State of California

Board of Equalization
Legal Division (MIC:82)

M e m o r a n d u m

135.0275

To: Audit Evaluation and Planning Section
(James Black)

Date: April 18, 1989

From: E. L. Sorensen, Jr.

Subject: [B]
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As requested, this is in response to your question regarding the liability of the subject taxpayer for California use tax.

California Constitution Article XIII, section 28, provides for an annual gross premiums tax on insurers which (with few exceptions not pertinent here), is "in lieu" of all other taxes on insurers and their property. Our Regulation 1567, as it pertains to insurance companies, is based on this "in lieu" concept.

Revenue and Taxation Code Sections 12001 – 13170 pertain to the taxation of insurers and, among other things, require such insurers to file tax returns and report gross premiums taxes to the Insurance Commissioner and the Board.

The term "insurer", as used in the Constitution and Revenue and Taxation Code includes:

> "… insurance companies or associations and reciprocal or interinsurance exchanges together with their corporate or other attorneys in fact considered as a single unit, and the State Compensation Insurance Fund. As used in this paragraph, 'companies' includes persons, partnerships, joint stock associations, companies and corporations."

(Cal. Const. Art. XIII §28a; Rev. & Tax Code §12003.)

The term "insurer" is defined in the Insurance Code as "the person who undertakes to indemnify another by insurance…" (Ins. Code §23). "Insurance" is defined as "… a contract whereby one undertakes to indemnify another against loss, damage, or liability arising from a contingent or unknown event." (Ins. Code §22). In order to transact insurance business in California an insurer must be "admitted" (Ins. Code §24); and, a precondition to admission, is the obtaining of a "Certificate of Authority" from the Insurance Commissioner (Ins. Code §700).

[B] is not an admitted insurer and is not entitled to transact the business of insurance in California under the foregoing definitions (See California Physicians's Service v. Garrison, 28 Cal. 2d 790). Because it is not an insurer, it also does not file tax returns with the Commissioner and Board nor pay gross premiums tax.

[B] is a "nonprofit hospital service corporation" under Chapter 11A, Division 2, Part 2 (§§11491-11517) of the Insurance Code. As such, it operates pursuant to a "Certificate of Authority" dated July 1, 1982, issued by the Insurance Commissioner pursuant to Insurance Code Section 11520.5 which limits its activities to the business of operating a hospital service plan for rendering hospital services to its subscribers (See Certification No 3984, attached.) Insurance Code Section 11493.5 provides for an exemption from taxes for nonprofit hospital services corporations, such as [B], by providing:

> "Every nonprofit hospital service corporation organized or admitted under this chapter is hereby declared to be a charitable and benevolent institution and all of its funds and assets shall be exempt from all and every state, county, district, municipal and school tax and other levies other than taxes on real estate and office equipment. The provisions of this section prohibit the imposition of a tax on the transfer of tangible assets to a nonprofit hospital service plan, licensed on or after July 1, 1982, under chapter 11a (commencing with Section 11491) of Part 2 of Division 2, from another nonprofit hospital service plan. This prohibition is applicable only to transfers conclude before January 1, 1983.
>
> The amendments to this section made at the 1983-84 Regular Session of the Legislature do not constitute a change in, but are declaratory of, existing law." (Emphasis added.)

The seminal case construing section 11493.5 is Hospital Service of California v. Oakland, 25 Cal. App. 3d 402. That case, which involved a predecessor corporation to [B], upheld a city utility user's tax on grounds that such a tax was an excise tax outside the scope of the exemption language in the statute. The court pointed out that the corporation, consistent with the court's interpretation, had voluntarily and properly subjected itself to the use tax (also an excise tax) imposed under Revenue and Taxation Code Section 6201-6207.

The Hospital Service of Calif. case was decided prior to the addition of amending language to Section 11493.5 during the 1983-84 legislative session (See, underlined portions of statute above). The amending language was designed to cover the transfer of assets between [B] and another hospital service plan which was consummated between July 1, 1982 and January 1, 1983. It does not affect the application of use tax to transfers other than the specific transfer alluded to, i.e., the Hospital Service of Calif. case rule of taxability is still good law.

Based on the foregoing, we conclude [B] is not an insurer subject to "in lieu" limitations of the Constitution. Rather, [B] is a nonprofit hospital corporation and is subject to use tax.

ELS:jb