

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
) No. 91A-0302-JG
WEST VALLEY LAND MANAGEMENT CO.,)
0477600, TAXPAYER, AND MARVIN)
MALMUTH AND EDWIN MALMUTH,)
ASSUMERS AND/OR TRANSFEREES)

For Appellant: Edwin Malmuth
President

For Respondent: A. Jovanovich
Counsel

OPINION

This appeal is made pursuant to section 25666^{1/} of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of appellant West Valley Land Management Co., 0477600, Taxpayer, and Marvin Malmuth and Edwin Malmuth, Assumers and/or Transferees, against a proposed assessment of additional franchise tax in the amount of \$82,104 for the income year ended October 31, 1989.

^{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.

The question presented is whether a tax on income from an installment sale in appellant's last year of operation was correctly proposed.

Appellant, a California corporation, began business in this state September 14, 1964. It elected S corporation status for federal purposes in 1985 and for state purposes in 1987. On July 19, 1989, appellant adopted a plan for complete dissolution. On September 15, 1989, appellant made an installment sale of its major asset and, thereafter, did no business. On September 20, 1989, appellant requested a Tax Clearance Certificate from respondent in furtherance of its dissolution. On December 21, 1989, appellant filed its final return. On that return it did not report any income from the installment sale.

Respondent determined, relying upon section 24672, that the unreported income from the installment sale was required to be included in the measure of appellant's tax. Appellant, on the other hand, reads section 24672 to allow unreported installment sale income to escape taxation in a corporation's final year.

We believe we need not resolve this apparent contradiction because we believe both parties have misapplied the law.

While section 24672 does deal with unreported income on installment obligations in the year of a corporation's dissolution, withdrawal from the state or cessation of business, and while it does contain some rules whereby tax on the income from such obligations may or may not be abated, we do not think it controls the issue in this appeal. Neither party has addressed the impact, if any, of Internal Revenue Code section 453B.

Senate Bill 572 (Stats. 1987, ch. 1139), operative for income years beginning on or after January 1, 1988, added section 24667 to the Revenue and Taxation Code. In relevant part, section 24667 provides: "(a)(1) Installment sales shall be treated in accordance with sections 453 and 453B of the Internal Revenue Code, except as otherwise provided. . . ."

Internal Revenue Code section 453B(h) provides:

If-

- (1) an installment obligation is distributed by an S corporation in a complete liquidation, and
- (2) receipt of the obligation is not treated as payment for the stock by reason of section 453(h)(1),

then, except for purposes of any tax imposed by subchapter S, no gain or loss with respect to the distribution of the obligation shall be recognized by the distributing corporation. Under regulations prescribed by the Secretary, the character of the gain or loss to the shareholder shall be determined in accordance with the principles of section 1366(b).

After inquiry, the respondent takes the position that section 24672 controls in this situation. Its conclusion is based upon the following language in section 24667, subdivision (a)(1), which we have underlined for identification: "Installment sales shall be treated in accordance with sections 453, 453A and 453B of the Internal Revenue Code, except as otherwise provided." The underlined language is said to refer to section 24672, which is described as a specific and mandatory provision regarding unreported income on installment obligations in the year of dissolution.

Such a conclusion makes Internal Revenue Code section 453B, incorporated into California law by section 24667, a nullity - a result not favored in the law. Civil Code section 3541 states: "An interpretation which gives effect is preferred to one which makes void." Section 1858 of the Code of Civil Procedure provides:

In the construction of a statute or instrument, the office of the judge is simply to ascertain and declare what is in terms or in substance contained therein, not to insert what has been omitted, or to omit what has been inserted; and where there are several provisions or particulars, such a construction is, if possible, to be adopted as will give effect to all.

And section 1859 of the Code of Civil Procedure recites:

In the construction of a statute the intention of the Legislature, and in the construction of the instrument the intention of the parties, is to be pursued, if possible; and when a general and particular provision are inconsistent, the latter is paramount to the former. So a particular intent will control a general one that is inconsistent with it.

It cannot be assumed that the Legislature indulges in idle acts. Every statute should be construed with reference to the whole system of law of which it is a part so that all may be harmonized and have effect. (Stafford v. Realty Bond Service Corporation, 39 Cal.2d 797 [249 P.2d 241] (1952).)

It is also a fundamental principle of statutory construction that a new law supersedes an old law on the same subject. (Union League Club v. Johnson, 18 Cal.2d 275 [115 P.2d 425] (1941); Appeal of Borden, Inc., Cal. St. Bd. of Equal., Feb. 3, 1977.)

We believe, therefore, that the better view would give effect to section 24667 and thereby apply the provisions of Internal Revenue Code section 453B to a distribution of installment obligations by an S corporation.

We also note that section 24667 and sections 23800-23810, inclusive, of the Bank and Corporation Tax Law, which authorize California S corporations, were enacted by the same legislation, Senate Bill 572 (Stats. 1987, ch. 1139). There can be little doubt that the Legislature intended to adopt federal treatment for California S corporations. It is presumed that the Legislature knew the existing laws. (Estate of Simpson, 43 Cal.2d 594 [275 P.2d 467] (1954).)

In spite of the above, we believe that respondent's action in this matter must be sustained, although not for the reason respondent states. As previously set forth, Internal Revenue Code section 453B(h) provides in part: "except for purposes of any tax imposed by subchapter S, no gain or loss with respect to the distribution of the obligation shall be recognized by the distributing corporation." (Emphasis supplied.)

Section 23802, subdivision (b)(1), provides for the imposition of a tax at a rate of 2½ percent upon the income of S corporations, and that is the treatment which is reflected in respondent's notice of proposed assessment. The statutory authorization is, however, section 24667, not section 24672.

For the reasons stated, respondent's action in this matter will 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 25667 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of West Valley Land Management Co., 0477600, Taxpayer, and Marvin Malmuth and Edwin Malmuth, Assumers and/or Transferees, against a proposed assessment of additional franchise tax in the amount of \$82,104 for the income year ended October 31, 1989, be and the same is hereby sustained.

Done at Sacramento, California, this 30th day of September, 1993, by the State Board of Equalization, with Board Members Mr. Sherman, Mr. Dronenburg, and Ms. Scott present.

Brad Sherman _____, Chairman

_____, Member

Ernest J. Dronenburg, Jr. _____, Member

Winnie Scott* _____, Member

_____, Member

*For Gray Davis, per Government Code section 7.9