BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
) No. 84A-615
WESSMAN TOYOTA-PONTIAC, INC.)

For Appellant: Morton J. Bregman
Certified Public Accountant

For Respondent: Mary E. Olden
Counsel

O P I N I O N

This appeal is made pursuant to section 25666[1/] of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Wessman Toyota-Pontiac, Inc., against proposed assessments of additional franchise tax in the amounts of $7,980 and $513 for the years 1978 and 1979, respectively.

1/ Unless otherwise specified, all section references are to sections of the Revenue and Taxation Code as in effect for the years in issue.

The issue presented is whether appellant has properly substantiated deductions taken for additions to its reserves for bad debts and repossession losses and for a robbery or theft loss.

Appellant is a California corporation that accounts for bad debts by the reserve method. Appellant made additions to its bad debt reserve of $16,663 in 1978 and $54,753 in 1979. Appellant also treated repossession losses similarly to bad debt reserves and made additions to its reserves for such losses of $27,687 in 1978 and $22,257 in 1979. In addition, appellant deducted $44,315 as a "robbery loss" on its 1978 return. Later, appellant characterized this loss as arising from casualties and embezzlement. (Resp. Br., Ex. A.)[2/] Upon audit, respondent asked for documents to substantiate each of the claimed deductions. When no such information satisfactory to respondent was provided by appellant, respondent disallowed all the above deductions.

Following respondent's ruling, appellant filed a protest in which it claimed that it had assembled additional information which would support all of the deductions. Appellant, however, did not present these facts in its protest. Accordingly, respondent affirmed its assessments and this appeal followed.

Section 24348 provides, in relevant part: "There shall be allowed as a deduction debts which become worthless within the income year; or, in the discretion of the Franchise Tax Board, a reasonable addition to a reserve for bad debts."

Both parties agree that the deductions for bad debt reserves and repossession reserves are properly computed using the six-year moving average formula developed in Black Motor Co. v. Commissioner, 41 B.T.A. 300 (1940), affd. on other grounds, 125 F.2d 977 (6th Cir. 1942). Respondent requested, among other documents, a list of bad debts and repossession losses written off during the years at issue in order to determine the proper amounts, if any, to be added to the reserves in each year under this method. (Information Request sent

2/ Allegedly, losses in this category arose from "stolen cars, wrecked cars, wrecked demos and etc." (over $36,000) and "monies taken by the General Manager and salesmen." (Resp. Br., Ex. A.)

to appellant dated October 8, 1982.) To date, no such information has been submitted by appellant.

It is, of course, well settled that respondent's determination with respect to a reserve for bad debts carries great weight because of the express discretion granted it by statute. Under the circumstances, the taxpayer must not only demonstrate that additions to the reserve were reasonable, but also must establish that respondent's actions in disallowing those additions were arbitrary and amounted to an abuse of discretion. (Appeal of H-B Investment, Inc., Cal. St. Bd. of Equal., June 29, 1982; Appeal of Brighton Sand and Gravel Company, Cal. St. Bd. of Equal., Aug. 19, 1981).

On appeal, appellant argues only that over the years sales have increased dramatically and that, accordingly, greater deductions to reserves should be warranted in the years at issue. As indicated above, no actual evidence as requested by respondent has been submitted. On the record before us then, we must conclude that appellant has failed to carry its burden of proving that the additions to its reserves for the years in question were reasonable. Further, we conclude that appellant has failed to prove that respondent's assessment was arbitrary and an abuse of discretion. Accordingly, respondent's action on these deductions will be sustained.

With respect to the deduction for "robbery," subdivision (a) of section 24347 allows, as a deduction, "any loss sustained during the income year and not compensated for by insurance or otherwise." In its request for information referred to above, respondent also requested proof of the loss for "robbery" (e.g., police report, insurance claims). As stated above, no such documentation has been submitted. Again, it is well settled that the burden of proof to establish entitlement to such a loss deduction is imposed upon the taxpayer. (Appeal of Villasenor Corporation, et al., Cal. St. Bd. of Equal., Aug. 18, 1980.) Since no such evidence was submitted, respondent's action with respect to this issue must also be sustained.

For the reasons cited above, respondent's action must be sustained in its entirety.

Appeal of Wessman Toyota-Pontiac, Inc.

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 protest of Wessman Toyota-Pontiac, Inc., against proposed assessments of additional franchise tax in the amounts of $7,980 and $513 for the years 1978 and 1979, respectively, be and the same is hereby sustained.

Done at Sacramento, California, this 9th day of October , 1985, by the State Board of Equalization, with Board Members Mr. Dronenburg, Mr. Collis, Mr. Bennett, Mr. Nevins and Mr. Harvey present.

Ernest J. Dronenburg, Jr. , Chairman

Conway H. Collis , Member

William M. Bennett , Member

Richard Nevins , Member

Walter Harvey* , Member

*For Kenneth Cory, per Government Code section 7.9