BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of )
)
RAMON S. AND REBECCA RAMOS )

Appearances:

For Appellants: Ramon S. Ramos
in pro. per.

For Respondent: Kendall E. Kinyon
Counsel

## O P I N I O N

This appeal is made pursuant to section 18593 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Ramon S. and Rebecca Ramos against a proposed assessment of additional personal income tax and penalty in the total amount of $1,807.81 for the year 1975.

The issue presented is whether appellants were entitled to a claimed bad debt loss deduction for 1975.

As Rebecca Ramos is a party to this action solely because of her filing a joint return with her husband, "appellant" hereinafter shall refer to appellant-husband, Ramon S. Ramos.

For 1975, appellant and his wife filed a joint return in which they stated his occupation as butcher and her occupation as homemaker. They also claimed a deduction for a bad debt loss in the amount of $15,416.00. The loss was explained as having arisen from a loan to Los Angeles Pyramyde, Inc. (Pyramyde), a California corporation of which appellant is a 33 1/3 percent shareholder.

Respondent audited the return and requested that appellant provide information concerning the claimed bad debt loss deduction. When appellant failed to furnish the requested information, respondent disallowed the claimed deduction and proposed an assessment accordingly. A 25 percent penalty for failure to furnish information was also imposed.

At appellant's protest hearing, he stated that he had loaned Pyramyde $15,416.00, in cash, as working capital to finance trips of Pyramyde's officers to Mexico. The stated purpose of the trips was to arrange sugar purchases. Appellant submitted two letters from the president of Pyramyde, the first of which carried the date of March 3, 1.975, and acknowledged a loan arrangement like the one claimed by appellant. That letter also stated, "[A]n official promissory note will be issue(d) at a later date." The second letter, dated September 20, 1975, stated that appellant's loan would not be repaid due to Pyramyde's indebtedness to others. Appellant was then asked if he had any better evidence of the advance. His response was that as far as Pyramyde's records were concerned, they had disappeared with Pyramyde's treasurer, and as far as his personal records were concerned, he had thrown away a corporate memo evidencing his advance. The only other thing learned at the protest hearing was that Pyramyde had not filed any tax returns. On the basis of all this information respondent denied appellant's protest and affirmed the propsed assessment. Appellant then appealed.

At the oral hearing in this matter, appellant came forward with additional documentary evidence which he argued supported his claim. The documents consisted mainly of correspondence between Pyramyde and Mexican sugar dealers. These documents had a charred appearance and were in the nature of information requests or preliminary offers, and most of them were written in the latter part of 1974. Appellant also stated that the balance of Pyramyde's records had been destroyed in a fire. His only other argument was that he had documented his travel in Mexico for purposes of arranging sugar purchases. Respondent, on the other hand, noted that the only travel appellant had attempted to document occurred in 1974. Respondent also argued that the submitted documents proved only that Pyramyde engaged in some preliminary negotiations in 1974, and that since this preceded the year at issue as well as Pyramyde's date of incorporation (Jan. 3, 1975), the correspondence should not be viewed to support appellant's claim. Moreover, noted respondent, appellant had not submitted any evidence of a note. Appellant was then advised that without evidence of a note, his case did appear weak. He responded that he might be able to find the note in Mexico, and was therefore given additional time to submit evidence of a note. Subsequently, within the time allowed him, he did submit a document dated February 14, 1975,. which he.claimed was the note in question. However, for reasons stated below, it is our conclusion that neither this note nor the other documents are supportive of the deduction appellant has claimed.

Section 17207 of the Revenue and Taxation Code provides, in pertinent part:

> (a)(1) There shall be allowed as a deduction any debt which'becomes worthless within the taxable year; ...

Revenue and Taxation Code section 17207 is substantially similar to section'166 of the Internal, Revenue Code, so federal case law and interpretations concerning the latter are highly persuasive as to the application of the California section; (Holmes v. McColgan, 17 Cal.2d 426, 430 [110 P.2d 428] (1941); Meanley v. McColgan, 49 Cal.App.2d 203, 209 [121 P.2d 451 (1942); Rihn v. Franchise Tax Board, 131 Cal.App.2d 356, 360 [280 P.2d 893] (1955).)

Entitlement to the deduction under section 17207 has been determined to be conditioned upon the satisfaction of two major requirements. First, a bona fide debt must exist (Cal. Admin. Code, tit. 18, reg. 17207(a), subd. (3).); and secondly, the debt must have become worthless in the taxable year for which the deduction is claimed. (Redman v. Commissioner, 155 F.2d 319 (1st Cir. 1946); Appeal of Fred and Barbara Baumgartner, Cal. St. Bd. of Equal., Oct. 6, 1976; Appeal of Grace Bros. Brewing Co., Cal. St. Bd. of Equal., June 28, 1966; Appeal of Isadore Teacher, Cal. St. Bd. of Equal., April 4, 1961.) The taxpayer has the burden of proving that these tests have been met. (Appeal of Andrew J. and Frances Rands, Cal. St. Bd. of Equal., Nov. 6, 1967.) We are of the opinion that appellant has failed to prove both the existence of a valid debt in the claimed amount and the debt's worthlessness in the year at issue.

Appellant claims to have advanced $15,416.00, not an insubstantial sum, to Pyramyde. However, when respondent first requested further information from appellant, appellant did not present any records, personal or otherwise, to show that this or any other amount was so advanced. Appellant's lack of documentary evidence was explained at first as being due to the disappearance of Pyramyde's records. However,, appellant later stated that the records had in fact been burned and he also stated that he had thrown away a corporate memo evidencing the note. In spite of all of this, appellant was subsequently able to provide two letters from Pyramyde's president which appear to show the existence of the note and its subsequent worthlessness, and when pressed to corroborate the letters, i.e. submit evidence of a note, he was able to "find" such a document in Mexico.

Appellant's above explanations and selective production of evidence give us some concern, for they tend to undermine the authenticity that otherwise would normally attach to the letters and the note. There is an additional factor, however, that causes us to discount the documents almost entirely. That factor is found in the fact that the March 3, 1975 letter indicates that an official note is to be executed in the future, but the note submitted by appellant actually antedates that letter, the note bearing the date of February 14, 1975. Since it is improbable that Pyramyde's president would write about a future note when such a note is supposed to have already been in

existence, it can easily be concluded that the note was not executed either at the time or for the purpose appellant has indicated. This factor, coupled with the convenient production of the two letters from Pyramyde's president when all other supporting records were claimed to be unavailable for a number of alternative reasons, causes us to question whether the note or the 'letters represent what appellant says they do. Consequently, since appellant's claim is based principally on the three documents just discussed, the question of whether appellant has shown the existence of a bona fide debt must be resolved against him.

A similar result follows as to the second requirement, the showing of the debt's worthlessness in the year claimed, for the only evidence of worthlessness is the second letter from Pyramyde's president. Since this letter is among the items which we have found discountable, and since appellant has not otherwise shown by objective factors that the claimed debt was entirely worthless (Joseph Rubin, 9 B.T.A. 1183 (1928); Redman v. Commissioner, supra) or that he took any steps to recover the debt (Earl V. Perry, 22 T.C. 968 (1954)), he has failed to satisfy that second requirement.

On the basis of the foregoing, it is our opinion that respondent's disallowance of the claimed bad debt loss was proper and must therefore be upheld. The penalty determination in this matter also must be upheld, for appellant has not attempted to refute the penalty and the burden was on him to do so. (Appeal of Myron E. and Alice Z. Gire, Cal. St. Bd. of Equal., Sept. 10, 1969.)

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 Ramon S. and Rebecca Ramos against a proposed assessment of additional personal income tax and penalty in the total amount of $1,807.81 for the year 1975, be and the same is hereby sustained.

Done at Sacramento, California, this 23rd day of June , 1981, by the State Board of Equalization, with Board Members Mr. Dronenburg, Mr. Reilly, Mr. Bennett and Mr. Nevins present.

Ernest J. Dronenburg, Jr. , Chairman

George R. Reilly , Member

William M. Bennett , Member

Richard Nevins , Member

, Member