CALIFORNIA FRANCHISE TAX BOARD

Legal Ruling No. 031

June 24, 1958

STATUTE OF LIMITATIONS: EXTENSION OF STATUTE FOR OMISSION FROM GROSS INCOME

Syllabus:

An omission from the payroll factor of the allocation formula is not an omission from gross income under section 25663(c) of the Personal Income Tax Law.

Advice is requested as to whether section 25663(c) can be invoked against Doe Company to extend the time within which assessments can be made to six years. There is no allegation of fraud which would extend the period indefinitely. Two misstatements by the taxpayer for income year 1945 are offered as grounds for applying section 25663(c): (1) The taxpayer subtracted a net loss of its subsidiary from its own income whereas it is contended that consolidation is not allowable. (2) The taxpayer failed to include all salaries in the payroll factor of the allocation formula thus understating the percentage within the State (but the percentage of sales within the State was overstated with the net result that the adjusted average percent is slightly lower than stated in the return).

Since the first suggested ground, if accepted, would not by itself amount to an omission of an amount in excess of 25 percent of gross income, the second suggested ground must also be accepted if section 25663(c) is to be applied. However, the taxpayer's misstatement of the payroll factor of the allocation formula is not such an omission as is covered by section 25663(c).

The section provides for an extended period where "the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return." Gross income is stated in the return at Item 15. Therefore, the omission must occur in one of the items preceding Item 15. Here the alleged omission occurred in Schedule R-1 which is designed for the computation of Item 52.

The allocation formula and the factors included therein constitute a mechanical device to facilitate computation of the portion of net income attributable to business done within the State. The factors have no influence whatever on the computation of gross income. Therefore, it cannot be said that an omission from the payroll factor is an omission from gross income necessary to bring section 25663(c) into operation.

Since the argument as to understatement of the salary factor must fall, there was no omission from gross income in excess of 25 percent and it becomes unnecessary to consider the contention as to deduction of the loss sustained by the subsidiary.