89-SBE-026

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BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
) No. 82R-2211-CB
NORTHRIDGE FASHION CENTER, INC.)

Appearances:

For Appellant: Schuyler M. Moore
Attorney at Law

For Respondent: Terry Collins
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 Northridge Fashion Center, Inc., for refund of a penalty in the amount of $44,194.19 for the income year ended March 31, 1982.

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.

After concession&/ the only issue remaining for determination is whether respondent properly imposed a penalty for underpayment of estimated tax on appellant, an exempt organization, for the income year in dispute.

For the appeal year appellant was a nonprofit public benefit corporation and was thus generally exempt from corporate franchise and income taxes by virtue of section 23701. However, as an exempt organization, appellant was subject to the tax imposed on unrelated business taxable income by section 23731.

On or before June 15, 1982, appellant filed an application for automatic extension of time to file its exempt organiiation business income tax return (form 109), the form which is used by an exempt organization to report its tax on unrelated business taxable income. The request for extension was accompanied by payment and respondent granted the extension request. The form 109 was filed prior to the extended due date.

Respondent observed that appellant had not made payments of estimated tax. Therefore, respondent assessed a penalty for underpayment of estimated tax in the amount of $44,194.19 and offset the penalty against a requested refund. Due to the fact that the tax shown on appellant's return was generated by a sale of property which took place in the third quarter of the fiscal year, respondent now concedes that appellant is eligible for partial relief from the penalty. Respondent has reduced the amount of the penalty to $12,360.39. Thus, appellant is entitled to a refund of at least $31,833.80.

Section 25951 provides for a penalty in the event of any underpayment of estimated tax, except for certain circumstances described in section 25954. Section 23731 specifically characterizes the amount to be paid on unrelated income as a tax. For purposes of this appeal, appellant concedes that it had unrelated debt-financed income for tax purposes.

Appellant argues that the estimated tax provisions should not apply to tax-exempt organizations, applying a federal analogy. Appellant contends that there is ample legislative history expressly stating that the Legislature's intent in adopting the unrelated business taxable income

2/ Respondent has conceded the other issue, which involved the payment of interest on a refund.

provisions in California in 1951 was to conform to federal changes in 1950.

In the absence of a specific statutory exemption, there is no obvious reason why exempt organizations which generate unrelated business taxable income, and thus compete with taxable organizations, should be placed in an advantageous position by not being subject to the estimated tax provisions. For the appeal year, such an exemption was not present in the Revenue and Taxation Code. Appellant has supplied some historical material on changes in California law for 1951 that is general in nature and does not explain the differences in federal and California law. Among the differences that have existed between federal and California law regarding penalties are the rate used to measure the penalty and the fact that no minimum tax is due on the first installment of estimated taxes under federal law. (Compare Rev. & Tax. Code, §§ 25951-25954 with. I .R.C. § 6655.) Also, federal law relating to domestic international sales corporations (DISCs) has no California counterpart, and a DISC under federal law is subject to the regular rules regarding payment of estimated taxes under California law. (Compare IRC §§ 991-997 with Appeal of Cerwin-Vega International, Cal. St. Bd . of Equal ., Aug. 15, 1978).

Appellant argues that the federal Tax Reform Act of 1986 amended Internal Revenue Code section 6154 by adding subsection (h), which for years subsequent to December 31, 1986, makes estimated tax penalties applicable to exempt organizations which are subject to the federal tax on unrelated business taxable income. Furthermore, appellant suggests that because such exempt corporations first became subject to the federal estimated tax penalty provisions beginning in 1987, the alleged similarity between federal and California laws should lead to the conclusion that appellant is not subject to the penalty under section 25951 for its 1982 income year.

California has a regulation which provides:

> (f) Returns. For requirements of filing annual returns with respect to unrelated business income tax see sections 23771 and 18405.1. Estimated tax returns must be filed but as the tax is imposed by chapter 3 of part II, Division 2, the payment of at least the minimum tax with the first installment is not required. Filing of form 109 is in addition to form 199 or 199B. (Emphasis added.)

(Cal. Admin. Code, tit. 18, reg. 23731, subd. (f).)

This regulation was amended slightly in 1982 (Register 82, No. 37) from the former section 23731, subdivision (f), which was added in 1973 and provided:

> (f) Returns. For requirements of filing annual returns with respect to unrelated business income tax see sections 23771 and 18405.1. Estimated tax returns must be filed but as the tax is imposed by article 3, the payment of at least the minimum tax with the first installment is not required. Filing of form 109 is in addition to form 199 or 199B. (Emphasis added.)

The regulations are similar, and both reflect the long-standing proposition that exempt organizations with unrelated business taxable income are subject to the estimated tax provisions contained in section 25561 et seq. For the appeal year, there was no similar federal provision. Furthermore, the instructions for form 109 (California Exempt Organization Business Income Tax Return) have clearly required estimated tax payments since at least 1965.

Appellant contends that this board should declare regulation 23731, subdivision (f), which requires appellant to make payments of estimated tax, invalid. The contentions are as follows: (1) the regulation does not further the legislative policy of keeping California's taxation of unrelated business taxable income in conformity with federal law; and (2) respondent is not authorized to issue "legislative regulations."

There is no policy which requires this state to have laws which are identical in every respect to those contained in the Internal Revenue Code. Regulation 23731, subdivision (f), merely reflects one of many differences which existed between California and federal law during the appeal year. Furthermore, respondent's long-standing administrative interpretation, as reflected in the regulation, suggests legislative acquiescence in respondent's construction of the applicable statutes. (See Great Western Financial Corporation v. Franchise Tax Board, 4 Cal.3d 1 (1971).)

Relief from the penalty for underpayment of estimated tax is available only under specified circumstances set forth in section 25954. Appellant has neither contended nor demonstrated that it is entitled to relief under this section. Accordingly, respondent's action in this matter, as modified in accordance with respondent's concessions, 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 Northridge Fashion Center, Inc., for refund of a penalty in the amount of $44,194.19 for the income year ended March 31, 1982, be and the same is hereby modified in accordance with the concessions made by the Franchise Tax board. In all other respects, the action of the Franchise Tax Board is sustained.

Done at Sacramento, California, this 26th day of September1989, by the State Board of Equalization, with Board Members Mr. Carpenter, Mr. Bennett, Mr. Dronenburg, and Mr. Davies present.

Paul Carpenter, Chairman

William M. Bennett, Member

Ernest J. Dronenburg, Member

John Davies*, **, Member

_____, Member

*For Gray Davis, per Government Code section 7.9

**Abstained