



BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
DUNNING PROCESS COMPANY)

Appearances:

For Appellant: Carroll H. Dunning, its President; S. J. McConnell, Certified Public accountant
For Respondent: W. M. Walsh, Assistant Franchise Tax Commissioner; Frank M. Keesling, Franchise Tax Counsel; Clyde Bondeson, Senior Franchise Tax Auditor

O P I N I O N

This appeal is made pursuant to Section 25 of the Bank and Corporation Franchise Tax Act (Chapter 13, Statutes of 1929, as amended) from the action of the Franchise Tax Commissioner in overruling the protest of the Dunning Process Company to his proposed assessment of additional tax in the amount of \$92.12 for the taxable year ended December 31, 1937, based upon the income of the company for the year ended December 31, 1936.

In its return of income for the year 1936 the Appellant claimed a deduction for 'salaries paid to two of its officers', Mr. Carroll H. Dunning and Mr. Dodge Dunning, President and Vice-President, respectively, in the amount of \$10 500 for each officer. The Commissioner allowed a deduction of \$9,000 for each officer, disallowed the balance and on the basis of that action levied his proposed assessment. The propriety of his action in disallowing the deduction for each salary to the extent of \$1,500 is the sole question-presented by this appeal.

The Appellant, a closely held corporation; maintains a technical motion picture studio and laboratory, its business for many years consisting principally of the creating of "composite" motion picture situations for the larger picture studios. In recent years its scientific activities have been conducted in the field of color motion picture photography. Mr. Carroll H. and Mr. Dodge Dunning devoted their entire time to Appellant's operations, which are based upon the scientific and technical knowledge possessed by those officers. Appellant generally has from ten to twelve employees. It has never paid any dividends.

Mr. Carroll H. Dunning has been engaged in technical work in the motion picture business since 1916, his services to Appellant being those of an executive engineer. The compensation paid to him for similar services performed for another corporation prior to his employment by Appellant was at no time less than \$15,000 a year. Other corporations during the year here in

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question paid salaries varying from \$15,000 to \$50,000 a year to employees performing services comparable to those performed by him. He testified that he could have obtained other employment during the year at a salary of \$25,000.

The services rendered to Appellant by Mr. Dodge Dunning during 1936 were, in part, those of a first cameraman. The minimum wage established by the Union of which he was a member, Local Number 659 of the International Alliance of Theatrical Stage Employees, for a first cameraman was \$54.45 per day or \$272.25 per week. First cameramen possessing the same degree of technical knowledge and proficiency as Mr. Dunning receive salaries varying from that minimum to \$700 a week. He also devoted a considerable portion of his time to the technical study of color motion picture photography, a highly specialized subject requiring a high order of scientific and technical knowledge.

Section 8(a) of the Bank and Corporation Franchise Tax Act authorizes a deduction from gross income of "...a reasonable allowance for salaries or other compensation for personal services actually rendered..." The facts hereinabove set forth respecting the character of the services rendered by Mr. Carroll H. and Mr. Dodge Dunning, the specialized nature of the business conducted by Appellant and the position and experience of these individuals in that business, and the prevailing rate of compensation for comparable services rendered to other firms establish in our opinion, that the salary deduction claimed by Appellant in its return of income was not unreasonable. We are mindful of the fact that in prior years when Appellant's earnings were lower than those of 1936, the salaries paid to those officers were much lower than those paid in that year, but believe nevertheless that the entire amount deducted as salaries for 1936 represented reasonable compensation for the services performed by them and that such amount did not constitute, in part, a distribution to them of profits. The action of the Commissioner on the Appellant's protest to his proposed assessment of additional tax is, therefore, overruled.

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 Hon. Chas. J. McColgan, Franchise Tax Commissioner, in overruling the protest of the Dunning Process Company to his proposed assessment of additional tax in the amount of \$92.12 for the taxable year ended December 31, 1937, based upon the income of the company for the year ended December 31, 1936, be and the same is hereby reversed. Said ruling is hereby set aside and the Commissioner is hereby directed to proceed in conformity with this order.

Done at Sacramento, California, this 26th day of September, 1939, by the State Board of Equalization.

R. E. Collins, Chairman

Fred E. Stewart, Member

William G. Bonelli

George R. Reilly, Member

ATTEST: Dixwell L. Pierce, Secretary