-514), as modified by Section 10206 of Public Law 100-203, that change shall be treated as initiated by the taxpayer with the consent of the Franchise Tax Board.

(b) With respect to any partner or shareholder of an 'S corporation' which is required to include the items from more than one taxable year of the partnership or 'S corporation' in any one taxable year, any income in excess of expenses for the short income year resulting from the change described in subdivision (a) of Section

^{2/} Subsequent to the Tax Reform Act of 1986, Congress enacted I.R.C. section 444 allowing an S corporation to elect a taxable year other than a calendar year, in exchange for the making of a deposit pursuant to I.R.C. section 7519. Appellant did not make such an election.

17551.5 shall be taken into account ratably in each of the first four income years (including the short year) beginning after December 31, 1986, unless the partner or shareholder elects to include all that income in the short income year.

(c) The spreading of income over four years, as allowed by subdivision (b), shall not apply unless the taxpayer receives similar treatment for federal income tax purposes.

Nothing in this section provides for recognizing over four years the income of the corporation in the short year caused by the change in accounting period. The spread is authorized for the shareholders of the corporation, not the corporation itself.

Appellant argues that the intent of section 24633.5 was to allow taxpayers the same treatment for state purposes as is allowed for federal purposes. The underlying rationale of this position appears to be that, for federal purposes, appellant would have been allowed to spread its income and any resulting corporate tax liability over four years. However, for federal purposes, the four-year spread only applies to the shareholders of the corporation, not to the corporation itself. (Section 806(e), TRA 1986, as amended by sections 1008(e)(7) and (10) of the Technical and Miscellaneous Revenue Act of 1988 (P.L. 100-647).) Therefore, section 24633.5 does offer the same treatment as provided for by federal law.

Based on the plain language of the statute, we conclude that appellant is not entitled to spread the income earned in the short period over a four-year period. Accordingly, respondent's denial of appellant's claim for refund must 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 26077 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the claim of Kurbo Corporation for refund of franchise tax in the amount of \$14,740 for the income year 1987 be and the same is hereby sustained.

Done at Sacramento, California, this 7th day of May, 1992, by the State Board of Equalization, with Board Members Mr. Sherman, Mr. Dronenburg, and Ms. Scott present.

Brad Sherman _____, Chairman

Ernest J. Dronenburg, Jr. _____, Member

Winnie Scott* _____, Member

_____, Member

_____, Member

*For Gray Davis, per Government Code section 7.9
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