

California's First MIC Appeal Decided in Favor of Taxpayer

By Chris Micheli, Michael D. Herbert & Jeffrey M. Vesely

The California State Board of Equalization (BOE) has issued its first decision involving an appeal on claiming the manufacturers' investment credit (MIC). The BOE held that a retailer, Save Mart Supermarkets, could successfully claim the MIC.

On August 14, 2001, the BOE ruled in a 4-0 decision for Save Mart Supermarkets, a Modesto, California-headquartered company. The three authors represented the taxpayer. No written opinion was issued in the case. Rather, the five-member Board acted upon the taxpayer's petition at its hearing in San Diego.

The BOE decision concerned whether Save Mart is a qualified taxpayer under California Revenue & Taxation Code Section 23649. Save Mart successfully argued that the Franchise Tax Board was denying its MIC claim solely because both its meat processing operations and bakery operations are located in the same facility as its retail stores.

The FTB conceded that Save Mart would be eligible for the MIC if Save Mart, using the same manufacturing equipment and employees, instead had conducted its meat processing and bakery operations at separate, stand-alone locations. Save Mart argued that it is a qualified taxpayer under the literal terms and plain meaning of the MIC statute because Save Mart's bakery and meat processing operations are "described in" the manufacturing section of the Standard Industrial Code (SIC) Manual (i.e., Division D). Save Mart asked the BOE to invalidate the Qualified Taxpayer portion of the FTB's MIC Regulation.

The FTB staff counsel agreed that the "MIC statute should be liberally construed in favor of the taxpayer." Nonetheless, the FTB argued that the "primary activity" of Save Mart is retail and that it should be assigned SIC Code 5411. Being "described in" a Division D SIC Code was not sufficient under the FTB's MIC regulation.

Save Mart argued in the alternative that, even if FTB Regulation 23649-3(b) is valid, Save Mart is a qualified taxpayer because it satisfied the three requirements under Reg. 23649-3(b)(1)(B) regarding multiple activities at a single physical location: (1) The activities at each store were not described in a single industry description in the SIC Manual; (2) for each activity, the taxpayer prepared separate reports on the number of employees, their wages and salaries, sales or receipts and other financial data; and (3) the taxpayer's employment in its manufacturing activities was "significant" under a test of facts and circumstances.

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