



BEFORE THE STATE BOARD OF EQUALIZATION  
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of )  
J. D. AND A. B. SPRECKELS INVESTMENT COMPANY )

Appearances:

For Appellant: Chester H. Stow, Assistant Secretary of  
Appellant Corporation  
For Respondent: Chas. J. McColgen, Franchise Tax Commissione

O P I N I O N

This is an appeal pursuant to Section 25 of the Bank and Corporation Franchise Tax Act (Chap. 13, Stats. 1929, as amended) from the action of the Franchise Tax Commissioner, in overruling the protest of J. D. and A. B. Spreckels Investment Company, a corporation, to a proposed assessment of an additional tax in the amount of \$11,019.78 for the year 1931 based upon its return for the year ended December 31, 1930.

The problems involved in this appeal are whether the following should be deducted from gross income in arriving at net income of Appellant for the year ended December 31, 1930:

- (1) An item of \$782,766.06, which, it is alleged, represents the amount of a loss sustained by Appellant during said year as a result of a sale by Appellant to the J. D. and A. B. Spreckels Securities Company of an account with the Mission Beach Company;
- (2) An item of \$378,498.36 which allegedly represents the amount of a loss sustained by Appellant during said year as a result of the sale by Appellant to the above mentioned Securities Company of twenty-five thousand shares of stock of the Spreckels Sugar Company; and
- (3) An item of \$7,283.63 representing income taxes paid to the Philippine Islands during said year.

First. It appears that on November 30, 1928, Appellant acquired an account with the Mission Beach Company, an affiliated corporation, at a cost of \$995,741.83, the amount of the balance due on the account at that date. Subsequent advances made by Appellant to the Mission Beach Company during the latter part of 1928 and during 1929 and 1930 increased the balance due to \$1,429,244.30. During 1930 Appellant transferred the account to the J. D. and A. B. Spreckels Securities Company for the sum of \$250,000. In its return for the year ended December 31, 1930, Appellant deducted as a loss the difference between the balance due and the amount for which the account was transferred. The Commissioner disallowed the deduction on the grounds that there

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had not been a bonafide sale of the account for its full value.

It appears that the entire stock of Appellant and of the Securities Company are held by the **same individuals** in the same proportions. Under these circumstances, it would seem that, insofar as the stockholders are concerned, it made but little difference whether the account was held by the Appellant or by the Securities Company, and likewise it would seem that the amount for which the account was transferred,, whether for its full value or for a lesser amount, was of but little concern to them.

It also appears that in prior years, the Appellant and the Securities Company filed consolidated returns, but for the year 1930 each company filed separate returns for no apparent reason other than to enable the Appellant to claim a loss on the transfer of the Mission Beach account,

In view of these circumstances and in the absence of a showing on the part of the Appellant that the financial condition of the Mission Beach Company was such that the account was actually not worth any more than the amount for which it was transferred, we are of the opinion that we would not be warranted in holding that the Commissioner acted wrongfully in disallowing the deduction in question.

Second. During the year 1930, Appellant transferred to the Securities Company twenty-five thousand shares of stock of the Spreckels Sugar Company for \$3,741,509.60. The stock so transferred was acquired prior to January 1, 1928 at a cost of \$5,895,894.21. In the return filed for Federal income tax purposes for the year ended December 31, 1930, the difference between the cost of the stock and the amount for which it was transferred was deducted as a loss. In the return filed under the Act for the year ended December 31, 1930, no loss whatsoever was claimed on account of the transfer. However, when the Commissioner proposed the additional assessment in question as a result of disallowing the loss claimed on account of the transfer of the Mission Beach account, Appellant contended that it was entitled to deduct as a loss on the transfer of the stock the sum of \$378,498.36, and that the failure to deduct such loss in its return was due to an oversight. This figure was arrived at by taking the difference between \$4,120,007.96, which Appellant claims was the fair market value of the stock on January 1, 1928 and the amount for which the stock was transferred in 1930.

Section 19 of the Act, as it read during the year for which the additional assessment in question was proposed, provided that the basis for determining gain or loss in the case of the sale or other disposition of property acquired prior to January 1, 1928 should be the fair market value thereof as of said date. In view of this provision, it is clear that in the case of property acquired prior to January 1, 1928 only the difference between the January 1, 1928 value and the selling price may be deducted as a loss even though the cost might be greater than the January 1, 1928 value (See U.S. v. Flannery, 268 U. S. 98, and McCaughn v. Ludington, 268 U. S. 106).

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The only evidence submitted by Appellant as to the fair market value of the stock on January 1, 1928 is the consolidated balance sheet of the Spreckels Sugar Company and certain affiliated corporations as of December 31, 1927. This evidence, we think, is obviously not competent to establish conclusively the amount a willing buyer would have paid for stock of the Spreckels Sugar Company on January 1, 1928. Furthermore, it would seem that the observations made above concerning the transfer of the Mission Beach account are also applicable to the transfer of the stock. Consequently, we must conclude that Appellant has not established that it was entitled to deduct any amount as a loss on account of the transfer in question.

Third. Appellant claims that it was entitled to deduct from gross income for the year 1930 in arriving at net income for that year income taxes in the amount of \$7,283.63 paid to the Philippine Islands.

Section 8(c) of the Act, as it read during the year for which the additional assessment in question was proposed, provides that no deduction should be allowed for taxes *on* income or profits imposed by the authority of (1) any foreign country, and (2) any state, territory, county, city and county, school district, municipality, or other taxing subdivision of any state or territory.

Appellant contends that the Philippine Islands are neither a foreign country nor are they a state or territory and that consequently, the deduction of income taxes paid to the Philippine Islands is not prohibited by the above provision. This contention is clearly without merit inasmuch as the Philippine Islands are unquestionably territory of the United States. If any authority were needed for this statement, it could be found in the following cases:

Fourteen Diamond Rings v. U. S. 183 U. S. 176.  
In re Shoop 41 Philippines 213, 216.  
Cunard Steamship Co. Ltd. v. Mellon 262 U. S. 100,  
27 A. L. R. 1306  
Dorr v. U. S. 195 U. S. 138.

For the above reasons, we conclude that the Appellant was not entitled to the deductions claimed and that the Commissioner acted properly in proposing the additional assessment in question.

O R D E R

Pursuant to the views expressed in the opinion of the Board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, that the action of Charles J. McColgan, Franchise Tax Commissioner, in overruling the protest of J. D. and A. B. Spreckels Investment Company, a corporation, against a proposed assessment of an additional tax in the amount of \$11,019.78 for the year 1931, based upon the

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return of said corporation for the year ended December 31, 1930, pursuant to Chapter 13, Statutes of 1929, as amended, be and the same is hereby sustained.

Done at Sacramento, California, this 17th day of May, 1934, by the State Board of Equalization.

R. E. Collins, Chairman  
Fred E. Stewart, Member  
Jno, C. Corbett, Member  
H. G. Cattell, Member

ATTEST: Dixwell L. Pierce, Secretary