BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
BRAND, WORTH AND ASSOCIATES, INC.)

Appearances:

For Appellant: Jay G. Foonberg
Attorney at Law

For Respondent: Joseph W. Kegler
Tax Counsel

O P I N I O N

This appeal is made pursuant to section 25667 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protests of Brand, Worth and Associates, Inc., against proposed assessments of additional franchise tax in the amounts of $1,682.98 and $1,682.98 for the taxable years ended September 30, 1960, and September 30, 1961, measured by income for the year ended September 30, 1960.

The issue to be resolved in this appeal is whether advance payments received by appellant for goods thereafter to be completed and delivered were includible in income at the time the payments were received.

Appellant designs, manufactures and installs decorative embellishments such as graphic signs, art objects and the like for commercial establishments. It computes its income on the accrual basis of accounting. In dealing with its customers, appellant normally gives an outside estimate of the price and requires an advance payment of from 10 percent to 33 1/3 percent of the estimated price. A typical contract provides as follows: "Total price as per above list is time and material not

to exceed $5,903.00. Terms: 1/3 with order, balance upon completion." When received, the advance payments are deposited by appellant in its general accounts. The total price ultimately charged by appellant is sometimes less than its estimate and, occasionally, appellant's cost exceeds the total amount charged. In one or two cases, appellant has refunded portions of advance payments made after the period in question.

In reporting its income for tax purposes, appellant treated the advance payments as deferred income, reportable when the contracts were completed. Respondent Franchise Tax Board, however, determined that the advance payments constituted income at the time they were received and issued proposed assessments accordingly.

All of the California statutes which have any bearing on the question presented are based upon federal income tax statutes, Sections 24271, 24661 and 24651, respectively, of the California Revenue and Taxation Code (1) define gross income as including all income from whatever source derived, including gross income derived from business; (2) provide that an item of gross income is includible in gross income for the year received unless, under the method of accounting used in computing income, the amount is to be properly accounted for as of a different period; and (3) permit respondent to compute income under such method as, in its opinion, clearly reflects income' when the taxpayer's method does not do so. The federal counterparts of these statutes are sections 61, 451 and 446, respectively, of the United States Internal Revenue Code of 1954 and their predecessors in earlier federal income tax acts.

The federal courts have held in a number of cases that where advance payments for goods to be delivered at a later date are received without restriction as to use, the payments are income for the years in which they are received.. (Wallace A. Moritz, 21 T.C. 622; Fifth & York Co. v. United States, 234 F. Supp. 421; Chester Farrara, 44 T.C. 189.) The mere contingency that part of the advances might be refunded in the future does not alter the result. (Wallace A. Moritz, supra.) The facts in the Moritz case are particularly similar to those before us. In that case, the customer was required to deposit at least a third of an estimated total price for photographic portraits which were yet to be completed through development of negatives, preparation of proofs and final finishing work,

We do not find any material distinction between appellant's case and those which we have cited. The initial payments were received without restriction pursuant to contracts which obligated appellant to complete and deliver goods. Although it appears that some portion of the initial payments made to appellant in subsequent periods were refunded, it is evident that refunds of that kind were only a contingent possibility at the time the payments here in question ware received. The record indicates that at the time of each agreement appellant was expected to retain the initial payment, complete and deliver goods and collect additional payments upon delivery.

Guided by the authorities which we have cited, it is our conclusion that the initial payments constituted income to appellant at the time they were received,

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 25667 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protests of Brand, Worth and Associates, Inc., against proposed assessments of additional franchise tax in the amount of $1,682.98 for each of the taxable years ended September 30, 1960, and September 30, 1961, be and the same is hereby sustained.

Done at Sacramento, California, this 30th day of August, 1967, by the State Board of Equalization.

Paul R. Leake, Chairman

John W. Lynch, Member

Richard Dean, Member

/ , Member

, Member

ATTEST: , Secretary