



BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
MILTON H. ESBERG COMPANY)

Appearances:

For Appellant: Dan S. Hewitt, Attorney at Law
For Respondent: W.M. Walsh, Assistant Franchise Tax
Commissioner; Harrison Harkins,
Assistant Franchise Tax Counsel

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 Milton H. Esberg Company to a proposed assessment of an additional tax in the amount of \$2,575.06 for the taxable year ended December 31, 1936, based upon the income of the company for the year ended December 31, 1935.

The proposed assessment arose from the disallowance by the Commissioner of a deduction in the amount of \$63,638.03 claimed by the Appellant in its return of income for the year 1935 on account of the worthlessness of certain shares of stock in the East Land Company. The Commissioner contends that the stock actually became worthless prior to 1935 and that, accordingly, the loss was not sustained during the income year 1935 within the meaning of Section 8 of the Bank and Corporation Franchise Tax Act.

During the latter part of 1934 the sole asset of the East Land Company was one parcel of real estate, which was mortgaged to secure an indebtedness of \$400,000, an amount far in excess of the market value of the property. Negotiations were carried on between the company and the mortgagee for the satisfaction of the liability through the transfer to the latter of the real estate and a sum of money. To obtain the necessary funds the company levied assessments upon its shares, assessments in the amounts of \$42,857.14 and \$3,122.86 being paid by the Appellant on November 21, 1934, and December 20, 1934, respectively. In

Appeal of Milton H. Esberg Company

January, 1935, the real estate and the sum of \$160,000 were transferred to the mortgagee in satisfaction of the indebtedness. Immediately thereafter, the company was dissolved and its remaining assets, consisting of \$1,580.80 in cash, distributed to the shareholders, the Appellant receiving \$395.20. The \$63,638.03 claimed as a deduction for 1935 represents the Appellant's investment in the East Land Company shares on December 31, 1933.

Although the appeal could doubtless be disposed of on the ground that the Appellant has failed to sustain the burden of establishing that the shares of the East Land Company did not become worthless prior to January 1, 1935 (see Appeal of Bertine T. Johnson, June 16, 1942), in our opinion the evidence affirmatively and conclusively establishes the unsoundness of the Appellant's position. Not only is it inconceivable that the stock could have had any value after the decision was made in 1934 to turn over the company's assets to its creditors and abandon the enterprise, but the fact that under the articles of incorporation of the East Land Company its shareholders could be held personally liable for the payment of assessments upon their stock made the ownership of the stock a definite liability.

The loss thus having been sustained not later than 1934, the deduction may not be taken in 1935 merely because the assessments yielded slightly more than the amount required to discharge the company from liability and thus made possible a small cash distribution to its shareholders in the latter year. See De Loss v. Commissioner, 28 F. (2d) 803; Schmidlap v. Commissioner, 96 F. (2d) 680.

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 overruling the protest of Milton H. Esberg Company to a proposed assessment of an additional tax in the amount of \$2,575.06 for the taxable year ended December 31, 1936, based upon the income of said company for the year ended December 31, 1935, pursuant to Chapter 13, Statutes of 1929, as amended, be and the same is hereby sustained.

Done at Sacramento, California, this 16th day of December, 1942, by the State Board of Equalization.

R. E. Collins, Chairman
George R. Reilly, Member
Harry B. Riley, Member

ATTEST: Dixwell L. Pierce, Secretary