

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
AUTOMATION INDUSTRIES, INC.)

For Appellant: Thomas W. O'Donnell
Corporate Director of Taxes

For Respondent: Bruce W. Walker
Chief Counsel

Kathleen M. Morris
Counsel

O P I N I O N

This appeal is made pursuant to section 26075, subdivision (a), of the Revenue and Taxation Code from the action of the Franchise Tax Board in partially denying, to the extent of \$24,607.04 for the income year 1969 and \$18,928.37 for the income year 1971, the claims of Automation Industries, Inc., for refund of franchise tax in the amounts of \$53,621.00 and \$37,114.00 for the income years 1969 and 1971, respectively.

Appeal of Automation Industries, Inc.

Appellant, Automation Industries, Inc., filed claims for refund in the amounts of **\$53,621.00, \$49,154.83** and **\$37,114.00** for the income years 1969, 1970 and 1971, respectively, on December 10, 1973. On July 12, 1974, respondent issued its notices of action on these claims. For 1969, respondent allowed appellant an overpayment of **\$29,013.96**, plus interest, where **\$53,621.00** had been claimed. For 1970, respondent allowed **\$61,115.33**, plus interest, where appellant had claimed only **\$49,154.83**. However, pursuant to section 26071 of the Revenue and Taxation Code, **respondent applied** part of the 1970 overpayment to satisfy unpaid tax liabilities in the amount of **\$1,462.11** for the income year 1966 (taxable year 1967), **\$1,501.99** for the income year 1967 (taxable year 1968), and **\$4,087.16** for the income year 1968 (taxable year 1969). For 1971, respondent allowed a refund of **\$18,185.63**, plus interest, where appellant had claimed **\$37,114.00**.

On October 15, 1974, appellant filed **this appeal** contesting respondent's action **with** respect to the income years 1969, 1970 and 1971. While challenging all aspects of respondent's action, appellant specifically questioned the offsets from the 1970 income year refund which were applied against the unpaid tax liabilities for the income years 1966 and 1967. However, appellant did not contest the offset against the unpaid liability for the income year 1968.

Since appellant's claims for refund were partially denied for income years 1969 and 1971, we acknowledged this appeal as an appeal from the denial of claims for refund for those years. (Rev. & Tax. Code, § 26075.) However, since appellant's claim for income year 1970 was granted in an amount exceeding the amount claimed, we reserved jurisdiction over that year. During the course of these proceedings, appellant agreed with respondent's partial denial of the claims for refund with respect to income years 1969 and 1971, but continued to contest respondent's application of part of its income year 1970 overpayment against additional unpaid tax liability for the income years 1966 and 1967. Accordingly, we treat this action as an appeal from the denial of a claim for refund in the amount of **\$6,246.16**, the aggregate amount of the credits taken against the unpaid deficiencies for the income years 1966 and 1967. (Rev. & Tax. Code, §§ 26073 & 26075, subd. (a).)

The two adjustments appellant objects to relate to the tax liability of appellant's subsidiary, Vitro Corporation of America (Vitro) for which appellant became liable as Vitro's transferee. (See Rev. & Tax. Code,

Appeal of Automation Industries, Inc.

§ 25701a.) With respect to income year 1966, appellant contests the amount of \$1,462.11 which was credited against Vitro's tax liability. For the income year 1967, appellant objects to the assessment resulting from respondent's disallowance of a bad debt deduction claimed by Vitro in the amount of \$755,232.00. The proposed assessment in the amount of \$3,680.73 was issued against Vitro on July 28, 1972. This assessment was not protested and became final 60 days after the notice was mailed. (Rev. & Tax. Code, §§ 25664 & 25665.) This liability remained unpaid when appellant claimed an overpayment of \$3,282.06 for a year not in issue which, on January 15, 1973, respondent applied against the unpaid liability of \$3,680.73 owed for the income year 1967. Appellant did not object to this application of the \$3,282.06 overpayment until the present appeal was filed. The remainder of the liability for the income year 1967, \$1,501.99 (\$398.67 tax plus \$1,103.32 interest) was deducted from appellant's overpayment for the income year 1970 on July 12, 1974. Thus, appellant has contested the offset of \$4,784.05 (\$3,282.06 offset on Jan. 15, 1973 and \$1,501.99 offset on July 12, 1974) to satisfy Vitro's tax liability for the income year 1967.

WE! will first consider appellant's challenge to respondent's offset of \$1,462.11 against the unpaid liability for the income year 1966, which is based upon an alleged procedural irregularity in the original proposed assessment for that year.

Vitro, a Delaware corporation, began doing business in California in 1956. In 1968, Vitro became a controlled subsidiary of appellant, a California corporation. Vitro was merged into appellant who assumed all of Vitro's obligations and liabilities in 1971. During 1971, respondent noted that the statute of limitations for issuing a proposed deficiency on Vitro's 1966 income year was to expire on September 15, 1971, and requested Vitro to execute a waiver of the statute of limitations for that year. When Vitro did not respond to the request, respondent issued a proposed assessment in the amount of \$3,575.00 based on income projections. The proposed assessment was issued one day before the statute of limitations expired. Vitro protested respondent's actions, stating that it understood the proposed assessment was only an estimate until an audit was completed. Upon completion of an audit, the proposed deficiency was reduced from \$3,575.00 to \$1,017.06. Respondent's action was not appealed and became final. The deficiency was not paid and was still outstanding in 1974 when appellant filed the claims for refund which are the subject of this

Appeal of Automation Industries, Inc.

appeal. Therefore, respondent applied part of appellant's overpayment for the 1970 income year to satisfy the deficiency.

Appellant contends that respondent did not comply with section 25662 of the Revenue and Taxation Code when it issued the proposed assessment one day prior to the expiration of the statute of limitations because respondent had not commenced its audit; therefore, the proposed assessment was arbitrary. We have previously considered and rejected arguments substantially identical to that of appellant. (Appeal of Eljer Company and Eljer Company of California, Cal. St. Bd. of Equal., Dec. 16, 1958; Appeals of Raymond H. Osbrink, et al., Cal. St. Bd. of Equal., Nov. 7, 1958.) For the reasons set forth in those opinions, appellant's argument is rejected.

The final issue concerns the propriety of respondent's action with respect to Vitro's income year 1967.

As the result of an audit of Vitro's return for the 1967 income year, respondent disallowed a claimed bad debt deduction in the amount of **\$755,232.00** for lack of substantiation. As a result of the disallowance, respondent issued a proposed assessment in the amount of **\$3,680.73** on July 28, 1972. The proposed assessment was not protested and became final upon the expiration of 60 days from the mailing of the notice. Since the **\$3,680.73** assessment remained unpaid, respondent, on January 15, 1973, applied a **\$3,282.06** overpayment made by appellant as a credit against the outstanding tax liability. Appellant did not object to this application until the present matter was appealed on October 15, 1974. Since appellant's objection, which we have treated as a claim for refund, was not made within one year from the date of the overpayment, January 15, 1973, or within four years from the last date for filing the return, March 15, 1968, it must be rejected as untimely. (Rev. & Tax. Code. **§ 26073**; Appeal of First Investment Service Company, Cal. St. Bd. of Equal., July 31, 1973; Appeal of Valley Home Furniture, Cal. St. Bd. of Equal., July 31, 1972; Appeal of Textron, Inc., Cal. St. Bd. of Equal., Jan. 3, 1967.)

The remainder of the tax, \$398.67, plus interest of **\$1,103.32**, was offset against the overpayment claimed by appellant for the income year 1970 by respondent's action on July 12, 1974. Therefore, appellant's claim with respect to this amount was timely. Accordingly, we must look to the merits of appellant's objections directed toward respondent's disallowance of Vitro's claimed bad debt deduction for its income year 1967.

Appeal of Automation Industries, Inc.

As we have indicated, Vitro claimed a bad debt deduction in the amount of **\$755,232.00** for its 1967 income year which was disallowed by respondent. Appellant now contends that the deduction should have been allowed to the extent of **\$700,751.00**. The deduction represents Vitro's loss on its investment in, and uncollectible receivables from, Polytronics Laboratories, Inc.

In 1965, Vitro purchased approximately 700,000 shares of Polytronics stock at a cost of **\$84,766.67**. At the same time, Polytronics was indebted to the National State Bank of New Jersey in an amount of **\$162,924.35**. Apparently, this indebtedness was secured. Vitro acquired this indebtedness from the bank for **\$145,000.00** in 1965. During the next 18 months Vitro loaned money, provided services and sold merchandise to Polytronics. As of April 30, 1967, Polytronics owed Vitro **\$617,684.33**, all of which was unsecured. On May 31, 1967, Polytronics sold part of its assets to Allied Research Associates, Inc., in exchange for 32,600 shares of Allied's stock valued at **\$146,700.00**. The stock was distributed to Vitro in payment of its secured debt, and Polytronics was liquidated in 1967. At the time of liquidation, Vitro's investment in, and receivables from, Polytronics totaled approximately **\$847,451.00**. As part of the liquidation, Vitro received the Allied stock valued at **\$146,700.00**. The difference, **\$700,751.00**, represents the bad debt deduction which appellant claims Vitro was entitled to for its 1967 income year,

Appellant has submitted documentary evidence to substantiate the aforementioned transactions. Based upon this information, it is apparent that for the 1967 income year, Vitro suffered a deductible loss in an amount at least sufficient to offset the \$398.67 in tax which is in issue. Accordingly, respondent's action with respect to appellant's 1970 income year must be modified to reflect this determination concerning Vitro's 1967 income year.

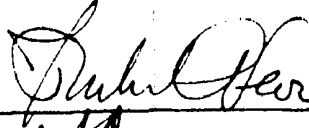
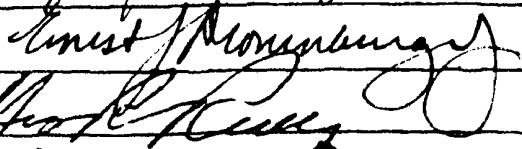
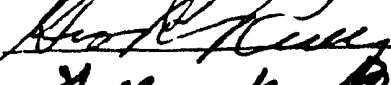

O R D E R

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

Appeal of Automation Industries, Inc.

IT IS HEREBY ORDERED ADJUDGED AND DECREED, pursuant to section 26077 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in partially denying, to the extent of \$24,607.04 for the income year 1969 and \$18,928.37 for the income year 1971, the claims of Automation Industries, Inc., for refund of franchise tax in the amounts of \$53,621.00 and \$37,114.00 for the income years 1969 and 1971, respectively, be and the same is hereby sustained; and that the action of the Franchise Tax Board in denying the claim of Automation Industries, Inc., for refund of franchise tax in the amount of \$6,246.06 for the income year 1970, be and the same is hereby modified in accordance with the views expressed in this opinion. In all other respects, the action of the Franchise Tax Board is sustained;

Done at Sacramento, California, this 21st day
of May, 1980, by the State Board of Equalization.

, Chairman
, Member
, Member
, Member
_____, Member