BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeals of)
)
ANTHONY T. AND TERESA SCHRILLO;)
HARRY A. AND FLORENCE SCHRILLO;)
EDWARD J. AND ELIZABETH T. SCHRILLO and)
ROBERT E. AND ELIZABETH ALLRED)

Appearances:

For Appellants: Werner F. Wolfen and
Lawrence M. Stone, Attorneys at Law

For Respondent: Burl D. Lack, Chief Counsel;
F. Edward Caine, Associate Tax Counsel

O P I N I O N

These appeals are made pursuant to Section 19059 of the Revenue and Taxation Code from the action of the Franchise Tax Board in denying the claims of Anthony T. and Teresa Schrillo for refund of personal income tax in the amounts of $1,277.55 and $744.84 for the years 1954 and 1955, respectively; the claims of Harry A. and Florence Schrillo for refund of personal income tax in the amounts of $1,277.55 and $433.40 for the years 1954 and 1955, respectively; the claims of Edward J. and Elizabeth Schrillo for refund of personal income tax in the amounts of $1,277.55 and $866.70 for the years 1954 and 1955, respectively; and the claims of Robert E. and Elizabeth Allred for refund of personal income tax in the amounts of $638.78 and $402.53 for the years 1954 and 1955, respectively.

Appellants were partners in the Schrillo Aero Tool Engineering Company, a partnership (hereinafter referred to as the Company) which reported income on the accrual basis of accounting. During 1951 and 1952, the Company received income under contracts it had with the United States Government. The Company reported total net income of $460,407.07 and $608,039.04 for those years, respectively. Appellants reported their distributive shares -of-that income in their 1951 and 1952 personal income tax returns. In 1954 and 1955 the Company entered into agreements pursuant to the Renegotiation Act of 1951 whereby a portion of that 1951 and 1952 income was to be returned to the Government. On September 15, 1954, the Company refunded $74,524 with respect to the year 1951, and on June 7, 1955, it refunded $141,527 with respect to the year 1952.

The Company made no adjustments in its 1954 and 1955 partnership returns *for* the amounts refunded to the government. It reported total net income of $426,968.34 and $41,152.91 for

those respective years. The Appellants reported their full distributive shares of the unadjusted partnership income for 1954 and 1955 in their personal income tax returns. On December 12, 1957, the Company filed amended partnership returns for 1954 and 1955 in which it reduced its reported income by the amounts of the repayments made to the Government. This reduction resulted in a reported loss of approximately $100,000 for 1955. On the same date, the Appellants each filed refund claims with the Franchise Tax Board for the years 1954 and 1955, based upon corresponding reductions in their share of the Company income.

Chapter 16 of the Personal Income Tax Law, Section 18351, et seq., Revenue and Taxation Code, specifically provides for the credit or refund of any overpayments of personal income tax resulting from the renegotiation of contracts with the United States. These sections provide that any reduction in profit is to be carried back to the year when the excessive profit was first reported. Section 18359 requires that such claims be filed within four years from the last day prescribed for filing the return to which adjustment is being made or within two years from the date of repayment, whichever is later. Under these provisions the Franchise Tax Board determined that any overpayments of tax arising from the repayments to the Federal Government were attributable to the years 1951 and 1952 and denied Appellants' refund claims on the ground that they were not timely.

Appellants, however, contend that Chapter 16 does not apply to this case because Section 18351, the controlling provision, only applies in the case of contracts with the United States which are "made by the taxpayer." They point out that Section 17004 defines "taxpayer" as an individual, fiduciary, estate, or trust subject to personal income tax and that Section 17851 provides that a partnership shall not be subject to personal income tax.

Under the rules of partnership law, a partnership is ordinarily considered not as an entity but as an association of individuals. (Reed v. Industrial Acc. Comm., 10 Cal 2d 191.) Each partner is jointly liable on a contract entered into by the partnership. (Section 15015 of the Corporations Code; Hobgood v. Glass, 161 Cal. App. 2d 208.) And, as stated in Charles H. Palda, 27 T. C. 445, 452, aff'd, 253 Fed. 23 302, "It has frequently been said that a partnership is not a taxable entity and has its place in the scheme of Taxation solely for income computation and reporting for tax purposes." (For similar language see Neuberger v. Commissioner, 311 U. S. 83, and Jennings v. Commissioner, 110 Fed. 2d 945.) The partnership here was merely a conduit for the actions of the individual partners, the "taxpayers," and the contracts were made by the individual "taxpayers" who made up the partnership. In accord with this principle the Federal counterpart of Chapter 16 has been consistently applied to partnerships.

(U. S. v. Sarkozy, 99 Fed. Supp. 736; Morris Kurtzon, 17 T. C. 1542; Joseph T. Miller, 23 T. C. 565, aff'd, 231 Fed. 2d 8.) Similarly, the Federal courts have applied to partnership gains from the sale of property, statutory provisions which apply, according to their terms, to property held by a "taxpayer." (Lobello v. Dunlap, 210 Fed. 2d 465; George J. Wibbelsman, 12 T. C. 1022; Mae E. Townend, 27 T. C. 99.)

We conclude that Chapter 16 does apply to Appellants. Thus, unless there is merit to Appellants' alternative contention, next discussed, the refund claims were not timely filed since they were not filed within four years from the due dates of the returns for 1951 and 1952 or within two years after the repayments.

Appellants contend that even if Chapter 16 does apply, their claims were timely because the repayment adjustments may be made to the years 1954 and 1955 rather than 1951 and 1952. They rely upon Section 18358, which provides:

> "Sections 18351 to 18357, inclusive, shall not apply in respect of any contract if the taxpayer shows to the satisfaction of the Franchise Tax Board that a different method of accounting for the amount of ... repayment ... clearly reflects income, and in such case ... repayment shall be accounted for . . . under that method." (Emphasis added.)

The Franchise Tax Board is not satisfied that a different method of accounting would clearly reflect income. This Board is not at liberty to substitute its judgment for that of the Franchise Tax Board unless that Board has clearly abused its discretion.

In the absence of unusual circumstances, the income of a taxpayer on the accrual basis is clearly reflected by excluding the excessive profit which is determined on renegotiation from the income of--the year in which that excess was reported. (Holmes Projector Co. v. U. S., 105 Fed. Supp. 690, cert. den. 344 U. S. 912, reh. den. 345 U. S. 914.) Appellants have failed to show that their case is exceptional. The method they propose would result in a reflection of income drastically different from that obtained by making the adjustments to the earlier years. Since the latter method clearly reflects income, we cannot say that the Franchise Tax Board abused its discretion by concluding that the method proposed by the Appellants does not.

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, pursuant to Section 19060 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the claims of Anthony T. and Teresa Schrillo for refund of personal income tax in the amounts of $1,277.55 and $744.84 for the years 1954 and 1955, respectively; the claims of Harry A. and Florence Schrillo for refund of personal income tax in the amounts of $1,277.55 and $433.40 for the years 1954 and 1955, respectively; the claims of Edward J. and Elizabeth Schrillo for refund of personal income tax in the amounts of $1,277.55 and $846.70 for the years 1954 and 1955, respectively, and the claims of Robert E. and Elizabeth Allred for refund of personal income tax in the amounts of $638.78 and $402.53 for the years 1954 and 1955, respectively, be and the same is hereby sustained,

Done at Sacramento, California, this 13th day of December, 1960, by the State Board of Equalization.

John W. Lynch, Chairman

Richard Nevins, Member

Paul R. Leake, Member

_____, Member

_____, Member

ATTEST: Dixwell L. Pierce, Secretary