ADOPTED 8/31/95 95-SBE-008

BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of	)	
	)	No. 91R-1452
Harminder S. and Harpal Chana	)	

Appearances:

For Appellant:	Dwight L. Martin Certified Public Accountant
For Respondent:	Richard Gould, Counsel

O P I N I O N

This appeal was originally made pursuant to section 19045(formerly section 18593) of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Harminder S. and Harpal Chana against a proposed assessment of additional personal income tax and penalty in the total amount of $2,976.13 for the year 1987. Subsequent to the filing of this appeal, appellants paid the proposed assessment in full. Accordingly, pursuant to section 19335 (formerly section 19061.1) of the Revenue and Taxation Code, this appeal is treated as an appeal from the denial of a claim for refund.

The issues to be decided in this appeal are: (1) whether a nonresident of California must incur a net operating loss from all sources in order to be able to report and carry over a California-source net operating loss deduction; (2) whether appellants have demonstrated that their failure to timely file their 1987 California return was due to reasonable cause; and (3) whether interest on the deficiency assessment should be abated.

In 1985, 1986, and 1987, appellants were nonresidents of the State of California. However, during those years the appellants were partners in a farming operation (partnership) located in California. In 1985, the California partnership generated a loss for appellants, but because of their income from other sources[1/] outside of California, the appellants claimed no net operating loss deduction on their 1985 federal return nor in computing adjusted gross income from all sources on their California return. On their 1987 California return, the appellants reported income of $27,910 from the partnership, but they also claimed a net operating loss carryover of $212,535, allegedly generated from their 1985 partnership loss. Respondent conducted an audit of appellant's 1987 return, and on August 13, 1990, issued a proposed assessment based upon the disallowance of the net operating loss carryover because appellants failed to have a net operating loss from all sources in 1985.

Further, respondent also assessed a late filing penalty against appellants, pursuant to Revenue and Taxation Code[1/] section 18681 because appellants failed to file their 1987 return until on or about October 15, 1988. Appellants contend that they had reasonable cause to file late, in that they had obtained an extension to file their federal 1987 return, and they believed that said federal extension would also extend their time to file the California return. Finally, appellants contend that they should not have to pay interest on the proposed assessment due to respondent's delay in issuing the assessments.

Respondent denied appellants' protest of these matters, and on August 30, 1991, issued a notice of action affirming the proposed assessment. Appellants paid the deficiency in full, and filed this timely appeal.

California's allowance of "net operating loss carryover" is described in the following pertinent portions of section 17276, which were applicable beginning in 1987:

> The deduction provided by Section 172 of the Internal Revenue Code, relating to a net operating loss deduction, shall be modified as follows:

[1/] On their 1987 federal return, the appellants listed their professions as "doctor" and "real estate broker."

[2/] Unless otherwise specified, all remaining section references are to the Revenue and Taxation Code as in effect for the year in issue.

> (a)(1) Net operating losses attributable to taxable years beginning before January 1, 1985, and on or after January 1, 1992, shall not be allowed, except for losses allowed by this section (as amended by Chapter 938 of the Statutes of 1984) and former Section 17276.5 (as amended by Chapter 158 of the Statutes of 1986).
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> * * *
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> (d) Notwithstanding the provisions of Section 172(b)(1) of the Internal Revenue Code, a net operating loss attributable to a taxable year beginning on or after January 1, 1985, and before January 1, 1987, shall be a net operating loss carryover to the first taxable year beginning on or after January 1, 1987, and before January 1, 1988, and for each of the two succeeding taxable years.
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> * * *
>
> (e) For purposes of computing the net operating loss deduction under Section 172(a) of the Internal Revenue Code, as modified by this section, the amount of a net operating loss sustained in any taxable year during any part of which the taxpayer was not a resident of this state shall be limited to the sum of the following:
>
> (1) The portion of the net operating loss attributable to the part of the year in which the taxpayer is a resident.
>
> (2) The portion of the net operating loss which, during the part of the year the taxpayer is not a resident, is attributable to California source income and deductions. (Emphasis added.)

Respondent contends that section 17276 allows nonresident taxpayers to have a carryover net operating loss on their California return only if the taxpayers' California losses exceed their income from all sources, just as is done under Internal Revenue Code (I.R.C.) section 172 in determining the taxpayer's federal income tax liability. Appellants focus on 17276, subdivision (e)(2), to argue that under the statute only California-source income may be used to offset California-source net operating losses.

We believe that the respondent is correct in its interpretation of section 17276. It appears clear to us that the Legislature's use of the term "portion" in subdivision (e)(2) indicates that only a part of the nonresident taxpayer's total net operating loss shall be allowed - the losses attributable to a California

source. Under the appellants' interpretation, the term "portion" is meaningless because all of the nonresident taxpayer's California-source net operating loss would be included in every situation. The presence of the clear statutory provision eliminates any discretion on our part in interpreting a statute. (Appeal of Dorothy Shinder, Cal. St. Bd. of Equal., Aug. 30, 1967.)

Moreover, operative in 1989 the Legislature moved the pertinent portions of the provisions found in section 17276, subdivision (e), relating to the net operating loss allowable to a nonresident, to section 17041, subdivision (i). Section 17041 deals with the general tax computation of both residents and nonresidents. In connection with that move, which was sponsored by the respondent, it issued a bill analysis summary which explained the then-existing California net operating loss (NOL) provisions as they applied to nonresidents, as follows:

> "NOLS -- California conforms to the federal provisions, with modifications. One of the modifications is the treatment of NOLs of nonresidents who have California source income. These nonresidents determine their tax (on total AGI) as described above. [i.e. using the California Method.] Therefore, **a nonresident determines whether he or she sustained an overall NOL by computing the loss as though a full year resident, regardless of source** (540NR). If an **overall** NOL was sustained, the taxpayer then determines how much of an overall NOL, if any, is attributable to California sources for carryover to Schedule SI in future years. **The amount of the California NOL may not exceed the overall NOL** or the sum of: (1) any loss attributable to the part of the year in which he or she was a resident, and (2) any loss, when a nonresident which is attributable to California source deductions in computing California-source income and deductions in computing adjusted gross income (AGI). This rule is being moved from the NOL provisions to the section that provides for the general tax computation of nonresidents. (Resp.Br., Exh. I., Emphasis added.)

The contemporaneous interpretation accorded a statute by the agency charged with administering the statute is to be given great weight. (Coca-Cola Co. v. State Board of Equalization, 25 Cal.2d 918, 921 [156 p.2d 1] (1945); Appeal of Estate of Philip Rosenberg, etc., Cal. St. Bd. of Equal., Aug. 2, 1975, modified Feb. 2, 1976.) Further, although the bill analysis summary was not a "regulation," the fact that the bill was approved after the Legislature received the summary, without any

apparent opposition by the Legislature to the contents of the summary, also supports respondent's interpretation of the net operating loss provisions.[1/]

In order for appellants to gain relief from the imposition of late filing penalties, they need to present evidence that the late filing was due to reasonable cause. (Rev. & Tax. Code, § 18681.) The appellants argue that they could not prepare their 1987 California return until their federal 1987 return was completed, and they had an extension to October 15, 1988, in which to file their federal return. Appellants also state that they believed their federal extension also extended the time they had in which to file their California return. Such excuses do not constitute the necessary reasonable cause. We have held that the lack of information or incomplete records - presumably here a federal 1987 return - does not constitute reasonable cause for failure to timely file a tax return. (Appeal of William T. and Joy P. Orr, Cal. St. Bd. of Equal., Feb. 5, 1968.) Moreover, ignorance of the law does not constitute reasonable cause for failure to timely file a California tax return. (Appeal of J.B. Ferguson, Cal. St. Bd. of Equal., Sept. 15, 1958.) Therefore, respondent's imposition of a late filing penalty was proper.

Finally, the imposition of interest on a deficiency is mandatory. (Appeal of Amy M. Yamachi, Cal. St. Bd. of Equal., June 28, 1977.) Appellants appear to contend that because it took "an unnecessarily long period of time" for respondent to provide its interpretation of section 17276 and to issue its proposed assessment to appellants, that they should not be held liable for the accrued interest. However, there is no statute which allows for the abatement of interest under such circumstances.[1/]

Therefore, the actions of the respondent in this matter will be sustained.

[3/] Because of the conclusion we reach on this first issue, another issue raised by respondent, regarding whether the appellants' California income qualified as "farm income" under the California statutes allowing net operating loss carryovers, is moot.

[4/] Section 18688, subdivision (c) (amended and renumbered as section 19104, operative January 1, 1994), allowed for the abatement of interest due to certain delays of respondent's employees in performing ministerial acts. However, even if the actions of respondent complained of in this case were to be considered "ministerial" (and clearly they were not merely ministerial), we have previously held that we have no jurisdiction to review the respondent's exercise of its discretion to abate or not to abate interest under this statute. (Appeal of Philip C. and Ellen Boesner Snell, 92-SBE-023, July 30, 1992.)

O R D E R

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 19333 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the claim of Harminder S. and Harpal Chana for refund of personal income tax and penalty in the total amount of $2,976.13 for the year 1987, be and the same is hereby sustained.

Done at Sacramento, California, this 31st day of August, 1995, by the State Board of Equalization, with Board Members Mr. Klehs, Mr. Dronenburg, Mr. Andal, Mr. Sherman and Mr. Halverson present.

Johan Klehs , Chairman

Ernest J. Dronenburg, Jr. , Member

Dean F. Andal , Member

Brad J. Sherman , Member

Rex Halverson* , Member

*For Kathleen Connell, per Government Code section 7.9.