



BEFORE THE STATE BOARD OF EQUALIZATION  
OF THE STATE OF CALIFORNIA

In the Matter of the Appeals of )  
FOOTHILL PUBLISHING CO. AND ) No. 82A-513-MW  
THE RECOHD LEDGER, INC. )

For Appellants: Philip S. Horwith  
President

For Respondent: Kathleen M. Morris  
Counsel

O P I N I O N

These appeals are made pursuant to section 25666<sup>1/</sup> of the Revenue and Taxation Code from the actions of the Franchise Tax Board on the protest of Foothill Publishing Co. against a proposed assessment of additional franchise tax in the amount of \$4,035 for the income year ended September 30, 1976, and on the protest of The Record Ledger, Inc., against a proposed assessment of additional franchise tax in the amount of \$709 for the income year ended September 30, 1977.

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.

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The question presented by these appeals is whether respondent properly determined that Foothill Publishing Co. (Foothill) and The Record Ledger, Inc. (Ledger), were not entitled to file a combined report.

Appellants are both wholly owned subsidiaries of American Publishing Company, Inc. (American). All three of these California corporations were engaged in the business of printing and publishing newspapers and other publications in California. During the appeal years, Foothill and Ledger did the printing for two small publications, one in Nevada and one in Arizona. They arranged for picking up copy in those states, did the printing in California, and delivered the finished publications to Nevada and Arizona in their own trucks. Appellants have also alleged that, for "a short period of time" they "took over the operation" of the Arizona publication (Appeal Ltr. at 2), but have presented no further information or substantiation.

Appellants apparently filed combined reports and calculated their income attributable to California by applying the standard three-factor formula for the appeal years. They did not file returns or pay tax in any other state. Respondent audited appellants' returns and determined that appellants' activities in other states were immune from taxation by virtue of Public Law 86-272. (15 U.S.C.A. §§ 381-384.) Therefore, in accordance with section 25135, subdivision (b) (2), respondent "threw back" their out-of-state sales to California, that is, treated them as sales in California. As a result of this "throwing back," respondent considered all of appellants' income to be derived from sources within California. Therefore, respondent considered use of the combined report and three-factor formula inappropriate and recalculated appellants' tax liability using separate accounting.

It is well settled that the authority for requiring a combined report rests in section 25101. Section 25101 provides that if a taxpayer has income "derived from or attributable to sources both within and without the state, the tax shall be measured by the net income derived from or attributable to sources within this state in accordance with the provisions of ..." the Uniform Division of Income for Tax Purposes Act (UDITPA) found in section 25120, et seq.

Respondent's only basis for disallowing appellants' use of a combined report stems from its "throwing

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back" of the Nevada and Arizona sales pursuant to section 25135. Section **25135** and its "throw back" rule, however, are not relevant in determining whether or not a taxpayer should file a combined report. The provisions of UDITPA, including section **25135**, are not applicable until it has been determined that a combined report is required under section 25101. Section **25135** is used only to determine the proper attribution of sales for purposes of calculating the sales factor of the apportionment formula.

For respondent to have used section **25135** at all, it must have concluded that appellants met the requirement of section **25101**; that is, that appellants had income "derived from or attributable to sources both within and without the state. ..." To then require separate accounting on the basis of a section which deals only with the calculation of the apportionment formula appears to us both illogical and contrary to the statutory provisions involved. We conclude, therefore, that appellants were entitled to report their income by using a combined report rather than by separate accounting.

We also conclude, however, that appellants' sales in other states were subject to the "throw back" rule of **section 25135** for purposes of their sales factor computations. Under section 25135, subdivision (b)(2), sales of tangible personal property are attributed to this state for sales factor purposes if the property is shipped from this state and the taxpayer is not taxable in the state of the purchaser. A taxpayer is taxable in another state if it is actually subject to certain types of taxes or if that state "has jurisdiction to subject the taxpayer to a net income tax regardless of whether, in fact, the state does or does not." (Rev. & Tax. Code, § 25122, subd. (b).) A state does not have jurisdiction to tax if it is prohibited from imposing a net income tax by virtue of Public Law 86-272. (Cal. Admin. Code, tit. 18, reg. 25122, subd. (c) (art. **2.5**.) Public Law 86-272 provides, in pertinent part:

No State ... shall have power to impose  
. . . a net income tax on the income derived  
**within** such State by any person from interstate  
commerce if the only business activities within  
such State by or on behalf of such person  
during such taxable year are ... the  
following:

(1) the solicitation of orders by such,  
person, or his representative, in such State

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for sales of tangible personal property, which orders are sent outside the State for approval or rejection, and, if approved, are filled by shipment or delivery from a point outside the State: ...

(15 U.S.C.A. § 381(a).)

From the facts before us, we can only conclude that appellants' activities fell within the prohibition to tax of Public Law 86-272. Therefore, the other states involved did not have jurisdiction to impose on appellants a net income tax and the sales should be "thrown back" to California pursuant to section 25135, subdivision (b)(2), when calculating appellants' sales factors.

Respondent's actions, therefore, are modified to the extent necessary to comport with our **conclusions** that appellants were entitled to file a combined report and that their out-of-state sales should be "thrown back" to California when calculating their sales factors.

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O R D E R

Pursuant to the views expressed in the opinion of the board on file in these proceedings, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 25667 of the Revenue and Taxation Code, that the actions of the Franchise Tax Board on the protest of Foothill Publishing Co. against a proposed assessment of additional franchise tax in the amount of \$4,035 for the income year ended September 30, 1976, and on the protest of The Record Ledger, Inc., against a proposed assessment of additional franchise tax in the amount of \$709 for the income year ended September 30, 1977, be and are hereby modified in accordance with the foregoing opinion.

Done at Sacramento, California, this 4th day of February, 1986, by the State Board of Equalization, with Board Members Mr. Nevins, Mr. Collis, Mr. Bennett, Mr. Dronenburg and Mr. Harvey present.

Richard Nevins, Chairman  
Conway H. Collis, Member  
William M. Bennett, Member  
Ernest J. Dronenburg, Jr., Member  
Walter Harvey\* m b ,e r

\*For Kenneth Cory, per Government Code section 7.9