

BEFORE THE STATE BOARD OF EQUALIZATION OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
JAMES M. AND MABEL H. HOLMES

Appearances:

For Appellants: George P. Coulter, Attorney

at Law

For Respondent: Burl D. Lack, Chief Counsel

<u>OPINION</u>

This appeal is made pursuant to section 18594 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of James M. and Mabel H. Holmes to proposed assessments of additional personal income tax in the amounts of \$1,190.48, \$6,929.35, \$9,477.75 and \$5,003.95 for the years 1951, 1952, 1953 and 1954, respectively.

During the years on appeal, appellant James M. Holmes was a partner in Los Osos Vendors, a business conducted in the San Luis Obispo area. His connection with this business constitutes the basis for the assessments against him and his wife, Mabel H. Holmes.

For each of the years under review, partnership information returns were filed with respondent for Los Osos Vendors. Appellants did not file individual income tax returns since according to their computations they incurred net losses each year from the operation of this business and another in which appellant James M. Holmes was engaged. The partnership returns for 1951, 1952 and 1953 could not be found for purposes of the hearing of this matter. Attached to respondent's notice of proposed assessment for each of the years in question, however, was a schedule which indicates the gross income and expenses reported on each partnership return.

Appellants urge that the assessments for 1951, 1952 and 1953 must be reversed because in the absence of the partnership information returns for those years they are unable to present their defense adequately. We cannot agree with appellants* contention. It is our duty to determine the appeal on the basis of the available evidence and such presumptions as may be applicable. If a taxpayer has lost or destroyed copies of his returns or records from which the returns may be reconstructed, he should not thereby be placed in a better position than a taxpayer who has retained them. Under the

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circumstances, respondent's notices of proposed assessment together with the schedules attached thereto are the best available secondary evidence of the contents of the returns as to the gross income and expenses reported.

Los Osos Vendors owned music machines, multiple-odd bingo pinball machines, flipper pinball machines and miscellaneous amusement machines. The equipment was placed in various locations, such as bars and restaurants. The proceeds from each machine, after exclusion'of expenses claimed by the location owner in connection with the operation of the machine, were generally divided equally between Los Osos Vendors and the location owner. With respect to some of the miscellaneous amusement machines, Los Osos Vendors received a fixed sum each week rather than half of the net proceeds.

The gross income reported in tax returns of Los Osos Vendors was the total of amounts retained from locations. Respondent determined that Los Osos Vendors was renting space in the locations where its machines were placed and that all the coins deposited in the machines constituted gross income to it. Respondent also disallowed all expenses of Los Osos Vendors pursuant to section 17359 (now 17297) of the Revenue and Taxation Code which read:

In computing net income, no deductions shall be allowed to any taxpayer on any of his gross income derived from illegal activities as defined in Chapters 9, 10 or 10.5 of Title 9 of Part 1 of the Penal Code of California; nor shall any deductions be allowed to any taxpayer on any of his gross income derived from any other activities which tend to promote or to further, or are connected or associated with, such illegal activities.

Except with respect to those miscellaneous amusement machines placed in locations for a fixed weekly amount, the evidence indicates that the operating arrangements between Los Ogos Vendors and each location owner were the same as those considered by us in Appeal of C. B. Hall, Sr., Cal. St. Bd. of Equal., Dec. 29, 1958, 2 CCH Cal. Tax Cas. Par. 201-197,3 P-H State & Local Tax Serv. Cal. Par. 58115. Our conclusion in Hall that the machine owner and each location owner were engaged in a joint venture in the operation of these machines is, accordingly, applicable here.

In Appeal of Advance Automatic Sales Co., Cal. St. Bd. of Equal., Oct.9, 1962, CCH Cal. Tax Rep. Par. 201-984, 2 P-H State & Local Tax Serv. Cal. Par. 13288, we held the ownership or possession of a pinball machine to be illegal under Penal Code sections 330b, 330.1 and 330.5 if the machine was predominantly a game of chance or if cash was paid to players for unplayed free games, and we also held bingo pinball machines to be predominantly games of chance.

It is clear from the testimony of a collector for Los Osos Vendors and the testimony of three location owners that cash was paid to players of the pinball machines for unplayed free games. Most of the pinball machines owned

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the protest of James M. and Mabel H. Holmes to proposed assessments of additional personal income tax in the amounts of \$1,190.48, \$6,929.35, \$9,477.75 and \$5,003.94 for the years 1951, 1952, 1953 and 1954, respectively, be modified in that the gross income is to be recomputed in accordance with the opinion of the board and penalties for failure to file returns are to be deleted. In all other respects the action of the Franchise Tax Board is sustained,,

Done at Sacramento, California, this 17th day of April, 1963, by the State Board of Equalization.

Paul R. Leake	, Acting Chai	irman
Richard Nevin	Member	
Geo. R. Reilly	Member	
Alan Cranston	Member	
	Member	

ATTEST: Dixwell L. Pierce , Secretary