

BEFORE THE STATE BOARD OF EQUALIZATION  
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of )  
WOODWARD ENTERPRISES, INC. )

For Appellant: Jerry B. Hicks  
Attorney at Law

For Respondent: Crawford H. Thomas  
Chief Counsel

Peter S. Pierson  
Counsel

O P I N I O N

This appeal is made pursuant to section 25667 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Woodward Enterprises, Inc., against a proposed assessment of additional franchise tax in the amount of \$5,290.17 for the income year ended August, 31, 1964.

At the outset, we must dispose of a procedural matter. Appellant has moved to strike the Franchise Tax Board's "Supplemental Memorandum" on the grounds that it does not deny allegations of fact in appellant's reply and thus is not authorized by section 5027 of title 18 of the California Administrative Code. That section provides in part:

The Franchise Tax Board will be allowed to file a supplemental memorandum to deny allegations of fact - in the reply of the appellant if it so desires....

Appellant is quite correct in interpreting this language to mean that a supplemental memorandum not limited to

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denying allegations of fact in the appellant's reply could be improper and subject to a motion to strike, Here, however, respondent's supplemental memorandum deals solely with an argument first made in appellant's reply and which respondent ha-3 no previous opportunity to answer. General principles of fairness, as well as the policy inherent in section 5026<sup>1/</sup> of title 18 of the California Administrative Code, require that the Franchise Tax Board be given the opportunity to answer each and every point urged by the taxpayer as grounds for reversal of that Board's action. Under these circumstances, appellant's motion to strike is denied.

Turning now to the merits of this appeal, appellant is a California corporation which files its franchise tax returns on the basis of a fiscal year ending August 31. On October 29, 1963, appellant sold 1.79 acres of real property under threat of condemnation and on the same day received the proceeds of \$116,350. Appellant's gain on the sale was \$110,850. On its franchise tax return for the fiscal year ended August 31, 1964, appellant elected not to recognize this gain, stating that it would purchase qualified replacement property within the time allowed by Revenue and Taxation Code section 24944. That section provides that, at the election of the taxpayer, the gain from the condemnation of its property shall be recognized only to the extent that the amount realized from the condemnation exceeds the cost of acquiring qualified replacement property, if the replacement property is acquired (1) within one year after the close of the first income year in which any of the gain is realized or (2) before such later date as the Franchise Tax Board may designate pursuant to application by the taxpayer. The section goes on to provide that an application for extension of the replacement period must be filed "at such time and in such manner as the Franchise Tax Board may by regulations prescribe."

In 1966 appellant purchased qualified replacement property at a cost of \$83,302. Since this property

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<sup>1/</sup> 5026. Memoranda to be Filed. After the filing of an appeal is complete, the Franchise Tax Board will be allowed not less than 30 days in which to file a memorandum in support of its position. The appellant will be allowed not less than 30 days thereafter in which to file a reply if he so desires.... [Emphasis added.]

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was purchased after August 31, 1965, it was not acquired within one year after the close of the first income year in which any of the gain was realized. Under the federal counterpart of section 24944, however, appellant applied for and received from the Internal Revenue Service an extension of time in which to acquire replacement property. But because of the oversight of appellant's officers and employees, appellant never filed a similar application with respondent. Respondent might have granted an extension of the replacement period had appellant applied for one. However, since appellant neither replaced the condemned property by August 31, 1965, nor obtained an extension of the replacement period under section 24944, respondent determined that all of the gain (\$110,850) was includible in appellant's income for the year in which the proceeds were received. Appellant admits, as it must, that the determination is correct to the extent of \$33,048, which is the difference between the proceeds from the condemnation and the cost of the replacement property, but claims that it is entitled to nonrecognition of the balance of the gain. (\$77,802).

Appellant's principal argument is based on regulation 24943-24947(b) of the California Administrative Code, which was promulgated on December 22, 1969, subsequent to the filing of this appeal. Appellant contends that this regulation, applies retroactively to the transactions here in question and that under its terms appellant should be treated as if it had applied for and been granted an extension of the replacement period. Appellant relies on subparagraph (3)(C) of the regulation, which provides that an application for extension of the replacement period must be filed prior to expiration of one year after the close of the first income year in which any part of the gain is realized, unless the taxpayer can show to the satisfaction of the Franchise Tax Board: (1) reasonable cause for not having filed the application within the required period of time, and (2) that the application was filed within a reasonable time after the expiration of the required period of time. With respect to these two requirements appellant contends (1) that the oversight of its officers and employees constitutes reasonable cause for not having filed a timely application, and (2) that it should be treated as having filed an application within a reasonable time after the expiration of the required period because delinquent applications were not authorized prior to the time this appeal was filed, and appellant should not now be penalized for having failed to perform a worthless act.

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Respondent contends that the part of regulation 24943-24947(b) upon which appellant relies does not apply to income years beginning before January 1, 1969. In respondent's view, the last sentence in subparagraph (3)(C) of the regulation limits the retroactive effect of all of paragraph (3) and not just that of the grammatical paragraph in which that sentence appears, as argued by appellant. Consequently, the applicable regulation would be former regulation 25035(c) which provides, without exception, that an application for extension of the replacement period must be made prior to the expiration of the first year after the close of the first income year in which any of the gain upon the conversion is realized. Since appellant did not file such an application with respondent at any time, respondent contends that appellant has not qualified for nonrecognition of any of the gain from the conversion of its property.

Although counsel for both parties have directed most of their attention to whether regulation 24943-24947(b) or regulation 25035(c) applies to this appeal, we do not find it necessary to decide that issue because appellant must lose in either case. If regulation 24943-24947(b) were to apply, appellant would lose because it did not have "reasonable cause" for failing to file a timely application for extension of the replacement period. Appellant has cited no authority, and we have found none, which suggests that simple oversight can constitute reasonable cause for failing to file a document within the time required by law. If regulation 25035(c) applies, appellant's failure to file a timely application is fatal because untimely applications are not authorized under any circumstances. Appellant seeks to avoid the clear requirements of regulation 25035(c) by arguing that its failure to file a timely application should be excused for the reasons expressed in the Appeal of Robert M. and Jean W. Brown, Cal. St. Bd. of Equal., decided December 10, 1963. That case is not applicable here, however, because the statute and regulations there involved did not, like section 24944 and regulation 25035(c), specifically define the time and manner of making the election.

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<sup>2/</sup> "This paragraph shall be applicable for income years beginning after December 31, of the year preceding its adoption."

