

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of }
MOR-BEN INSURANCE MARKETS }
CORPORATION }

Appearances:

For Appellant: Jay Zybelman
Attorney at Law

For Respondent: Michael R. Kelly
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 denying the claim of **Mor-Ben** Insurance Markets Corporation for refund of franchise tax in the amount of \$20,799 for the income year ended October 31, 1979.

Appeal of Mor-Ben Insurance Markets Corporation

The issue on appeal is whether a series of cash advances made by appellant to its wholly owned subsidiary **became** totally worthless during the year in question so as to allow appellant a business bad debt deduction for the total amount advanced.

Appellant is a California corporation currently seeking protection under chapter 11 of the Federal Bankruptcy Act. From June 1977 to September 1979, appellant advanced a series of sums totaling \$161,786 to its wholly owned subsidiary, Vealettes, Inc., No. 1 (Vealettes). After a year of operation, Vealettes considered its sole asset, a deep-fried veal fast food restaurant, a failure and attempted to sell the operation. When no buyer could be **found**, the restaurant was closed in October 1979. In December 1979, with another infusion of capital from appellant, the restaurant was reopened in the hope that a going concern would be easier to sell. Business did improve but not enough to satisfy Vealettes or any prospective buyers. The restaurant closed permanently in July 1980.

On or about July **17**, 1981, appellant filed a claim for refund for its income year ended in October 1979, based upon the theory that it was entitled to a bad debt deduction for the total amount it had advanced to Vealettes. Appellant's contention is that the **advances** were loans which became totally worthless in October 1979, when the restaurant temporarily closed. Respondent denied the claim, indicating there was insufficient evidence to show that the debt owed by Vealettes became totally worthless that month. In the alternative, respondent argues the advances were contributions to capital which would not be deductible as a business bad debt.

It is unnecessary to discuss whether the advances **were** contributions to capital or bona fide loans. Assuming, without so deciding, that the advances were bona fide loans, appellant has failed to carry its burden of proving that the debt became worthless in the 1979 income year.

Revenue and Taxation Code section 24348 allows a deduction for "debts which become worthless within the income year." In order to **be** entitled to a bad debt deduction, the taxpayer must establish that the debt became totally worthless in the year claimed. . (Appeal of Parabam, Inc., Cal. St. Bd. of Equal., June' 29, 1982;
Appeal of Valley View Sanitarium and Rest Home, Inc.,

Appeal of Mor-Ben insurance Markets Corporation

Cal. St. Bd. of Equal., Sept. 27, 1978.) The standard for the determination of worthlessness is an objective test of actual worthlessness. The time **for** actual worthlessness must be fixed by an identifiable event or events which furnish a reasonable basis for abandoning any hope of future recovery. (United States v. White Dental Mfg. Co., 274 U.S. 398 [71 L.Ed. 11201 (1927)]; Appeal of Parabam, Inc., supra.)

Appellant argues that the October closure- of the restaurant is the objective, identifiable event which furnished the reasonable basis **for** abandoning any hope of future recovery. Appellant reasons that at that time the amount owed it by Vealettes was so much greater than the amount appellant would have realized had the restaurant 'been liquidated, that for all intents and purposes the debt was totally worthless. We do not agree with **appellant's** analysis.

It is the fact that at the time of the temporary closure appellant saw some value in Vealettes that is important. The amount of value appellant saw as recoverable is irrelevant. **Mere** insolvency of Vealettes at the time of the temporary closure, **without** more, does not establish the debt's total worthlessness; it merely indicates that the debt may only have been partially recoverable. (See Trinco Industries, Inc., 22 T.C. 959 (1954); Appeal of Parabam, Inc., supra.) As appellant admits there was some value to its debt as of October 1979, albeit minimal, it has failed to prove the debt was totally worthless.

For the reasons stated above, we find appellant has failed to carry its burden of proving it was entitled to a bad debt deduction during the income year ended in October 1979 for money it advanced to Vealettes. While section 24348 also provides, under certain conditions, for the deduction of partially worthless bad debts, appellant has neither alleged nor proved the amount of any such partial worthlessness. Accordingly, respondent's action in this matter will be sustained.

