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10 **BOARD OF EQUALIZATION**

11 **STATE OF CALIFORNIA**

12 In the Matter of the Appeal of:

) **HEARING SUMMARY<sup>2</sup>**

) **CORPORATION FRANCHISE TAX APPEAL**

13 **JK GROUP, LLC<sup>1</sup>**

) Case No. 448306

<u>Years</u>	<u>Claims For Refund<sup>3</sup></u>
2001	\$10,254
2002	\$9,914
2003	\$9,278
2004	\$7,977
2005	\$7,337

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19 <sup>1</sup> Appellant, a Limited Liability Company (LLC), was headquartered in San Diego County, California.

20 <sup>2</sup> This appeal was pulled from the February 24, 2010 hearing calendar to allow the parties to enter settlement negotiations.  
 21 The matter was placed on the April 24, 2012 oral hearing calendar and, after appellant waived appearance, it was rescheduled  
 22 to the May 30, 2012 consent calendar. Appellant subsequently asked that the appeal to be reinstated for an oral hearing and  
 23 the matter was scheduled for the Board's July 24-26, 2012 Culver City Board meeting. The matter was pulled from the July  
 24 24, 2012 calendar to allow appellant additional time to respond to a Board Member Inquiry, and rescheduled to the October  
 25 23-25, 2012 Culver City Board meeting.

26 <sup>3</sup> The amounts listed here are the amounts submitted by appellant on appeal. Respondent notes that the amounts are  
 27 overstated, since those amounts include the annual \$800 LLC tax, penalties, and interest associated with that tax, and late  
 28 filing penalties. (Resp. Op. Br., p. 1, fn. 1 & pp. 12-14.) Appellant concedes the \$800 LLC tax and related penalties and  
 interest. (App. Add'l Br., p. 1.) Respondent states that the appropriate amounts at issue are as follows (see Resp. Op. Br., p.  
 1, fn. 1 & p. 14):

2001	\$9,400.69
2002	\$8,821.03
2003	\$8,376.67
2004	\$7,176.76
2005	\$6,482.16

1 Representing the Parties:

2 For Appellant: Edwin P. Antolin, Silverstein and Pomerantz, LLP<sup>4</sup>

3 For Franchise Tax Board: Todd Watkins, Tax Counsel III

4  
5 QUESTIONS: (1) Whether appellant operated the Burger King restaurant businesses during the  
6 taxable years 2001 through 2005, and therefore is obligated to pay LLC fees  
7 based upon the total income generated from those businesses.

8 (2) Whether the proposed assessment of the LLC fees is unconstitutional.<sup>5</sup>

9 (3) Whether the refund amounts at issue are properly calculated.

10 HEARING SUMMARY

11 Procedural Background

12 Respondent collected LLC fees, and other related amounts, for 2001 through 2005  
13 through a jeopardy assessment filed in 2006. (Resp. Op. Br., exhibit F.) After the assessment became  
14 final, appellant filed claims for refund in the form of amended returns, asserting that it never operated  
15 the restaurant businesses. (Resp. Op. Br., exhibit M.) Respondent denied appellant’s claims for refund  
16 on the basis that it operated the businesses during those years and the gross receipts of the restaurant  
17 businesses were therefore attributable to appellant. (Resp. Op. Br., p. 10; App. Op. Br., exhibit A.)  
18 This timely appeal followed.

19 Factual Background

20 In January 1991, James Kozen began operating at least one Burger King restaurant  
21 franchise as a sole proprietor under the d.b.a. of JK Group with a federal employer identification  
22 number (EIN) beginning with “95”. On January 18, 1995, Mr. Kozen formed appellant, JK Group,  
23 LLC. (Resp. Op. Br., exhibit A.) The articles of organization include an attachment that states, “The  
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26 <sup>4</sup> Appellant was originally represented by Arthur Martinez & Associates, CPA, who submitted appellant’s appeal letter,  
27 opening brief, and additional briefs up through August 14, 2009. Mr. Antolin became appellant’s representative on  
28 February 9, 2010, prior to the pre-hearing conference.

<sup>5</sup> Litigation regarding the constitutionality of the LLC fee, as applied to a taxpayer deriving income wholly from California is  
still proceeding. (See *Bakersfield Mall v. Franchise Tax Board* (currently pending in San Francisco Superior Court, case no.  
CGC-074627228). Appellant is aware of the pending litigation and at appellant’s request this appeal is moving forward on  
the basis that appellant’s primary argument is factual in nature.

1 limited liability company is a single-purpose limited liability company formed solely for the purpose of  
2 operating Burger King Restaurants.” (*Id.* at exhibit A, p. 2.) Statements filed by appellant with the  
3 Secretary of State’s (SOS) office indicated the LLC’s type of business was operating a Burger King  
4 franchise. (*Id.* at exhibit B.) Appellant’s operating agreement lists appellant’s first purpose as to  
5 “[a]cquire, own, buy, sell, trade, operate, manage, exchange or otherwise dispose of Burger King  
6 restaurants, that the Managers may from time to time deem to be in the best interests of the Company.”  
7 (Resp. Op. Br., exhibit D.) The operating agreement notes on its opening disclaimer that “ownership of  
8 the company may be transferred only after authorization by Burger King Corporation in accordance  
9 with the terms and conditions outlined in the Franchise Agreement with Burger King Corporation.”  
10 (App. Add’l Br., exhibit C, p. 4.) JK Group, LLC, operated until the company was dissolved on  
11 January 3, 2007. (Resp. Op. Br., exhibit C.)

12 Respondent indicates that appellant filed California LLC tax returns from 1997 through  
13 2000 reporting that it operated a restaurant business, using an EIN beginning with “33”.<sup>6</sup> (Resp. Op.  
14 Br., exhibit E.) Respondent notes that appellant paid the reported LLC tax and LLC fee for tax years  
15 1997 through 2000. (*Id.* at p. 3.) The LLC became a single-member LLC effective January 1, 2000.  
16 (*Id.* at exhibit E, p. 17.) Respondent indicates that appellant became taxable as a subchapter S  
17 corporation on June 26, 2005, and was therefore no longer required to pay the LLC tax or LLC fee after  
18 that date. (*Id.* at p. 2.) Respondent indicates that appellant did not timely file its 2001, 2002, and 2003  
19 returns. (*Id.* at p. 3.)

20 Respondent apparently contacted Mr. Kozen by phone on January 6, 2005, and informed  
21 him that appellant had a filing requirement that included the LLC fee. Mr. Kozen informed respondent  
22 at this time that he was selling both Burger King stores. (Resp. Post-Conf. Reply Br., p. 1 & exhibit  
23 A.) Appellant subsequently filed a timely 2004 return (received March 1, 2005), and untimely returns  
24 for 2001 through 2003 (all received January 15, 2005) and 2005 (received March 29, 2006).<sup>7</sup> (Resp.  
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27 <sup>6</sup> On appellant’s 2000 LLC tax return, it reported its principal business activity as “restaurant,” and its principal product or  
28 service as “food & beverage.” (Resp. Op. Br., exhibit E, p. 17.) Appellant asserts that the LLC at this time, and always was,  
only leasing land to Mr. Kozen’s sole proprietorship, which ran the restaurant business. (App. Op. Br., p. 1 & 2.)

<sup>7</sup> Appellant also filed late returns for the 1995 and 1996 tax years, reporting its activity in the same manner as for the 2001  
through 2005 returns. (Resp. Op. Br., exhibit H.)

1 Op. Br., exhibit G.) Appellant reported no income and paid only the \$800 annual LLC tax, listing its  
2 principal business as “Service,” and product or service as “Pension MGMT.” (*Ibid.*) Appellant  
3 reportedly informed respondent that the employee pension plan was established and that such plan  
4 remains under the LLC. (*Id.* at exhibit J.)

5 A letter from an escrow company dated November 23, 2005, was received by  
6 respondent and indicated that a Burger King in Montrose, California (the Montrose Burger King) was  
7 being sold with a reference to the taxpayer EIN beginning with “33” (the number associated with  
8 appellant). (Resp. Op. Br., exhibit K.) A similar letter was received in regard to the sale of a different  
9 Burger King restaurant on Airport Boulevard in Los Angeles (the LAX Burger King) to Mangen  
10 Group, Inc., on May 5, 2006, also referencing appellant’s EIN.<sup>8</sup> (*Id.* at exhibit L.) Respondent  
11 indicates that appellant was attempting to sell its last known asset, the LAX Burger King, and therefore  
12 issued a jeopardy assessment on May 30, 2006. (*Id.* at exhibit F.)

13 The jeopardy assessment was based on unpaid LLC fees, penalties, and interest for years  
14 2001 through 2005, plus penalties and interest for the late paid 2005 LLC tax, a collection fee, related  
15 penalties, plus other amounts not at issue here. (Resp. Op. Br., p. 5 & exhibit F.) Appellant did not  
16 protest the assessment and it became final on June 30, 2006. Respondent collected the unpaid amounts  
17 on August 4, 2006, pursuant to an Order to Withhold after the second Burger King sale closed.<sup>9</sup> (*Ibid.*)

18 On July 24, 2006, appellant filed amended returns for tax years 1997 through 2005,  
19 which were treated as claims for refund.<sup>10</sup> (Resp. Op. Br., exhibit M.) The amended returns reflected  
20 rental real estate income of between \$30,000 and \$57,000 for each year, still reported only the \$800  
21 LLC tax as an amount due, and noted that previous payments of \$800 satisfied any liability. These  
22 returns reflected a new principal business of “Leasing,” and a principal product or service of  
23

24 <sup>8</sup> Evidence provided by appellant appears to show that, in connection with sales taxes, the BOE replied to a similar letter,  
25 regarding the escrow on the LAX Burger King restaurant, on August 15, 2006, by stating that Mr. Kozen, d.b.a. JK Group  
26 (as opposed to referring to JK Group, LLC), was current on his taxes. (App. Add’l Br., exhibit F, p. 2.)

27 <sup>9</sup> Respondent provides detailed statements of the items of tax, penalties, and interest collected from appellant for each of the  
28 tax years at issue. (Resp. Add’l Br., exhibit A.)

<sup>10</sup> Respondent notes that appellant’s amended returns for 1997 through 1999 classify its structure as a solely-owned LLC,  
rather than as a partnership as was previously reported on the original returns for those years. (Resp. Op. Br., p. 6.)

1 commercial property. The returns were accompanied by the required federal Form 8825, regarding  
2 rental real estate income. Because appellant was disregarded for federal tax purposes, it was not  
3 required to report such rental income or file a federal Form 8825 with the Internal Revenue Service  
4 (IRS) for the years at issue. (*Id.* at p. 6.)

5 In a correspondence dated December 22, 2006, appellant summarized its view of  
6 Mr. Kozen's franchise operation for respondent, concluding that it never conducted the Burger King  
7 restaurant business at any time.<sup>11</sup> (Resp. Op. Br., exhibit N.) Appellant states in the letter that it was  
8 formed with the intention of only holding the ground lease, which it subleased to Mr. Kozen or his sole  
9 proprietorship which operated the Burger King restaurant. Appellant asserted in the letter that its  
10 accountant misinformed Mr. Kozen of the proper filing requirements, and began reporting the activity  
11 of the proprietorship under the EIN (beginning with "33") of the LLC. Appellant stated that his current  
12 accountant properly reported all Burger King restaurant income to Mr. Kozen, but still erred by using  
13 appellant's EIN rather than the sole proprietorship's EIN. Appellant also noted that the use of the name  
14 JK Group for the sole proprietorship and JK Group, LLC, for the LLC caused confusion during the sale  
15 of the Burger King restaurant. (*Ibid.*)

16 In reviewing appellant's claim, respondent obtained third party records in the form of  
17 Minutes of the City of Los Angeles Board of Airport Commissioners for December 5, 2005, which  
18 state that appellant was the lessee for the property on Airport Boulevard where the LAX Burger King  
19 restaurant was located. (Resp. Op. Br., exhibit P, p. 2; see also App. Add'l Br., exhibit D.) Records  
20 from the same group on July 17, 2006, label appellant as the operator of the Burger King at that  
21 location. (*Id.* at exhibit Q, p. 2.) Other records provided by respondent show that vendors of the LAX  
22 Burger King restaurant business entered into legal relationships with appellant, rather than Mr. Kozen  
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26 <sup>11</sup> During the protest period prior to this appeal, and the original briefing period on appeal, appellant and respondent appeared  
27 to only contest whether appellant operated the LAX Burger King. During the pre-hearing conference, discussed *infra*, it  
28 became known that respondent calculated the fee on the basis that appellant operated both the LAX Burger King and the  
Montrose Burger King. However, it appears that inclusion of the Montrose Burger King did not change the amount of LLC  
fee due (since the gross income of the LAX Burger King, alone, resulted in the maximum possible LLC fee), and this may be  
why the parties did not focus on the Montrose Burger King. Early contentions from the parties refer only to the LAX Burger  
King.

1 individually or the sole proprietorship.<sup>12</sup> (Resp. Op. Br., exhibit W.)

2 Other documents provided show that a Wells Fargo Bank account was held in the name  
3 of “J K Group, Burger King,” with no LLC label attached. (Resp. Op. Br., exhibit X.) Transaction  
4 activity on this account shows payments were made to the Burger King Corporation and the BOE, as  
5 well as payments to State Farm Insurance for a “J.K. Group LLC” account. Information regarding the  
6 name and EIN under which the account was opened and used was not provided. (*Ibid.*) Appellant  
7 provided a copy of a fax from the Burger King Corporation which states that the franchise was started  
8 by Mr. Kozen, and was 100 percent owned by Mr. Kozen as of the July 2006 date on the fax. (Resp.  
9 Op. Br., exhibit Y.) Appellant provides the first and last page of a sales agreement for the LAX Burger  
10 King with a signature date of April 14, 2006. The first page of the agreement lists Mr. Kozen and JK  
11 Group, LLC, collectively as the seller, and further states that JK Group, LLC was the owner and seller  
12 of the real property lease and building, and Mr. Kozen was the owner and seller of the Franchise  
13 Agreement and all personal property transferred. The partial submission did not list or describe all of  
14 the property transferred in the sale. (Resp. Op. Br., exhibit Z.)

15 Appellant provides permits and forms from government agencies to support its  
16 contention that the LAX Burger was operated by Mr. Kozen and not appellant. Appellant provides a  
17 fire permit from the City of Los Angeles issued December 29, 2004, to Mr. Kozen; a 2005 license for  
18 soft serve milk product production listing Mr. Kozen as the owner of the LAX Burger King; a  
19 wastewater permit in Mr. Kozen’s name effective January 1, 1991, amended July 30, 2002, and with no  
20 expiration date; a public health operating permit from the County of Los Angeles for the LAX Burger  
21 King issued August 26, 2005, to Mr. Kozen, “C/O J K Management Co” with an expiration date of  
22 June 30, 2006; and a police commission permit from the City of Los Angeles issued to Mr. Kozen and  
23 “JK Group King” for the LAX Burger King issued January 5, 1991. (App. Add’l Br., exhibit B.)  
24 Appellant also provides a City of Los Angeles tax registration certificate to Mr. Kozen and “JK Group  
25 King” issued December 8, 1990; an equipment permit renewal for a charbroiler dated July 30, 1999,  
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28 <sup>12</sup> These public records gathered from LexisNexis show appellant as a debtor in a secured arrangement with food and  
beverage suppliers, among others. The arrangements were all active during at least a couple of the years at issue, if not all of  
the years at issue. (Resp. Op. Br., exhibit W.)

1 issued to “Burger King Rest” at the LAX location; a release of unemployment insurance liability for the  
2 LAX Burger King operation listing the seller as “J K Group,” dated July 31, 2006; and a Form W-3  
3 (relating to payroll) for 2006 listing the employer as “JK Group” with no reference to a specific Burger  
4 King location. (*Ibid.*)

5 Appellant provided respondent copies of Mr. Kozen’s federal Schedule C forms for the  
6 years at issue. (Resp. Op. Br., exhibit R.) The Schedule C for 2002 reports the business name as JK  
7 Group, LLC, and provides appellant’s EIN. (*Id.* at exhibit R, p. 1.) Respondent states that Mr. Kozen  
8 used this business name and number for 2002 through 2004, but subsequently submitted amended  
9 federal returns changing the business name to JK Group, and providing his personal EIN beginning  
10 with “95”. (*Id.* at p. 8.) The Schedule C forms, in conjunction with and verified by quarterly sales tax  
11 returns, report gross receipts for the years at issue.<sup>13</sup> (*Id.* at exhibits R & S.) Evidence shows that  
12 Mr. Kozen applied for the seller’s permits for the two Burger King restaurants in 1990 and 1994, and  
13 appellant apparently never applied for new permits, which it would be required to do if it began  
14 operating the restaurants. (*Id.* at pp. 8-9 & exhibits T & U; App. Add’l Br., exhibit F.) Appellant is  
15 listed as the lead name on the quarterly sales tax returns for the LAX Burger King from at least  
16 January 1, 2001, through the end of 2004.<sup>14</sup> (*Id.* at exhibit S.) Respondent provided documents which  
17 show that wages from the restaurant businesses were reported to the Employment Development  
18 Department (EDD) under appellant’s name and EIN from the beginning of 1997 into 2006. (*Id.* at  
19 exhibit V; Resp. Add’l Br., exhibit B.)

#### 20 Developments on Appeal

#### 21 *Pre-hearing Conference*

22 At appellant’s request, Appeals Division staff conducted a pre-hearing conference with  
23 the parties on July 21, 2011. At the pre-hearing conference, appellant gave further background  
24 information regarding Mr. Kozen’s operation of Burger Kings prior to appellant’s formation. The  
25 parties also discussed the evidence provided as well as the evidence respondent desired from appellant.  
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28 <sup>13</sup> Respondent notes that there are discrepancies with the 2002 and 2005 tax years, but appears to follow the amounts listed on  
the Schedule C forms whenever a discrepancy exists. (Resp. Op. Br., p. 8.)

<sup>14</sup> The 2005 quarterly sales tax returns list the lead name as “J.C. Group.” (Resp. Op. Br., exhibit S, pp. 18-19.)

1 Appeals Division staff was able to clarify that respondent included the income from the Montrose  
2 Burger King location in calculating appellant's LLC fees. As noted below, after the pre-hearing  
3 conference, Appeals Division staff issued an additional briefing request to enable appellant to submit  
4 for the record the relevant evidence brought to the conference, as well as any additional relevant  
5 evidence, and provide additional briefing.

6 Mr. Kozen indicated at the conference that he formed KP Partnership with a partner in  
7 either 1980 or 1981 for the purposes of operating Burger King restaurants. Mr. Kozen asserted he  
8 located, negotiated the price of, and maintained the real property for the restaurants. KP Partnership  
9 opened the Montrose Burger King (store #4424) around 1985 on a 20 year lease for the land and  
10 building, and built the building for the LAX Burger King (store #6941) on leased land in 1991. (App.  
11 Aug. 3, 2011 Submission, exhibit 1.) The partners agreed to split in 1996, with Mr. Kozen taking the  
12 Montrose and LAX locations and his partner taking three other locations.<sup>15</sup> (*Id.* at exhibit 2; App. Post-  
13 Conf. Br., exhibit 35.)

14 *Additional Evidence*

15 At the conference, appellant presented evidence not yet in the record.<sup>16</sup> To ensure that  
16 all available records were entered into the record for this appeal, Appeals Division staff instructed  
17 appellant to formally submit the documents provided at the conference and any other documents  
18 appellant believed relevant. In addition to evidence provided prior to the pre-hearing conference (App.  
19 July 15, 2011 Submission, exhibits), appellant provided additional exhibits on August 3, 2011, and with  
20 its post-conference brief on October 3, 2011. These documents are described in the parties' contentions  
21 below.

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25 <sup>15</sup> At this time, it appears that the ground leases for the two locations may have remained in the KP Partnership name. The  
26 next indication of when the ground lease was transferred is a resolution from the Board of Airport Commissioners dated  
27 October 13, 1998, authorizing the transfer of the lease from the partnership to appellant. (App. Aug. 3, 2011 Submission,  
28 exhibit 4.)

<sup>16</sup> The Appeals Division had requested that any additional materials or evidence be provided prior to the conference, to  
enable prior review by the Appeals Division and the other party and facilitate a productive conference.

1           Contentions

2                   Appellant

3                   *Mr. Kozen operated the LAX Burger King franchise*

4                   Appellant contends that it never owned or operated the Burger King restaurant  
5 businesses. Appellant provides the 1991 LAX Burger King Franchise Agreement to show that the  
6 franchise was originally run by the partnership (App. Post-Conf. Br., exhibit 1), a 1996 letter from  
7 Burger King showing the Montrose and LAX Burger Kings were transferred from the partnership to  
8 Mr. Kozen (*Id.* at exhibit 2), and a 2006 letter from Burger King authorizing the assignment of the  
9 LAX Burger King from Mr. Kozen to the Mangen Group. (*Id.* at exhibit 3). Appellant provides a year  
10 2000 annual Administrative Report for the “JK Group Defined Benefit Pension Plan,” listing “JK  
11 Group” as the employer and using the EIN beginning with “95”. (*Id.* at exhibit 6.) Appellant provides  
12 a Workers’ Compensation claim signed May 14, 2003 which lists the employer as “Burger King / JK  
13 Group.” Also provided are a Workers’ Compensation Invoice and letters from 2003 regarding policy  
14 payments. The invoice lists “Burger King” as the insured, one letter is addressed to “policyholder,”  
15 and a second letter is addressed to Mr. Kozen. (*Id.* at exhibit 7.)

16                   Appellant provides letters from utility companies indicating Mr. Kozen was receiving  
17 service at the LAX Burger King location during or at the end of the period in question, a BOE seller’s  
18 permit from 1990, a 1995 letter from the BOE regarding payment methods for sales and use tax, a 2006  
19 BOE letter for escrow purposes, and a June 2006 EDD quarterly wage report all listing either “JK  
20 Group,” Mr. Kozen, or both. (*Id.* at exhibits 11-15, 20-21.) An EDD Certificate of Release of Buyer  
21 dated July 28, 2006, lists “J K Group” as the seller. (*Id.* at exhibit 16.) Appellant provides various  
22 permits active during the years at issue that include Mr. Kozen’s name. (*Id.* at exhibits 22-24.)  
23 Appellant provides JK Group financial statements from January of 2006 and August of 2006 to support  
24 its assertion that JK Group operated the restaurants.<sup>17</sup> (*Id.* at exhibits 25-26.)

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28 <sup>17</sup> Among these documents, appellant provides copies of four checks paid from a “JK Group” account for cleaning services, credit card payments, gas payments, and department of water and power payments. The dates on these checks are mostly illegible, but appear to be dated July of 2006.

1           *Appellant only operated the LAX location ground lease*

2           Appellant states that it was created with the intention to pay the ground lease and collect  
3 rent from the proprietorship that was operating the restaurant businesses. (App. Op. Br., p. 1.)  
4 Appellant provides an excerpt from the LAX Burger King Unit Sale Agreement, apparently relating to  
5 the sale to the Mangen Group in 2006, listing Mr. Kozen as the seller of the franchise and appellant as  
6 the seller of the real property interest. (App. Post-Conf. Br., exhibit 4.) Appellant also provides a Bulk  
7 Sale Certificate from FTB issued for escrow purposes during the sale to the Mangen Group that lists  
8 Mr. Kozen and “JK Group” as the sellers of the LAX Burger King. (*Id.* at exhibit 5.) Appellant  
9 provides an amended 2005 S Corporation return for appellant, which removes all the previously-  
10 recorded income and includes \$30,000 of rental real estate income, indicating that the original return  
11 improperly reported all the income from the sole proprietorship. (*Id.* at exhibit 19.) Appellant provides  
12 a Board of Airport Commissioners resolution dated October 13, 1998, authorizing the transfer of the  
13 LAX Burger King ground lease from the partnership to appellant, noting that the assignment “will have  
14 no effect on the operation of [the] restaurant.” (*Id.* at exhibit 27.) Appellant also provides a second  
15 document assigning the ground lease for the LAX Burger King to the Mangen Group, Inc., in June of  
16 2006, around the time the LAX Burger King was being sold. This document notes that the ground  
17 lease was assigned from the partnership to appellant on October 13, 1998. (*Id.* at exhibit 28; see also  
18 *Id.* at exhibit 29.) Documents from 1998 and 1999 show appellant as a loan holder with AT&T  
19 Commercial Financial Corporation and show the LAX Burger King property listed as collateral. (*Id.* at  
20 exhibits 30-33.) Appellant also provides the property tax bill for the LAX location, listing “JK Group  
21 LLC DBA” as the assessee, and provides a copy of a check for the owed amount sent to the assessor on  
22 the account of “JK Group.”<sup>18</sup> (*Id.* at exhibit 34.)

23           Appellant contends that the stated purpose of engaging in business dealings with Burger  
24 King restaurants listed on its Articles of Organization and Operating Agreement filed with the  
25 Secretary of State is not a binding purpose, and was permissive so as to allow it to conduct any business  
26 regarding Burger King restaurants, if it so chose. (App. Add’l Br., “Summary of Facts and Exhibits,”  
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28 \_\_\_\_\_  
<sup>18</sup> Appellant indicates that “JK Group” paid the bills of appellant because appellant “did not engage in any activities other than holding the ground lease.” (App. Post-Conf. Br., p. 8.)

1 p. 6.) The business purpose of appellant holding the ground lease was to insulate the real property  
2 against the operating business. (App. Post-Conf. Reply Br., p. 6.) Appellant asserts that the Montrose  
3 Burger King was only operated by Mr. Kozen, doing business as JK Group. Appellant asserts that it  
4 had no connection with that restaurant location.<sup>19</sup> Appellant asserts that the two Burger King  
5 franchises were transferred to Mr. Kozen individually and that appellant had no authority to operate the  
6 franchises and, in fact, did not do so. (App. Post-Conf. Br., p. 8.) Appellant contends that Mr. Kozen  
7 could not simply declare through his tax returns that appellant operated the franchises. (App. Post-  
8 Conf. Reply Br., p. 2.) Appellant contends that the reporting of the restaurants under the LLC returns  
9 was due to an accountant's error, was corrected by amended returns, and did not net Mr. Kozen any  
10 gain. (*Id.* at p. 3.) Appellant states that respondent's argument that Mr. Kozen assigned the franchise  
11 to appellant is based on pure speculation and is not true. (*Id.* at p. 7.)

12 *Appellant was erroneously represented as operating the restaurants*

13 Appellant asserts that any prior listing of the restaurant's business income under  
14 appellant's name or EIN was the result of data entry error, tax preparer mistakes, and confusion  
15 between the sole proprietorship (JK Group) and appellant (JK Group, LLC). (App. Add'l Br.,  
16 "Summary of Facts and Exhibits," pp. 3-4; Resp. Op. Br., exhibit N.) Appellant alleges that the  
17 erroneous reporting of the restaurant operations lasted from 1997 through 2000, and, when the error  
18 was discovered, Mr. Kozen dismissed his accountant and hired a new accountant with the instructions  
19 to report the restaurant business as a sole proprietorship. (App. Post-Conf. Reply Br., p. 1.) Appellant  
20 provides a copy of a letter to Intuit, the payroll company used for at least the LAX Burger King, dated  
21 April 19, 2006, near in time to the sale to the Mangen Group, stating that JK Group had requested a  
22 cancellation of payroll services under EIN "33" and another letter from Intuit dated December 14,  
23 2006, terminating services under EIN "95". (*Id.* at exhibits 8 & 10.) Appellant also provides a letter to  
24 the Department of Treasury dated August 4, 2006, explaining that JK Group had erroneously been  
25 using EIN "33" instead of EIN "95". (*Id.* at exhibit 9.) Appellant asserts that these letters show that  
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27  
28 <sup>19</sup> Appellant states that, if respondent prevails on the LAX Burger King issue, and appellant prevails on the Montrose Burger  
King issue, that the LLC fee should be computed on only the LAX location income. Appellant contends that the LAX  
location accounted for approximately 50 percent of the income, but also states that the LAX location's sales likely exceeded  
\$1 million for each year at issue, and thus the fee would still be \$6,000 for each year. (App. Post-Conf. Reply Br., p. 9.)

1 the EIN beginning with “33” had been erroneously used and terminated, in order to correct the error by  
2 Intuit of erroneously using that EIN. (*Id.* at p. 3.) Appellant indicates that it has copious amounts of  
3 evidence which supports the conclusion that Mr. Kozen operated the Burger King restaurant business  
4 as a sole proprietorship since 1991.<sup>20</sup> (App. Add’l Br., p. 2.) Appellant addresses respondent’s  
5 contention that appellant reported the restaurant income for the second half of 2005, after making its  
6 S election, and states that this was an error by Mr. Kozen’s accountant. (App. Post-Conf. Reply Br.,  
7 p. 4.) Appellant also asserts the preprinted sales tax returns and filings by creditors with the Secretary  
8 of State and other agencies listing appellant as the operator or debtor on business transactions are errors  
9 made by the creditors and BOE. (*Id.* at pp. 4-5.)

10 *LLC fee is unconstitutional*

11 Appellant contends that the LLC fee is unconstitutional. Appellant states that the  
12 California Supreme Court concluded that the LLC fee is unconstitutional, and thus Revenue and  
13 Taxation Code (R&TC) section 17942 is invalid. (App. Op. Br.) In its initial briefing (filed prior to  
14 appellant’s current counsel), appellant also argued that respondent committed double taxation on the  
15 Burger King restaurant income by assessing the LLC fees on the income after Mr. Kozen already paid  
16 taxes on the income through his proprietorship.<sup>21</sup> (App. Op. Br; App. Add’l Br.) Appellant does not  
17 contend that the \$800 LLC tax and related penalties and interest should be refunded, and concedes  
18 those amounts. (App. Add’l Br., p. 1.)

19 Respondent

20 *Amount at issue*

21 Respondent asserts that the amount at issue is misrepresented and should be reduced by  
22 the \$800 LLC tax and associated penalties and interest, as conceded by appellant on appeal. (Resp. Op.  
23 Br., pp. 12-14; App. Add’l Br., p. 1; see footnote 3.)

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26 <sup>20</sup> Appellant stated that the evidence is too bulky to submit by mail or fax, but it will bring the documentation to the hearing.  
27 (App. Add’l Br., p. 2.) At the pre-hearing conference, appellant provided additional evidence, as discussed herein, and  
28 appellant submitted additional evidence into the record following the conference, as noted previously.

<sup>21</sup> Appellant has not withdrawn this double-taxation argument, but the focus of briefing and argument following appellant’s  
representation by its current counsel has been on the factual record.

1                    *Appellant operated the Burger King restaurant businesses*

2                    Respondent contends that appellant conducted the Burger King restaurant businesses  
3 during the years on appeal, as supported by the evidence provided in the briefing and described in the  
4 Background section above. Respondent contends that the EDD evidence provided, in conjunction with  
5 the wages reported on Mr. Kozen’s Schedule C forms for 2002 through 2005, show that all wages from  
6 the restaurant business were reported on appellant’s EDD account. (Resp. Add’l Br., pp. 2-3.)  
7 Respondent contends that appellant was formed for the purpose of operating Burger King restaurants,  
8 reported on tax returns that it was doing so, paid the LLC fee for years prior to the years at issue, and  
9 continued to hold itself out to third parties as the entity operating the business but did not pay the LLC  
10 fee for the years at issue. (Resp. Op. Br., pp. 1-2 & 19-20.) Respondent contends that Mr. Kozen  
11 enjoyed the benefits of conducting his business through appellant, including the protection of limited  
12 liability for the debts and obligations of the business, and therefore appellant must bear the  
13 consequences, namely the filing of tax returns and the payment of the annual fee on the income of the  
14 business. (*Id.* at pp. 20-21.) Respondent states that appellant has not provided canceled checks, a  
15 sublease agreement, or any other evidence to support its position that it merely leased the commercial  
16 property to Mr. Kozen and was not involved in the operation of the Burger King restaurant.<sup>22</sup> (Resp.  
17 Op. Br., p. 7.)

18                    Respondent provides documents showing that it contacted Mr. Kozen in January 2005  
19 regarding appellant’s failure to file returns and pay the LLC fee, which predates Mr. Kozen’s request in  
20 2006 to the IRS to change the EIN associated with the business from appellant’s EIN of “33”, which  
21 had been used since 1997, to the EIN “95”. (Resp. Post-Conf. Reply Br., p. 1 & exhibit A.)  
22 Respondent also provides a printout of appellant’s EDD account which shows a comment by an EDD  
23 agent regarding the sale of the Montrose Burger King, indicating appellant was the seller of that  
24 business. (*Id.* at exhibit B.) Respondent asserts that many of appellant’s documents submitted as  
25 exhibits regarding the ownership of the Burger King businesses predate the existence of appellant or  
26 were created after the close of the tax years at issue, and therefore are not convincing. (*Id.* at pp. 2-3.)  
27

28 \_\_\_\_\_  
<sup>22</sup> Appellant subsequently provided a canceled check to show that “JK Group” paid the property tax liability of appellant. The parties should be prepared to discuss this payment arrangement.

1 Respondent contends that the contemporaneous tax documents filed during the years at issue and the  
2 substance of the transaction (i.e., which entity conducted the business) show that appellant operated the  
3 business. (*Id.* at p. 3.) Respondent asserts that it was not informed that appellant had changed its  
4 federal classification to a corporation, effective June 27, 2005, and therefore respondent treated  
5 appellant as a disregarded entity on documents prepared during the sale of the business, explaining why  
6 Mr. Kozen was listed as the seller on the Bulk Sale Certificate and other escrow documents. (*Id.* at  
7 p. 4.) Respondent assert that, as a disregarded entity, appellant would be obligated to report its owner’s  
8 EIN on most federal tax documents, explaining why EIN “95” was used on the retirement plan. (*Id.* at  
9 pp. 4-5.)

#### 10 *Federal Employer Identification Numbers*

11 Respondent asserts that the Federal Insurance Contributions Act (FICA) requires  
12 employers to withhold tax and unemployment tax and obtain an EIN. (Resp. Post-Conf. Br., pp. 2-5.)  
13 Respondent notes that Mr. Kozen was required to acquire an EIN when he first operated the Burger  
14 King restaurants, obtaining the EIN beginning with “95” in 1990, and then beginning the use of EIN  
15 “33” in 1997. (*Id.* at p. 6.) Respondent indicates that the EDD issues its own state employer number  
16 and that the EDD linked its own number, starting with “402”, with EIN “95” in 1994. Respondent  
17 states that the “402” EDD number was later listed under appellant’s account and, in 1997, the EIN “33”  
18 was associated with that EDD number. (*Ibid.*; Resp. Op. Br., exhibit V, p. 1.) Respondent contends  
19 that appellant had to have filed an EDD form 24 in order to affirmatively change the EIN and EDD  
20 number association. (Resp. Post-Conf. Br., p. 6 & exhibit B.) Appellant filed employment and  
21 withholding returns for the Burger King restaurants for all of the years at issue, and the EIN “33” was  
22 obtained by appellant when it became an employer of the Burger King restaurants. (*Id.* at p. 6.)  
23 Respondent asserts that this analysis is consistent with Treasury Regulation section 301.6109-3(h)(2),  
24 IRS Notice 99-6, and Revenue Ruling 2001-61 (situation 1), and that appellant continued to use EIN  
25 “33” after its S election. (*Id.* at p. 7.) Respondent indicates that appellant’s name and EIN are on the  
26 escrow documents for both Burger King locations and that Mr. Kozen didn’t change the EIN to “95”  
27 with the EDD and the IRS for W-2 purposes until 2006. (*Id.* at p. 7 & exhibit D; Resp. Op. Br.,  
28 exhibits K, L.) Respondent asserts that Mr. Kozen had to personally sign federal and state employer

1 identification number requests and withholding returns, and finds it hard to believe that the reporting  
2 was a “mistake” as it persisted for nine years with affirmative actions. (Resp. Post-Conf. Br., p. 8.)

3 *Form 100S*

4 Respondent notes that appellant became an S corporation on June 27, 2005, and filed a  
5 Form 100S which reported that it conducted the Burger King businesses.<sup>23</sup> (Resp. Post-Conf. Br., p. 8  
6 & exhibit E.) Respondent asserts that, if appellant conducted the Burger King businesses for the  
7 second half of 2005, the most likely conclusion is that appellant operated the businesses during the first  
8 half of 2005 and prior as a disregarded single-member LLC, and is therefore subject to the LLC fee.  
9 (*Id.* at pp. 8-9.)

10 *Creditors*

11 Respondent asserts that appellant entered into contractual relationships with suppliers  
12 and lenders of the Burger King Businesses. (Resp. Post-Conf. Br., p. 9.) Respondent notes that  
13 Secretary of State guidelines state that creditors must use their true name and not a trade name, and that  
14 filings during the years at issue name appellant as the debtor for the Burger King business. (*Id.* at  
15 p. 10; Resp. Op. Br., exhibit W.) Respondent therefore contends that appellant legally entered into  
16 contracts with third parties in operating the businesses, and Mr. Kozen received the benefit of LLC  
17 liability protection in the businesses. (Resp. Post-Conf. Br., p. 10.)

18 *State Tax Returns*

19 State sales tax returns were filed under appellant’s name from January 1, 2001, through  
20 June 30, 2005. (Resp. Op. Br., exhibit S.) These returns bear the pre-printed name of appellant from  
21 BOE from January 1, 2001, through December 31, 2004. Respondent notes that seller’s permits were  
22 issued to Mr. Kozen in 1990 and 1994 and that he must have at some point told BOE that appellant was  
23 conducting the businesses and to change the name on the pre-printed returns. Respondent asserts that

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28 <sup>23</sup> Although appellant’s Form 100S states that its primary business is leasing commercial property, it appears to have listed all  
of the sales income from the Burger King businesses on its form. (Resp. Post-Conf. Br., exhibit E, pp. 2-3.)

1 Mr. Kozen was legally required to notify BOE of a change in business ownership, and apparently did.<sup>24</sup>  
2 (Resp. Post-Conf. Br., pp. 10-11.)

3 Respondent contends that sellers reporting sales can use a consolidated report for  
4 multiple locations, if there is the same ownership operating the businesses. (Resp. Post-Conf. Br.,  
5 p. 20.) Respondent asserts that, in this instance, both the LAX and Montrose locations were reported  
6 on a consolidated report and the owner of both locations was appellant. (*Id.* at p. 20 & exhibit H.)  
7 Respondent indicates that Mr. Kozen's Form 1040 includes only one Schedule C reporting all Burger  
8 King income and, therefore, all of the income must have come through one single source, which was  
9 appellant. (*Id.* at pp. 20-21.) Respondent states that the use of appellant's EIN "33" for the sales of the  
10 Burger King franchise businesses shows that appellant operated both locations. (*Id.* at p. 21; Resp. Op.  
11 Br., exhibit K, L.)

12 Respondent asserts that the employment tax returns were filed under appellant's "33"  
13 EIN, and not Mr. Kozen's "95" EIN. (Resp. Post-Conf. Br., p. 21.) Respondent contends that wages  
14 reported on Mr. Kozen's Form 1040 Schedule C roughly match or include all wages reported to the  
15 EDD by appellant. (*Id.* at p. 22; Resp. Op. Br., exhibit R.) Respondent indicates that all wages for both  
16 Burger Kings were reported for federal and state purposes on appellant's EDD account.

17 *LAX Burger King location ground lease*

18 Respondent contends that appellant purposefully limited itself to being a single-purpose  
19 LLC formed only to operate Burger King franchise businesses. (Resp. Post-Conf. Br., p. 12.)  
20 Respondent asserts that limiting appellant's activity to only rental activity is contrary to the self-  
21 asserted limitation. (*Ibid.*) Respondent contends that there is no purpose in having the LLC own and  
22 rent back the property. (*Id.* at p. 13.) Respondent notes that there is no sublease agreement provided,  
23 no economic effect in the alleged arrangement, and no rental income reported on Mr. Kozen's Form  
24 1040 Schedule E. Respondent asserts that the income should have been separately reported and  
25 deducted on the Schedule E or C, reporting the income on the amended Form 568s is inconsistent with  
26

27  
28 <sup>24</sup> Appellant asserts that Mr. Kozen was issued seller's permits, and appellant was never issued seller's permits and therefore  
was not able to conduct the business. Respondent asserts that appellant must have notified BOE of the change in ownership,  
prompting the otherwise unexplained change of the pre-printed name to appellant's name. The parties should discuss how  
appellant's name became the pre-printed name on the returns.

1 the original reporting, and Form 568 is only for net gain from real estate activity. (*Ibid.*) Respondent  
2 asserts that appellant needs to provide a ground lease with LAX including amendments and subleases,  
3 as well as banking records and cancelled checks showing that rent was paid. (*Id.* at pp. 13-14.)

4 *Burger King Franchise Agreement*

5 Respondent contends that the franchise agreement is for the “business method,”  
6 including service marks, etc., and not a goods distribution franchise. (Resp. Post-Conf. Br., p. 14.)  
7 Respondent asserts that the gross receipts were generated by food production and sales, and not the  
8 franchise per se. (*Id.* a p. 15.) Respondent contends that the value of the franchise is the difference  
9 between the income of a franchise versus a non-franchise operation in the same business. In other  
10 words, respondent is arguing that assigning all sales income to the franchise owner misrepresents who  
11 earned the income, and instead a majority of the income should be attributed to the entity selling the  
12 hamburgers (i.e., appellant). Respondent therefore contends that the holder of the franchise is  
13 immaterial and that Mr. Kozen contributed the intangible franchise asset to appellant for appellant’s  
14 use. In support of this contention, respondent notes that appellant deducted the franchise fee and  
15 royalties on its Form 568 for tax years 1997 through 1999, while it was classified as a partnership.  
16 Alternatively, respondent contends that Mr. Kozen may have assigned the franchise to appellant.  
17 Respondent asserts that, despite the clause prohibiting this in the Franchise Agreement, Mr. Kozen may  
18 have breached the contract by the unauthorized assignment, but this does not mean that the entire  
19 Franchise Agreement was void, and the Burger King Corporation may have allowed the assignment  
20 after the fact. (*Ibid.*)

21 *LAX Burger King sale agreement*

22 Respondent addresses the apparent excerpt of the purchase agreement of the LAX  
23 Burger King to the Mangen Group. (Resp. Op. Br., exhibit 2.) Respondent contends that the  
24 agreement is not relevant to what entity conducted the Burger King businesses from January 1, 2001,  
25 through June 26, 2005. (Resp. Post-Conf. Br., p. 16.) Respondent argues that the substance of the  
26 actions during those years overrides the form of the operations as presented by the purchase agreement,  
27 and the representation on the purchase agreement conflicts with the Form 100S filed in 2005.  
28 Respondent also notes that there is no similar sales agreement provided for the Montrose Burger King.

1 (*Ibid.*)

2 *JK Group trade name*

3 Respondent states that the continued use of the “JK Group” trade name for business  
4 dealings is not inconsistent with appellant operating the business. (Resp. Post-Conf. Br., p. 17.)  
5 Respondent references Business and Professions Code sections 17900 through 17930, asserting that a  
6 fictitious business name is acceptable for an LLC. Mr. Kozen filed for the fictitious business name in  
7 1991, and never updated the business name after it expired five years later. (*Id.* at p. 18.) Respondent  
8 asserts, however, that the name may still be used even after the official filing expires, and that use of  
9 the name by Mr. Kozen in some dealings, including prior to appellant’s formation, does not mean  
10 appellant cannot use it. (*Id.* at p. 19.) Respondent asserts that, when entity had to be identified legally  
11 (i.e., UCC filings), the name reported was appellant’s full name. (*Ibid.*) Respondent asserts that  
12 appellant may have acted under its LLC name, its JK Group trade name, Burger King, or its owner’s  
13 name of Mr. Kozen. Therefore, documents provided with only JK Group, Burger King, or Mr. Kozen’s  
14 name are not persuasive in attempting to show that appellant did not operate the Burger King  
15 Businesses. (Resp. Post-Conf. Reply Br., p. 6.)

16 *LLC fee calculation*

17 Respondent asserts that R&TC section 17942 provides for a \$6,000 LLC fee if total  
18 income is \$1 million or more, and less than \$5 million. (Resp. Post-Conf. Br., p. 22.) Respondent  
19 states that it used quarterly sales tax returns to compute gross sales for each year and to get gross  
20 income. (*Id.* at p. 23.) Respondent notes that “total income” also includes non-business income, but  
21 respondent did not include any non-business income in its calculations. Respondent compares the  
22 gross sales for each year per the sales tax returns and Mr. Kozen’s Form 1040 Schedule C. (*Id.* at  
23 p. 24.) Respondent asserts that under either method, total income is greater than \$1 million and less  
24 than \$5 million for each year, and therefore the appropriate LLC fee amount for each year is \$6,000.  
25 (*Id.* at pp. 24-25.)

26 *LLC fee is constitutional as applied here*

27 Respondent notes that appellant never presented the argument that the LLC fee is  
28 unconstitutional on amended returns or claims for refund. (Resp. Op. Br., p.7) Respondent contends

1 that the Board should abstain from deciding the constitutional issue of whether the LLC fee is  
2 unconstitutional as applied in this appeal, in accordance with Article 3, Section 3.5, of the California  
3 Constitution and the Board's own regulations. (Resp. Op. Br., p. 11; see Cal. Code Regs., tit. 18,  
4 § 5412, subd. (b)(1).) While respondent concedes that California appellate courts have held the LLC  
5 fee unconstitutional in limited situations (where the LLC was conducting at least some business outside  
6 of California), the courts have not found the fee to be unconstitutional where the LLC conducted all its  
7 business within California, as is the situation proposed by respondent for the years at issue here. (Resp.  
8 Op. Br., p. 11.)

9           Respondent contends that its assessment of the LLC fee does not constitute a double  
10 taxation on the Burger King restaurant income. (Resp. Add'l Br., pp. 4-6.) Respondent states that even  
11 when a LLC is treated as a disregarded single-owner LLC with all the income passing directly through  
12 to the owner and taxed as a sole proprietorship, the LLC is still required to file a return, pay the LLC  
13 tax, and pay the LLC fee based on the total income that passed through to the owner. (*Id.* at pp. 4-5;  
14 Treas. Reg. § 301.7701-2; Cal. Code Regs. tit. 18, § 23038(b)-2.) Respondent asserts that the LLC fee  
15 is imposed in return for the benefits conveyed to the LLC owner as a cost of conducting business in a  
16 particular legal form, and not for the benefits of being a resident or receiving California source income  
17 as normal income tax is. (Resp. Add'l Br., p. 6.) Respondent states that double taxation only exists  
18 where two taxes of the same character are imposed on the same property for the same purpose, which is  
19 not the case here. (*Ibid.*)

#### 20           Applicable Law

#### 21                   Burden of Proof

22           It is well settled that a presumption of correctness attends respondent's determinations as  
23 to issues of fact and that an appellant has the burden of proving such determinations erroneous.  
24 (*Appeals of Oscar D. and Agatha E. Seltzer*, 80-SBE-154, Jun. 29, 1980.) This presumption is,  
25 however, a rebuttable one and will support a finding only in the absence of sufficient evidence to the  
26 contrary. (*Appeals of Oscar D. and Agatha E. Seltzer, supra.*) Respondent's determinations cannot,  
27 however, be successfully rebutted when the taxpayer fails to provide uncontradicted, credible,  
28 competent, and relevant evidence as to the issues in dispute. (*Appeals of Oscar D. and Agatha E.*

1 *Seltzer, supra.*)

2 LLC Fee

3 California imposes an annual tax on all LLC's, fixed at \$800. (Rev. & Tax. Code,  
4 § 17941, subd. (a).) The annual LLC tax is due on or before the 15th day of the 4th month of the  
5 taxable year, which in this case was April 15 of each year following the taxable year, since appellant  
6 filed its tax returns on a calendar year basis. (Rev. & Tax. Code, § 17941, subd. (c).) California also  
7 imposes an annual fee, based on total income, on those LLC's that elect not to be taxed as corporations.  
8 (Rev. & Tax. Code, § 17942, subd. (a).) The annual LLC fee is due on the original due date of the  
9 LLC's return.<sup>25</sup> (Rev. & Tax. Code, §§ 17942, subd. (c) & 18633.5.)

10 R&TC section 19131, subdivision (a), provides, in pertinent part, that a penalty shall be  
11 imposed if a taxpayer fails to file a return before the regular or extended due date of the return, unless it  
12 is shown that the failure is due to reasonable cause and not willful neglect. R&TC section 19132,  
13 subdivision (a), provides, in pertinent part, that the failure to pay the amount of tax shown on a return  
14 before the regular due date of the tax will result in a penalty, unless it is shown that the failure is due to  
15 reasonable cause and not willful neglect. R&TC section 19172 provides, in pertinent part, that a  
16 penalty shall be imposed upon a limited liability company, which is classified as a partnership, that fails  
17 to file a return by the regular or extended due date of the return, unless it is shown that the failure is due  
18 to reasonable cause.

19 "Double taxation occurs only when two taxes of the same character are imposed on the  
20 same property, for the same purpose, by the same taxing authority within the same jurisdiction during  
21 the same taxing period." (*Associated Home Builders of the Greater East Bay, Inc. v. City of Walnut*  
22 *Creek* (1971) 4 Cal. 3d 633, 642 (*Home Builders*) [internal quotes and citation removed].) In *Home*  
23 *Builders*, the court decided that there was no double taxation when new residents paid for the cost of a  
24 park through both property taxes and increased purchase prices on homes. The court reasoned that for  
25 double taxation to exist, it must meet the elements listed above. (*Ibid.*) California law allows for the  
26 assessment of the LLC tax, LLC fee, and LLC filing requirement even when there is a single-owner  
27

28 <sup>25</sup> Even if a LLC is disregarded for federal tax purposes, it must still file a return, pay the annual tax, and be subject to and pay the annual LLC fee. (Rev. & Tax. Code, § 23038, subd. (b)(2)(B)(iii).)

1 LLC that is an otherwise disregarded entity. (Rev. & Tax. Code, § 23038, subd. (b)(2)(B)(iii); Cal.  
2 Code Regs. tit. 18, § 23038(b)-2(c)(2).)

3 Constitutional Issues

4 Section 3.5 of article III of the California Constitution states in relevant part:

5 An administrative agency, including an administrative agency created by the Constitution  
6 or an initiative statute, has no power (a) [t]o declare a statute unenforceable, or refuse to  
7 enforce a statute, on the basis of it being unconstitutional unless an appellate court has  
8 made a determination that such statute is unconstitutional; (b) [t]o declare a statute  
9 unconstitutional; (c) To declare a statute unenforceable, or to refuse to enforce a statute  
on the basis that federal law or federal regulations prohibit the enforcement of such  
statute unless an appellate court has made a determination that the enforcement of such  
statute is prohibited by federal law or federal regulations.

10 In addition, the Board has a long-established policy of declining to consider constitutional issues. In  
11 the *Appeal of Aimor Corporation* (83-SBE-221), decided on October 26, 1983, the Board stated:

12 This policy is based upon the absence of any specific statutory authority which would  
13 allow the Franchise Tax Board to obtain judicial review of a decision in such cases and  
14 upon our belief that judicial review should be available for questions of constitutional  
importance. Since we cannot decide the remaining issues raised by appellant,  
respondent's action in this matter must be sustained.

15 This policy was in place long before the enactment of article III, section 3.5. As far back as 1930, the  
16 Board stated:

17 It is true that we have occasionally asserted that right [to question the constitutionality of  
18 a statute]. But this has been only under circumstances wherein such action on our part  
was necessary in order to protect the revenues of the state and get the problem before the  
19 Courts . . . . In the instant case, and in all others like it before us, the taxpayers will have  
the opportunity of taking the question to the Courts for decision. . . . It might be argued  
20 that, if the law is plainly unconstitutional, why should taxpayers be put to that trouble and  
expense? However, there is diversity of opinion as to the constitutionality of the Act, and  
21 it seems to us desirable that this controversy should be settled by the Courts, whose  
authority to hold acts of the Legislature invalid cannot be questioned.

22 (*Appeal of Vortex Manufacturing Co.*, 30-SBE-017, Aug. 8, 1930 [internal citations omitted].)

23 STAFF COMMENTS

24 Whether appellant conducted the Burger King restaurant businesses

25 Both parties agree that the main issue before the Board is a factual one; whether  
26 appellant operated the Burger King businesses during the years at issue. Both parties should be  
27 prepared to list and summarize in a concise manner the evidence that supports their conclusion that the  
28 Burger King restaurant businesses were or were not conducted by appellant during the years at issue.

1 Any additional evidence that the parties wish to provide should be submitted in an  
2 organized manner. Due to the necessary time constraints of the Board Hearing, both parties should,  
3 provide any additional evidence at least two weeks prior to the hearing to allow time for the full  
4 consideration of such evidence and ensure a productive hearing that resolves this matter.<sup>26</sup>

5 This matter was pulled from the July 24, 2012 oral hearing calendar to allow appellant  
6 additional time to respond to a Board Member Inquiry. At the time of the writing of this summary, the  
7 response to the inquiry has not been submitted. Therefore, additional evidence may be received by the  
8 Board and parties that is not discussed herein. Staff requests that this response be submitted as soon as  
9 possible.

10 Staff notes that there is conflicting evidence in the record, and appellant bears the  
11 burden of proof. Appellant will want to discuss further the fact that it initially filed returns, under  
12 penalty of perjury, for years preceding the years at issue, that indicated that the Burger King restaurant  
13 was operated by the LLC; then, apparently after being contacted by the FTB, subsequently filed late  
14 returns for the LLC (for the years at issue) that indicated no lease income or income of any nature; and  
15 then, subsequently, after respondent's jeopardy assessment for unpaid taxes became final, filed  
16 amended returns showing rental income of between \$30,000 and \$57,000 for each year. Appellant will  
17 also want to address the trade documents found by respondent, which appear to show appellant  
18 engaging in business with beverage companies and the like. Respondent will want to address the fact  
19 that appellant has submitted documentation, such as permits and Workers' Compensation documents,  
20 that refer to Mr. Kozen or "JK Group", rather than JK Group, LLC, in connection with the business.

21 Burger King operation documents provided by the parties bear combinations of the  
22 names James I. Kozen, JK Group, Burger King, and JK Group, LLC, without a clear pattern. The  
23 parties should address the concern of how to clarify from these documents whether actions were  
24 performed by appellant, a single-member disregarded (for at least a portion of the years at issue) LLC  
25 ran by Mr. Kozen, or Mr. Kozen in his personal capacity, particularly when documents refer only to  
26 ///

27  
28 <sup>26</sup> Evidence exhibits should be sent to: Claudia Madrigal, Appeals Analyst, Board Proceedings Division, State Board of  
Equalization, P.O. Box 942879 MIC:80, Sacramento, California, 94279-0080.

1 JK Group or a Burger King location.<sup>27</sup>

2 Constitutional Issues

3 As noted above, the California Constitution prohibits an administrative agency, such as the  
4 BOE, from ruling on the basis that a California statute is unconstitutional unless an appellate court has  
5 made such a determination. Here, no appellate court has ruled that the LLC fee statute is  
6 unconstitutional as applied to a taxpayer, such as appellant, that did business entirely in California.  
7 Therefore, the Board has no jurisdiction to rule on this basis, and should abstain from considering such  
8 constitutional issues in its determination.

9 Staff notes that in *Ventas Finance I, LLC v. Franchise Tax Board* (2008) 165  
10 Cal.App.4th 1207, cert. den. (2009) 129 S. Ct. 1917, the court ruled that the LLC fee for a company  
11 operating both in and out of California was constitutional to the extent of California-sourced income,  
12 but was unconstitutional to the extent of other income. However, other LLC fee constitutional  
13 litigation is still pending in the California Superior Court. (See *Bakersfield Mall, LLC v. Franchise Tax*  
14 *Board*, San Francisco Superior Court Case No. CGC-07462728, filed April 25, 2007; *CA-Centerside II,*  
15 *LLC v. Franchise Tax Board*, Fresno Superior Court Case No. 10CECG00434, filed February 4, 2010.)  
16 Appeals Division staff notes that appellant's counsel in this appeal is the taxpayers' counsel of record  
17 in both *Bakersfield Mall, supra*, and *CA-Centerside, supra*. If appellant is unsuccessful in this appeal,  
18 it may pursue any constitutional arguments through a refund suit filed in California Superior Court.

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22 JK Group LLC\_jj

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27  
28 <sup>27</sup> Further ambiguity in the actions and obligations of the respective business forms is revealed in the documents. For  
example, appellant provides documents that show appellant was liable for property taxes on the LAX location, yet also shows  
that payments were made from the JK Group banking account, explaining that appellant's debts were paid by JK Group.  
Appellant should explain the intermingling of funds and obligations among the respective business forms.