OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Consolidated Appeals of: **MCGARVEY-CLARK REALTY, INC.;** **AVIS BUDGET GROUP, INC.**	OTA Case Nos. 18083623 & 18083632

OPINION ON PETITION FOR REHEARING

Representing the Parties:

For Appellants: Jeffrey M. Vesely, Attorney
Zachary Atkins, Attorney

For Respondent: Michael R. Laisne, Attorney

A. LONG, Administrative Law Judge: On March 21, 2023, the Office of Tax Appeals (OTA) issued an Opinion sustaining respondent Franchise Tax Board's (FTB's) proposed assessment of additional tax. Appellants timely filed a petition for rehearing (petition) under Revenue and Taxation Code (R&TC) section 19048.

In the Opinion, OTA held that (1) FTB timely issued Notices of Proposed Assessment (NPAs) for the 1999 tax year to McGarvey-Clark Realty, Inc. (McGarvey) and Avis Budget Group, Inc. (Avis) (collectively, appellants), and (2) appellants' transaction did not constitute a "statutory merger" that qualifies as a tax-free reorganization under Internal Revenue Code (IRC) section 368(a)(1)(A).) Upon consideration of appellants' petition, OTA concludes they have not established a basis for rehearing.

OTA may grant a rehearing where one of the following grounds exists and materially affects the substantial rights of the party seeking a rehearing: (1) an irregularity in the appeal proceedings which occurred prior to issuance of the Opinion and prevented fair consideration of the appeal; (2) an accident or surprise, occurring during the appeal proceedings and prior to issuance of the Opinion, which ordinary caution could not have prevented; (3) newly discovered evidence, material to the appeal, which the filing party could not have reasonably discovered and provided prior to issuance of the Opinion; (4) insufficient evidence to justify the Opinion; (5) the

Opinion is contrary to law; or (6) an error in law in the OTA appeals hearing or proceeding. (Cal. Code Regs., tit. 18, § 30604(a)(1)-(6); *Appeal of Do*, 2018-OTA-002P.)

Appellants request a rehearing on the ground that the holding for each issue is contrary to law. To find that an opinion is against or contrary to law, OTA need not reweigh the evidence but must find that the opinion is "unsupported by any substantial evidence." (*Appeal of Graham and Smith*, 2018-OTA-154P, citing *Sanchez-Corea v. Bank of America* (1985) 38 Cal.3d 892, 906.) This requires a review of the Opinion to indulge in all legitimate and reasonable inferences to uphold the Opinion. (*Appeals of Swat-Fame, Inc., et al.*, 2020-OTA-045P.) The relevant question is not over the quality or nature of the reasoning behind the opinion but whether the opinion can be valid according to the law. (*Ibid.*) The evidence is considered in the light most favorable to the prevailing party (here, respondent). (*Ibid.*) Each issue is addressed separately below.[1]

Timeliness of FTB's NPAs

Appellants assert that the Opinion's holding that FTB timely issued the 1999 NPAs under R&TC section 19060(b) is wrong. In support of their position, appellants argue that the Opinion violates California law, which requires statutes of limitations to be strictly construed in favor of the taxpayer and not the tax agency; that R&TC section 19060(b) applies to NPAs only if the NPAs "[result] from" the final adjustment made by the IRS to a taxpayer's federal tax return and the NPA is for the same tax year adjusted by the IRS; the NPAs are time-barred because they did not "result from" any final adjustments made by the closing agreement; and the Opinion expands FTB's assessment authority well beyond what the legislature ever intended.

The Opinion held that the NPAs were timely issued because FTB issued them within the four-year statute of limitations provided under R&TC section 19060(b), as extended. The Opinion determined that R&TC section 19060 is not ambiguous, and there was no need to construe the statute's language.

Appellants argue that the Opinion is contrary to law because it states that statutes of limitations must be interpreted with a strict construction in favor of the taxing agency. Appellants also contend that California law requires strict construction in favor of the taxpayer.

[1] Appellants also state that there was insufficient evidence to justify the Opinion. However, appellants do not mention this ground for rehearing again in their petition or provide separate arguments to support their position; accordingly, this ground is not discussed in this Opinion.

However, the Opinion's statement was dicta that did not affect the outcome of the issue. In the Opinion, OTA found "[t]he plain language of R&TC sections 19059 and 19060 is not ambiguous." Unless there is some ambiguity in the language of a statute, the analysis ends with the statute's plain language. (*Amalgamated Sugar Co. LLC v. Vilsack* (9th Cir. 2009) 563 F.3d 822, 829.) Therefore, there was no need to further analyze or interpret the statute beyond the plain meaning of what was written by the Legislature.

Appellants' cited cases also support this proposition. *Edison California Stores, Inc. v. McColgan* (1947) 30 Cal.2d 472, 476 states, "*In case of doubt*, construction is to favor the taxpayer rather than government." (Italics added.)

In a recent appeal, *JP Morgan Trust Co. of Delaware v. FTB* (2022) 79 Cal.App.5th 245, 263, the court states, "*To the extent a tax statute is unclear*, it should be construed to favor the taxpayer." (Italics added.) "[Courts] may only construe a tax statute in favor of a taxpayer if the language of that statute is unclear." (*MCI Communications Services, Inc. v. Cal. Dept. of Tax & Fee Admin.* (2018) 28 Cal.App.5th 635, 650.) The Opinion found that there was no ambiguity in the statute; therefore, it did not construe the statute in favor of either the taxpayer or the tax agency. As stated in the Opinion, there is nothing in the language of R&TC section 19060(b) that limits the issuance of an NPA to the same tax year for which the IRS made its changes to the taxpayer's return.

The remainder of appellants' arguments rest on their argument that the NPAs did not "result from" (as used by R&TC section 19060(b)) a final adjustment made by the IRS, and the NPA was not for the same tax year. Appellants argue that R&TC section 19060(b) authorizes FTB to adjust appellants' returns arising as a consequence of the IRS's final adjustment, and only for the same year adjusted by the IRS. Appellants contend that because the Closing Agreement only required appellants to recognize gain from the sale of assets in 2002, even though the Closing Agreement acknowledges that gains should have been reported in 1999, FTB is limited to issuing an assessment only for the 2002 tax year.

These arguments, and others not restated here,[2] were already considered at length and decided in the Opinion. OTA is unpersuaded by appellants' citation to *Ordlock v. Franchise Tax Board* (2006) 38 Cal.4th 897 or to section 16.4 of FTB's Manual of Audit Procedures, for

[2] To the extent OTA does not specifically address appellants' arguments raised in their petition, they were considered and rejected.

example, for the proposition that the Opinion's interpretation of "resulting from" must be limited to the year adjusted by the IRS. The Opinion appropriately considered the evidence and arguments presented by appellants on appeal in reaching its conclusions. Appellants have not cited or presented any law that limits the interpretation of R&TC section 19060(b) in the manner advocated by appellants. Appellants' petition largely restates the same arguments appellants made in the underlying appeal, and OTA continues to find those arguments unpersuasive. (*Appeal of Graham and Smith*, *supra*.)

Definition of "statutory merger" under IRC section 368(a)(1)(A)

Regarding the second issue in the appeal, appellants argue that the Opinion's holding violates basic rules of statutory construction; the Opinion relies on dicta; the Opinion cites to precedent that was not in fact precedent; and that OTA did not address the 2003 Temporary Regulations and 2006 final Regulations and their effective dates, which were briefed and addressed by both parties at the hearing.

Appellants argue that the Opinion violates statutory construction by failing to follow the plain meaning of IRC section 368(a)(1)(A) because it interprets "merger" as a union of two or more corporations by the transfer of property of all to one of them which continues in existence and the other ceasing to exist. Appellants criticize the Opinion's consultation of IRS guidance, caselaw, Black's Law dictionary definitions, legislative history, and a law review article for supporting its interpretation of the word "merger," which appellant asserts are dicta. As explained in the Opinion, dictionary definitions are consulted in determining the plain meaning of language. (*Transwestern Pipeline Co., LLC v. 17.19 Acres of Property Located in Maricopa County* (9th Cir. 2010) 627 F.3d 1268, 1270.) Appellants have not presented any other statute, resource, or dictionary definition to support a plain meaning of the word "merger" where both corporations continue in existence without cessation of one of those corporations at the end of the transaction.

Appellants also argue that the Opinion's interpretation of "merger" would render the word "statutory" meaningless. The Opinion already addressed the effect of having the word "statutory" before "merger" in IRC section 368(a)(1)(A) and the legislative history indicating why the word was added. The term "statutory merger" is defined, in part, as "effected pursuant to the corporation laws of the United States or a State or Territory or the District of Columbia."

(Treas. Reg. § 1.368-2(b)(1).)[3] This part of the definition is not a part of the common meaning of "merger," which indicates that "statutory" was not rendered meaningless by the Opinion's interpretation of "merger."

Appellants also take issue with the Opinion's citations to six cases that support defining a merger as a transaction where one entity ceases to exist or liquidates. Appellants contend these cases are not precedent and should not be followed. Instead, appellants point to American Bar Association's (ABA's) comments submitted to the IRS Acting Commissioner of its finding that congress did not intend that one corporation must cease to exist for statutory mergers. Appellants also contend that the Opinion did not address the relevant regulations and their effective dates.

When reviewing the Opinion on a petition for rehearing, OTA must indulge in all legitimate and reasonable inferences to uphold the Opinion. (See *Appeals of Swat-Fame Inc., et al., supra*.) Thus, when examining the language at issue in light of this standard, OTA finds that the term "statutory merger" is unclear. As stated in the Opinion, the cited six opinions are persuasive authority that aid in understanding the commonly accepted definition or meaning of merger. It is well settled that where federal law and California law are the same, federal rulings and regulations dealing with the IRC are persuasive authority in interpreting the applicable California statute. (See *Appeal of Sedillo*, 2018-OTA-101P; *J.H. McKnight Ranch v. Franchise Tax Board* (2003) 110 Cal.App.4th 978, fn. 1.) As such, the Opinion properly reviewed and relied on the six cited cases to aid in the interpretation of IRC section 368(a)(1)(A).

Similarly, appellants' reliance on the ABA's commentary is not binding authority on how this statutory language must be interpreted. In 2007, the ABA's Section of Taxation submitted comments to the IRS Acting Commissioner, which invited commentary from the public on its proposed Treasury Regulation section 1.368-2. Appellants rely on the following statement in support of its position that their definition of statutory merger should prevail: "[W]e can find no evidence that Congress intended that a target corporation must strictly cease its existence 'for all purposes' in connection with a Type A Reorganization." However, the ABA's comments are also not binding authority. The comments are one organization's commentary on the treatment of stock acquisition transactions where, following the initial stock acquisition and as part of an

[3] See IRS Proposed Rules, Statutory Mergers and Consolidations, 68 FR 3384-01, 2003-1 C.B. 524, 2003 WL 158498 (Jan. 24, 2003).

integrated plan, the target corporation in a state law conversion becomes a disregarded entity. The ABA commentary argues that although there is no cessation of the target corporation, the conversion of the target corporation to a disregarded entity should nevertheless meet the definition of IRC section 368(a)(1)(A). That is not the situation that was at issue in this appeal. Moreover, the ABA commentary concedes that even under its flexible interpretation of IRC section 368(a)(1)(A), the transaction cannot resemble a taxable sale. Appellants did not argue or demonstrate in the underlying appeal that their transaction similarly did not resemble a taxable sale.

Also, as admitted in appellants' brief, the issue of whether a cessation or liquidation requirement existed was far from settled for the tax year at issue. Based on the lack of direct and binding authority on this issue, the Opinion is not contrary to law.

Based on the foregoing, OTA finds that the Opinion is valid according to the law, and appellants failed to establish that a ground for rehearing exists in this petition.

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Andrea L.H. Long
Administrative Law Judge

We concur:

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Veronica I. Long
Administrative Law Judge

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Asaf Kletter
Administrative Law Judge

Date Issued: 4/10/2024