BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
ANTHONY H. EREDIA)

For Appellant: Anthony H. Eredia, in pro. per.

For Respondent: Kathleen M. Morris 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 Anthony H. Eredia against a proposed assessment of additional personal income tax in the amount of **$1,568.69** for the year **1976.**

The issue to be decided is whether appellant sustained a deductible loss under. the terms of Revenue and Taxation Code section 17206,

Appellant is the president of Giant Furniture, Incorporated, a corporation engaged in the retail furniture business. Appellant claims that in May of 1975 he gave a total of $18,000.00 in cash to his friend, Frank Ramirez to "invest.? Ramirez is -generally known to have usually maintained large quantities of narcotics. Appellant claims that on two separate occasions in May of 1975 he placed $10,000.00 and $8,000.00 in a manila envelope for pickup by an Eleanor Palacios and a James Best for delivery to Ramirez. However, there were no written records evidencing these transactions between the parties although respondent did verify that sometime in May of 1975 appellant withdrew $18,000.00 from his bank account. Palacios and Best both denied under oath ever having received the funds which appellant claims to have given them.

Appellant maintains nonetheless that he had an oral agreement with Ramirez that allowed Ramirez use of the $18,000.00 for twelve months with appellant to receive $800.00 monthly (a total of $9,600.00 for the year), in return for use of the money. According to appellant, the agreement provided that appellant was to receive his original "investment" at the end of the twelve month period and would have the option of having his funds.repaid.to him at any time upon demand.

According to appellant, in October of.1975 he reconsidered having made the' "investment" with Ramirez and requested that the $18,000.00 be returned to him. Appellant states that immediately following a discussion regarding return of the funds, he was shot three times and seriously wounded by one of Ramirez's cohorts. Appellan.t further alleges that he obtained $500.00 from Ramirez immediately prior to the shooting.

In 1976, after.recuperating from his injuries, appellant recounted the above facts in a criminal prodeeding against Ramirez and his cohort on charges of assault; During the course-of.the proceedings appellant admitted having received cocaine from Ramirez and further acknowledged his own belief that the funds he advanced to Ramirez were intended for use' by Ramirez in purchasing narcotics. This acknowledgement came during

testimony by appellant in which he stated: "I was kind of closing my eyes to it, but I knew." Both defendants were convicted of assault with a deadly weapon and the convictions were upheld on appeal.

Appellant did not institute legal proceedings to recover the $18,000.00 he claims to have invested. However, he claimed this amount as a casualty loss deduction in his personal income tax return for 1976. Respondent concluded that appellant was not entitled to his claimed loss. Accordingly, respondent issued its deficiency notice on April 17, 1979. Appellant protested. Respondent subsequently affirmed its deficiency notice on December 28, 1979, and this appeal followed.

It is well established that deductions are a matter of legislative grace, and the taxpayer bears the burden of proof to establish that he is entitled to a particular deduction. (New Colonial Ice Co. v. Helvering, 292 U.S. 435 [78 L.Ed. 1348] (1934); Appeal of Joseph A. and Marion Fields, Cal. St. Bd. of Equal., May 2, 1961.) Appellant's argument here is that the loss he sustained should be deductible under the provisions of Revenue and Taxation Code section 17206 which, in the case of an individual, allows as a deduction certain specified losses sustained during the taxable year and not compensated for by insurance or otherwise. Appellant's major contention is that he sustained, one of the losses deductible under section 17206, a loss due to theft. Alternatively, he contends that his claim falls under the remaining loss categories allowed under section 17206. These contentions are without merit. Although there is evidence here that appellant withdrew $18,000.00 from his bank account, there is no convincing proof that these funds were ever advanced to Ramirez or his cohorts. On the contrary, there is sworn testimony by the individuals involved that they never received the funds. Where a theft loss is alleged, it must be shown that the loss was a product of circumstances which clearly and convincingly indicate theft. (Michele Monteleone, 34 T.C. 688 (1960).) We find that appellant has not presented evidence sufficient to substantiate the allegation of theft. Furthermore, this deficiency of proof applies to a-11 the other loss categories specified under section 17206. Appellant's claim thus fails under all loss categories applicable to individuals.

The above conclusion is especially appropriate for the additional reason -that allowance of the deduction would be contrary to ublic polidy.

Revenue and Taxation Code section 17206, which provides for the deduction of losses, is identical to Internal Revenue Code section 165(a)-(e). Therefore, federal court decisions interpreting Internal Revenue Code section 165(a)-(e) should be given great weight in the interpretation of section 17206. (Meanley v. McColgan, 49 Cal.App.2d 203 [121 P.2d 45] (1942); Appeal of Glenn M. and Phyllis R. Pfau, Cal. St. Bd. of Equal., July 31, 1972.) In Raymond Mazzei, 61 T.C. 497 (1974), the taxpayer claimed a theft loss from a transaction entered into for profit. The taxpayer invested $20,000.00 in a scheme to conterfeit United States currency through the use of a black box. (The box was incapable of reproducing currency..) At the time the taxpayer invested his $20,000.00, two co-conspirators broke into the room and confiscated the funds. The court found that the taxpayer sustained a theft loss, but the deductibility of such a loss was precluded by public policy considerations. That is, the court felt that allowance of the loss deduction would constitute an immediate and severe frustration of the clearly defined policy against counterfeiting obligations of the United States. (See also Luther M.Rickey, Jr., 33 T.C. 272 (1959).) We feel that public policy dictates a denial of appellant's claim in the instant case. Appellant had knowledge that Ramirez was a narcotics dealer, having on several occasions purchased drugs from him himself. He also knew that the money he advanced to Ramirez, in all probability, would be used to traffic narcotics. Therefore. even if it is accepted that appellant in fact advanced $18,000.00 to Ramirez; that this money was advanced with the intention of the appellant making a profit; and further, that the funds were later misappropriated by Ramirez, the reasoning in Mazzei would hold that such loss should, nevertheless, be nondeductible. As the court stated in Mazzei at page 501:

> In our opinion, the fact that the petitioner was victimized . . . does not make his participation in what he considered to be a criminal act any less violative of a clearly declared public policy.

In this case, the; clearly defined' national and state policy is prohibitive of the trafficking of narcotics. Appellant's actions were violative of this policy, and consequently, he should not be, allowed benefit of a deduction under section 17206.

Accordingly, the judgment of respondent is affirmed.

Appeal of Anthony H. Eredia

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 Anthony H. Eredia against a proposed assessment of additional personal income tax in the amount of $1,568.69 for the year 1976, be and the same is hereby sustained.

Done at Sacramento, California, this 29th day of July, 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