BEFORE THL STATE BOARD CF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
CARL AND EVA FLESCHLER)

Appearances:

For Appellants: Archibald M. Mull, Jr., Attorney at Law

For Respondent: A. Ben Jacobson, Associate Tax Counsel

O P I N I O N

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 Carl and Eva Fleschler to proposed assessments of additional personal income tax in the amounts of $1,085.37, $787.12, $558.98 and $336.15 for the years 1953, 1954, 1955 and 1956, respectively.

Appellant Carl Fleschler (hereinafter called Appellant) owned and operated Carl's Smoke Shop in San Francisco from 1937 through October 1956.

Carl's Smoke Shop sold tobacco products, liquor, candy and other similar items. During the years under appeal several pinball machines belonging to a corporation called Williamson Associates were located in the Smoke Shop. Some of these were the type known as bingo pinball machines. The proceeds from each pinball machine, after exclusion of expenses claimed by Appellant in connection with the operation of the machines were divided equally between Appellant and Williamson Associate;. The Smoke Shop also featured a dice game called "26" until sometime during 1955 when it was stopped by order of the San Francisco Police Department.

Respondent disallowed all expenses on Appellant's returns relative to the Smoke Shop pursuant to Section 17297 (17359 prior to June 6, 1955) of the Revenue and Taxation Code which reads:

> In computing taxable 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 drived from any other activities which tend to promote or to further, or are connected or associated with, such illegal activities.

The evidence indicates that the operating arrangements between Appellant and Williamson Associates with respect to the latter's pinball machines 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. 58145. Our conclusion in Hall that the machine owner and each location owner were engaged-a joint venture in the operation of the 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 or other thing of value was paid to players for unplayed free games, and we also held bingo pinball machines to be predominantly games of chance.

Section 330 of the Penal Code makes it illegal to conduct any banking game played with dice for "money, checks, credit, or other representative of value, ..." A banking game is one in which one person takes all that is lost by the bettors and pays out all that is won, as contrasted with a game in which the players bet a gainst each other. (People v. Ambrose, 122 Cal. App. 2d Supp. 966 [265 P. 2d 191].)

Respondent's auditor testified that during interviews in 1959 an employee of Appellantthroughoutthe years under appeal told him that cash payouts were made to winning players of both the pinball machines and the dice game while Appellant denied making payouts on the pinball machines and only admitted making a few payouts in merchandise to winners of the dice game. The auditor further testified that during these interviews he had been told that the dice game played at the Smoke Shop was called "26", which he understood was a banking game played between the house and the customer. The testimony of the employee at the hearing of this appeal was somewhat confusing. However, we gather from his testimony that the dice game called "26" was played at the Smoke Shop and that the players were allowed to select merchandise at the regular retail price in redemption of their winnings. The employee also testified that he thought he had sometimes seen Appellant make merchandise payouts to winners on the pinball machines. On the basis of the privilege against self-incrimination Appellant refused to answer questions relating to whether cash or merchandise payouts were made to winning players of the pinball machines for unplayed free games and he

also refused to answer the question of whether dice games were played in his establishment. He did, however, later testify that the police closed down the dice game in 1955. A party's refusal to answer a question on the ground of possible self-incrimination can give rise to an inference that a truthful answer to the question would have supported the opposing party's factual contentions. (Fross v. Wotton, 3 Cal. 2d 384 [44 P.2d 350].)

Based on the evidence and on the inferences to be drawn from Appellant's refusal to answer questions relating to the operation of the pinball machines and the dice game on grounds of possible self-incrimination, we find that it was the general practice to make cash or merchandise payouts to players of the pinball machines for unplayed free games and that Appellant conducted a banking game played with dice for "money, . . . credit, or other representative of value" within the meaning of Section 330 of the Penal Code. Accordingly, the pinball and dice game phases of the business were illegal. Respondent was therefore correct in applying Section 17297.

There were no records of amounts paid to winning players of the pinball machines. Respondent estimated these unrecorded amounts as equal to 50 percent of the total amounts deposited in the pinball machines and attributed one-half to Appellant as a joint venturer with Williamson Associates. Respondent made no adjustment for payouts with respect to the dice game in the belief that such payouts were nominal.

As we held in Hall, supra, Respondent's computation of gross income is presumptively correct. There is no evidence which would indicate that the 50 percent payout estimate relative to the pinball machines was excessive and, under the circumstances, it must be sustained.

Tax returns filed by Appellant indicate that the illegal activities contributed 85 percent or more of the gross income of the Smoke Shop during 1953, 1954 and 1955 and 75 percent in 19%. It is clear that the merchandising phase played a secondary and complementary role and was associated and connected with the illegal activities. Consequently, the expenses of the entire business were properly disallowed.

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 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of Carl and Eva Fleschler to proposed assessments of additional personal income tax in the amounts of $1,085.37, $787.12, $558.98 and $336.15 for the years 1953, 1954, 1955 and 1956, respectively, be and the same is hereby sustained.

Done at Pasadena, California, this 25th day of June, 1963, by the State Board of Equalization.

John W. Lynch, Chairman

Paul R. Leake, Member

Geo. R. Reilly, Member

_____, Member

_____, Member

ATTEST: R. G. Hamlin, Acting Secretary