

STATE BOARD OF EQUALIZATION
LIMITED LIABILITY COMPANY TAX APPEAL

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BOARD OF EQUALIZATION
STATE OF CALIFORNIA

In the Matter of the Appeal of:) **SUMMARY DECISION**
) **LIMITED LIABILITY COMPANY TAX**
) **APPEAL**
LEGEND PLUS ENTERPRISE, LLC) Case No. 486026
) Adopted:

Representing the Parties:

For Appellant: Reza Jafari
For Respondent: Maria Brosterhous, Tax Counsel
Counsel for the Board of Equalization: Linda Frenklak, Tax Counsel III

This appeal is made pursuant to section 19324 of the Revenue and Taxation Code (R&TC) from the action of the Franchise Tax Board (FTB or respondent) on appellant's protest against a denial of refund in the amount of \$800 for 2005. The issue presented in this appeal is whether appellant was "doing business" in California in 2005 such that appellant is liable for the Limited Liability Company (LLC) annual tax.

FINDINGS AND DISCUSSION

Background

In February 2005, Reza Jafari formed Legend Enterprise, a California LLC, for the purpose of purchasing commercial real property located in Texas. Legend Enterprise remains in active status and continues to pay the California annual tax. Mr. Jafari wished to purchase commercial real property located in Texas. Wachovia Bank was the lender of an assumable loan on the Texas

1 commercial real property and it required Mr. Jafari to form a Delaware LLC as a condition for
2 assuming the loan. In May 2005, Mr. Jafari formed appellant, a single-member LLC organized in
3 Delaware, with the purpose of holding the Texas commercial real property. Appellant subsequently
4 acquired the Texas commercial real property in 2005. Since its establishment, appellant reportedly has
5 been paying fees to Delaware. During 2005, appellant was not registered with the California Secretary
6 of State's Office. The Texas Secretary of State's Office records indicate that as of June 10, 2005,
7 appellant was registered to do business in Texas and Mr. Jafari was listed as appellant's sole managing
8 member.

9 On October 10, 2006, appellant filed a 2005 California LLC return (Form 568), which
10 lists appellant's address in Oceanside, California, and lists Mr. Jafari as its sole member with the same
11 address as appellant's in Oceanside. Appellant (apparently) elected a tax year ending December 31st.¹
12 On its 2005 return, appellant self assessed the annual \$800 LLC tax, and reported zero total income tax
13 and zero fees due. Respondent processed the return and appellant remitted payment of the outstanding
14 tax, penalty and interest on July 2, 2007.² On July 24, 2007, appellant filed a 2005 amended Form 568
15 which reported no annual tax due. In a letter attached to the 2005 amended Form 568, Mr. Jafari
16 requested a refund of the paid 2005 annual tax because appellant was only doing business in Texas in
17 2005 and it was not doing business in California. Respondent treated the 2005 amended return as a
18 claim for refund.³ In a letter dated January 5, 2009, respondent informed appellant that its claim for
19 refund was denied based on respondent's determination that appellant had an office in California and
20 was doing business in California. This appeal followed.

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23 ¹ Nothing in the appeal file indicates that appellant operated on a fiscal year (i.e., a financial year ending on a date other than
24 December 31st). Appellant's California 2005 return does not list a fiscal year.

25 ² The appeal file does not identify the penalty referenced in respondent's opening brief. It appears appellant elected a tax
26 year ending December 31 as the return filed for tax year 2005 does not list a 2005 fiscal year. Thus, appellant's 2005 tax
27 return was due on April 15, 2006. Presumably, the penalty was a late filing penalty imposed pursuant to R&TC section
19172 because appellant failed to file its 2005 return by the April 15, 2006 deadline. (Rev. & Tax. Code, § 18633.5.) The
above-referenced penalty is not an issue in this appeal.

28 ³ Appellant's July 24, 2007, claim for refund was filed within one year of the July 2, 2007 purported overpayment and
therefore is not barred by the statute of limitations set forth in R&TC section 19306. The statute of limitations is not an issue
in this appeal.

1 Contentions

2 Appellant contends that it does not owe the annual LLC tax for 2005 because it was not
3 doing business in California. Appellant asserts that Mr. Jafari established appellant on May 25, 2005,
4 because Wachovia Bank required a Delaware LLC as a condition to purchase the Texas commercial
5 property and assume the loan on that property. Appellant further asserts that it has been paying fees to
6 Delaware. In its Appeal Letter, appellant lists its business address in Austin, Texas, the address of its
7 registered office in Wilmington, Delaware, and the name of the registered agent, The Corporation
8 Trust Company. Appellant attached to the Appeal Letter a certified copy of its Delaware Certificate of
9 Formation dated May 25, 2005 and filed on May 26, 2005, with the Delaware Secretary of State's
10 Office, a copy of a certificate from the Delaware Secretary of State's Office dated June 8, 2005,
11 stating that appellant was in good standing and annual taxes had not yet been assessed, and a copy of
12 appellant's 2008 Delaware LLC Tax Notice for a total balance due of \$604. In its Appeal Letter,
13 appellant states that Legend Enterprise, the California LLC, is active and continues to pay California
14 fees and "[t]he California address, California tax preparer and California resident belong to this entity
15 and following other California entities." Appellant then lists the following California entities: Legend
16 Enterprise LLC, Caspian Enterprise LLC, Dynasty Enterprise LLC, Dynasty One Enterprise LLC,
17 Dynasty Plus Enterprise LLC, Depot Land Enterprise LLC, Greenway Commerce LLC, Baseline
18 Commerce LLC, TIPT Enterprise LLC, BKSA Enterprise LLC, BKWK Enterprise LLC, and BBAG
19 Enterprise LLC.

20 Respondent contends that appellant owed the annual LLC tax for 2005 because it was
21 being managed in California and thus doing business in California. Respondent argues that Mr. Jafari,
22 appellant's sole member and manager, appears to be managing appellant in California based on the
23 fact that the 2005 return lists both appellant and Mr. Jafari with the same California address, and
24 appellant's tax preparer for its 2005 return was located in California. Respondent relies on the *Appeal*
25 *of Reno Liquor Co., Inc.*, 59-SBE-004, which this Board decided on February 17, 1959, for the
26 proposition that the "management of a corporation within California, even of property or a business
27 principally located or operated outside of California, is considered to be 'doing business' in California.
28 Respondent asserts in that case, this Board determined that the taxpayer corporation was doing

1 business in California because it was carrying on minimal management activities in California based
2 on its warehouse operation in Nevada and its management office was in California.

3 Discussion

4 Burden of Proof

5 The FTB’s determination of tax is presumed to be correct, and a taxpayer has the
6 burden of proving error. (*Todd v. McColgan* (1949) 89 Cal.App.2d 509; *Appeal of Aaron and Eloise*
7 *Magidow*, 82-SBE-274, Nov. 17, 1982.)⁴ Unsupported assertions are not sufficient to satisfy a
8 taxpayer’s burden of proof. (*Appeal of Aaron and Eloise Magidow, supra.*)

9 Annual Tax

10 R&TC section 17941, subdivision (a), imposes an annual tax in the amount of \$800 on
11 all LLC’s that are “doing business” (as defined in R&TC section 23101) in California. R&TC section
12 23101 defines “doing business” as “actively engaging in any transaction for the purpose of financial or
13 pecuniary gain or profit.” The regulations under section 23101 elaborate on that definition, stating that
14 “doing business” includes such things as “liquidating activities consisting of sales, rentals, collections
15 on notes, etc.” (Cal. Code Regs., tit. 18, § 23101, subd. (a).) However, “doing business” does not
16 include “the mere receipt of dividends and interest” and the distribution of such income to
17 shareholders. (Cal. Code Regs., tit. 18, § 23101, subd. (b).)

18 In *Golden State Theatre & Realty Corp. v. Johnson* (1943) 21 Cal.2d 493 (*Golden State*
19 *Theatre & Realty Corp.*), the taxpayer contended that it was not “actively” engaged in any transaction
20 for financial gain (and thus not “doing business”) because it merely acquired property and derived
21 income therefrom, and none of the transactions occurred regularly. The California Supreme Court
22 disagreed, stating:

23 The doing of business, however, does not necessarily mean a regular course of business
24 under the [predecessor to section 23101], for by its plain terms a corporation is doing
25 business if it actively engages in any transaction for pecuniary gain or profit. [The
26 taxpayer] would identify “doing business” with “carrying on a trade or business.” A
27 series of transactions regularly engaged in may be necessary to establish the “carrying on
of a trade or business” but the Legislature made it clear that it had no such concept in
mind when it referred to transaction in the singular as “any transaction.” The word
“actively” must therefore be interpreted as the opposite of passively or inactively, and as

28 ⁴ Board of Equalization cases are generally available for viewing on the Board’s website (www.boe.ca.gov).

1 used in [the predecessor to section 23101] it means active participation in any transaction
2 for pecuniary gain or profit. Within this meaning [the taxpayer] was doing business in
3 1936.

4 (*Id.* at p. 496.)

5 In *Carson Estate Co. v. McColgan* (1943) 21 Cal.2d 516 (*Carson Estate Co*), the
6 California Supreme Court held that a corporation was doing business in California when it made a
7 purchase of bonds in one year, a sale of bonds in the following year, 12 purchases and sales of stock in
8 the year thereafter and 2 such transactions in the last year that was considered. Thus, a single purchase
9 of bonds in one year constituted “doing business.” (See also *People v. Alexander Goldstein Co.* (1944)
10 66 Cal.App.2d 771, 774 (the taxpayer’s purchase and sale of stocks and bonds during each of said years
11 constitute activity in the doing of business, as defined by the statute, which renders the defendant liable
12 for franchise taxes.) Also, a transaction does not need to result in actual profit for purposes of R&TC
13 section 23101, and the relevant inquiry is whether the activity or transaction was motivated by financial
14 or pecuniary gain. (*Hise v. McColgan* (1944) 24 Cal.2d 147, 150-151; *Appeal of Columbia Supply Co.*,
15 60-SBE-012 (June 9, 1960).) Moreover, to constitute “doing business,” it is not necessary that there be
16 a regular course of business or transactions. (*Hise v. McColgan, supra*, 24 Cal.2d at p. 151.)

17 In a member-managed LLC, every member of an LLC has a right to participate in its
18 management and every member is an agent of the LLC for conducting the usual business of the LLC,
19 unless the articles of organization or operating agreement restrict the scope of the agent’s authority.
20 (Corp. Code, §§ 17150, 17157.) A non-member may become an agent through precedent
21 authorization or ratification by the LLC’s members-managers. (Civ. Code, § 2307.)

22 Whether appellant was doing business in California in 2005 depends on its activities
23 during that year. The record shows that appellant engaged in the following transactions in 2005:
24 appellant assumed a loan from Wachovia Bank and purchased Texas commercial property. It is
25 undisputed that appellant’s sole member and manager, Mr. Jafari, was a California resident during tax
26 year 2005, and appellant’s 2005 return lists the same Oceanside address for appellant and Mr. Jafari
27 and a California address for the firm that prepared appellant’s return. This Board has held that
28 conducting negotiations preparatory to the execution of a formal agreement is sufficient for purposes
of “doing business.” (*Appeal of Kleefeld & Son Construction Co., Inc. and Don Ja Ran Construction*

1 Co., Inc., 60-SBE-013, June 9, 1960.) Thus, appellant would be held to have done business in
2 California in 2005 if it engaged in acts related to the purchase of the Texas commercial property while
3 its sole member acted on its behalf in California. Any action that appellant's sole member took on
4 behalf of appellant for financial gain is attributable to appellant; if any such action was taken in
5 California, then appellant was doing business in California. The purchase within California of such
6 things as real property would constitute doing business in California. In addition, performing
7 managerial functions in California constitutes doing business in this state.

8 During 2005, appellant, as borrower, entered into a loan transaction with Wachovia
9 Bank and purchased commercial property in Texas during 2005. In regards to appellant's property
10 being located in Texas, it is not where property is located that is most germane, but where the activity
11 of the business that owns that property occurred. It is difficult to imagine that Mr. Jafari conducted no
12 business on appellant's behalf or performed no management functions during 2005. Appellant has not
13 alleged, and has provided no evidence to indicate, that its sole member and manager left California
14 whenever conducting appellant's business. Furthermore, appellant's 2005 return shows that it was
15 prepared by a firm located in Del Mar, California. Based on the evidence in the record, we conclude
16 that, with appellant's sole member and manager being a California resident, some activities related to
17 appellant's assumption of the loan from Wachovia Bank and the purchase of the Texas commercial
18 property occurred in California. Under the California Supreme Court's decisions in *Carson Estate*
19 *Co., supra*, and *Golden State Theatre & Realty Corp., supra*, those activities are sufficient to constitute
20 "doing business" for purposes of R&TC section 23101. It is readily apparent that the term "doing
21 business," as defined by R&TC section 23101 and its predecessors, has been construed broadly. With
22 that broad construction in mind, we conclude that appellant was "doing business" in California in 2005
23 and, accordingly, it was subject to the LLC annual tax.

24 CONCLUSION

25 For the foregoing reasons, respondent's action is sustained.

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28 Legend Plus Enterprise, LLC_if