BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
TIDINGS PUBLISHING COMPANY)

Appearances:

For Appellant: George Andre, its Attorney

For Respondent: Chas. J. McColgan, Franchise Tax Commissioner

O P I N I O N

This is an appeal pursuant to Section 27 of the Bank and Corporation Franchise Tax Act (Chapter 13, Statutes of 1929, as amended) from the action of the Franchise Tax Commissioner in denying the claim of the Tidings Publishing Company for a refund of tax in the amount of $166.59 paid pursuant to an assessment of deficiency tax levied against the company by the Commissioner based upon its return of income for the year ended December 31, 1932.

The Appellant is a California corporation, organized in 1904, and has been continuously engaged in the publication of a weekly religious newspaper which is the official organ of the Roman Catholic Bishop of the Diocese of Los Angeles and San Diego The newspaper is circulated partially through mail subscriptions and partially through Sunday sales at Catholic churches *in* Southern California.

A large part of the Appellant's income is derived from two years' subscriptions received from individuals. In order to maintain, or, perhaps, to increase, its circulation, Appellant has found it necessary to conduct circulation drives or campaigns about every two years. A circulation drive held in 1929 increase subscriptions from 8,217 on January 1, 1929, to 14,904 on June 30 1929, and the circulation drive of 1931, which is involved in this appeal, increased circulation from 6,185 on January 1, 1931, to 12,587 on May 1, 1931. The increased circulation resulting from the 1931 drive was attributable largely to renewal subscriptions although a few new subscriptions were also obtained.

The entire two years' subscription price is collected at the time of the signing of the two years' subscriptions. The circulation drive conducted in 1931 resulted in cash collections of approximately $32,000 and costs of $18,910.90. The Appellant filed its returns of income for the years 1931 and 1932 on the accrual basis, allocating for each year one-half of such collections and one-half of such costs to income and expense, respectively. The Commissioner allowed the deferring of one-half of the collections until 1932, but disallowed the deduction of one-half of the circulation drive costs, $9,455.45, reported as an expense for the year 1932. The validity of the action of the Commissioner in disallowing this expense item is the sole question presented by the appeal. The only contention advanced by the Commissioner in support of his action is that the circulation drive expense constituted a capital expenditure and was not, therefor, deductible as an ordinary and necessary business expense for the year.

Expenses incurred in connection with newspaper or periodical circulations are of two general types: (1) the cost of building up the circulation; (2) the cost of maintaining the circulation which is already in existence. The circulation structure is regarded as an asset which must be continually supported by bringing in new subscriptions to replace those which are continually expiring. The cost of so supporting the circulation structure is an ordinary and necessary business expense, but the cost of building up or establishing a circulation structure is a capital expenditure. Gardner Printing Co. (1926) 4 B.T.A. 37; Successful Farming Publishing Co. v. Commissioner (1931) 23 B.T.A. 150, aff'd sub nom. Meredith Publishing Co. v. Commissioner(1933) 64 F. (2d) 890; The Reuben H. Donnelley Corporation v. Commissioner (1932) 26 B.T.A. 107; Perkins Bros. Co. v. Commissioner (1935) 78 F. (2d) 152. See also Houston Natural Gas Corporation v. Commissioner (1936) 34 B.T.A. 228.

The question whether the expense of a particular drive is chargeable to current expense or to capital is, accordingly, essentially one of fact. In our opinion, Appellant's circulation drive of 1931 was conducted primarily to maintain rather than to increase the circulation structure. At the beginning of 1929 there were 8,217 subscribers, whereas at the beginning of 1931 there were but 6,185 subscribers; at the end of the 1929 drive there were 14,904 subscribers, whereas at the end of the 1931 drive there were but 12,587 subscribers, a loss for the two year period of 2,317 subscribers. It is also to be noted that the period was one in which activity was being devoted in practically all lines of business primarily to retaining existing business or minimizing losses of business, rather than to expansion.

While it may be true that the result obtained through the circulation drive and its expenditures does not conclusively establish the character of the expenditures (Perkins Bros. Co. v. Commissioner (1935) 78 F. (2d) 152), the facts and circumstances of this case compel, in our opinion, the conclusion that the circulation drive conducted by Appellant in 1931 constituted an effort to maintain the already existing circulation structure of the newspaper and that the expense of that drive, accordingly, are deductible as ordinary and necessary business expenses.

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 Chas. J. McColgan, Franchise Tax Commissioner, in denying the claim of the Tidings Publishing Company for a refund in the amount of $166.59, said amount having been paid as a tax for the year ended December 31, 1933, based-upon the return of income of said company for the preceding year, be and the same is hereby reversed, The Commissioner is hereby directed to refund to or to give the Tidings Publishing Company credit for said amount of $166.59 paid by said company for said year and otherwise to proceed in conformity with this order.

Done at Sacramento, California, this 16th day of December, 1936, by the State Board of Equalization.

R. E. Collins, Chairman
Ray L. Riley, Member
Ray Edgar, Member

ATTEST: Dixwell L. Pierce, Secretary