CALIFORNIA FRANCHISE TAX BOARD

Legal Ruling No. 407

July 22, 1977

FILING REQUIREMENTS OF A RECEIVER/TRUSTEE OF A BANKRUPT CORPORATION

Syllabus:

Advice has been requested concerning the liability of a trustee or receiver of a bankrupt corporation for payment of the minimum franchise tax.

Question:

Is a federal trustee or receiver that is liquidating a bankrupt and nonoperating corporation required to file and pay the minimum franchise tax?

Decision:

Yes.

Discussion:

To do business in California, a corporation can be created as an artificial legal entity with those powers permitted by state law. As a creature of statute, a corporation is also subject to state regulation from beginning of legal life to termination of existence.

As part of that regulatory life and for the benefit and protection extended under the law and government of California, a corporation is taxable pursuant to Revenue and Taxation Code Section 23151 for so long as it is "doing business" within the limits of this state. "Doing business" is defined in Revenue and Taxation Code Section 23101 as ". . . actively engaging in any transaction for the purpose of financial or pecuniary gain or profit." This definition is applicable during the entire existence of a corporate entity. It is not limited by or contingent upon the fact a business may be winding up its affairs under the auspices of either court appointed fiduciaries or regularly elected corporate officers.

If a business is being liquidated under the jurisdiction of a federal court, the authority of state taxing bodies to levy a tax upon such an entity is derived from 28 USC § 960 which provides:

> Any officers and agents conducting any business under authority of a United States court shall be subject to all Federal, State and local taxes

> applicable to such business to the same extent as if it were conducted by an individual or corporation. June 25, 1948, c. 646, 62 Stat. 927.

The history of § 960, enacted in 1948, including its predecessor, 28 USC § 124a, shows that its purpose was to prevent receivers and trustees from operating tax free businesses in competition with tax burdened operators of businesses not in receivership or bankruptcy. H.R. Rep, No. 1138, 73rd Cong.2d Sess.

For federal tax purposes, "conducting a business" has been determined to include gradual liquidation of assets during bankruptcy. In In re I. J. Knight Realty Corp., 501 Fed.2d 62 (1974), the court held that 28 USC § 960 was not intended to establish or limit substantive income tax liability. As such, a nonoperating trustee of a bankrupt corporation was responsible for payment of federal taxes on income generated during the liquidation and distribution of the bankrupt estate. Also, in United States v. Sampsell, 266 Fed.2d 631 (1959) (9th Circuit), the court sustained the imposition of tax on income from the liquidation activities of a trustee after examination of the relevant statutes and a finding that the tax law determined the scope of its own applicability.

With regard to the California franchise tax, the phrase "conducting any business" has not been subject to federal judicial interpretation in a liquidation circumstance. In an analogous state corporate liquidation, however, such tax was determined appropriate in Hise v. McColgan, 24 Cal.2d 147 (1944).

The question before the California Supreme Court was whether a corporation in liquidation under state order was "doing business" to be subject to payment of the franchise tax. The Bank and Corporation Franchise Tax Act (Section 5) defined "doing business" as

> . . . actively engaging in any transaction for the purpose of financial or pecuniary gain or profit.

The court held that during the process of liquidation, business transactions (sales, rentals and transfer of assets; collections upon notes and other obligations) were conducted; and

> [w]hile no profit may have been made as that term is usually understood, such factor is not controlling in the definition of the term "doing business"; rather the criterion is whether or not the goal or aim is financial or pecuniary gain [Citation]. It should be clear that the[Building and Loan] commissioner in liquidating . . . [the corporation] was endeavoring to get the best price obtainable for its assets and to conduct its affairs in liquidation to the end that the most financial gain would be realized for its

> creditors and stockholders . . . . It is not necessary to constitute doing business for franchise tax purposes that there be a regular course of business or transactions.

As such, activities in liquidation were embodied in the concept of "doing business" for purposes of franchise tax liability.

Although a federal court would not be bound by the state construction of the California franchise tax law, such interpretation should be entitled to substantial weight. Accordingly, it would appear present application of the franchise tax should be harmonious with the direction provided by the California Supreme Court. "Doing business," as defined by Revenue and Taxation Code Section 23101 and as applied in corporate liquidation by this state's Supreme Court, should be considered synonymous with "conducting a business" under 28 USC § 960.

Consequently, a tax measured by income realized by a nonoperating trustee or receiver during the period of liquidation or receivership should be asserted in favor of the state. Furthermore, if the activities during the period under consideration result in negative income or in a measured tax that is less than the statutory minimum, the provisions of Revenue and Taxation Code Section 23151 still require payment of the minimum tax from every corporation "doing business" within the limits of this state.