76-SBE-117

BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
JOSEPH J. AND LILLIAN VICINI)

Appearances:

For Appellants: Louis Fong
Certified Public Accountant

William Kerfoot

For Respondent: James C. Stewart
Counsel

O P I N I O N

This appeal is made pursuant to section 18594 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Joseph J. and Lillian Vicini against proposed assessments of additional personal income tax in the amounts of $318.75, $754.60, and $618.54 for the years 1969, 1970, and 1971, respectively.

The issue is whether certain cash withdrawals made by appellant Joseph J. Vicini from his wholly-owned corporation were taxable dividends.

Appellant is the sole shareholder of Joe Vicini, Inc., a California corporation engaged in the road construction business. During the years in question and for some years prior thereto, appellant withdrew large amounts of money from the corporation each year. He used about half of this money to purchase road construction equipment which he then leased to the corporation, while the remainder was used for personal purposes unrelated to the business.

The withdrawals were carried on the corporation's books in an account labeled "advances due from shareholder." Appellant states that he considered the withdrawals loans and at all times intended to repay them. He in fact did repay some of them, primarily by crediting to the withdrawal account all amounts which the corporation owed to him as salary or rental credits. Appellant did not execute any notes evidencing indebtedness to the corporation or give the corporation any security for repayment. Nor was any provision made for interest, allegedly since the corporation owed offsetting interest charges to appellant.

The following table summarizes the withdrawals and repayments for the years 1966 through 1971:

Year	Withdrawal	Repayment	Ending Balance	Increase (Decrease)
1966			$40,688	
1967	$73,638	$72,827	41,499	$ 811
1968.	49,209	55,757	34,951	(6,548)
1969	72,891	67,368	40,474	5,523
1970	78,126	73,179	45,421	4,947
1971:	70,502	-60,213	55,710	10,289

The corporation did not pay a dividend at any time during these years. As of September 30, 1971, the corporation had $75,052 in retained earnings.

On his California. personal income tax returns, for the years in question, appellant reported as income the salary and lease payments which had been credited to the withdrawal account. Respondent determined that he

should also have included in income, as disguised dividends, the excess of the withdrawals over the repayments in each of the years at issue. Appellant objected to that determination, and this appeal followed.

Whether a withdrawal of corporate funds by a shareholder represents a taxable dividend or a nontaxable loan is a question of fact to be resolved in light of all the surrounding circumstances. (Appeal of Jack A. and Norma E. Dole, Cal. St. Bd. of Equal., Nov. 6, 1970.) The controlling determination is whether, at the time of the withdrawal, the parties to the transaction intended that the funds would be repaid. (Appeal of Richard M. and Beverly Bertolucci, Cal. St. Bd. of Equal., May 4, 1976.)

After examining the evidence presented by the parties to this appeal, we have concluded that respondent's determination was correct. The alleged loans were neither secured nor evidenced by notes. Despite the vague allegations of offsetting interest charges, it appears that there were no express arrangements for the payment of interest. Appellant used about half the withdrawals for personal purposes, and there was accordingly no business reason for the corporation to loan such amounts to appellant. In addition, the corporation paid no formal dividends during this period. Appellant states that the corporation was financially unable to do so, but since the corporation had over $75,000 in retained earnings at the end of September 1971, it certainly had sufficient earnings and profits to cover substantial dividends. Taken together, these circumstances indicate that the withdrawals were actually disguised dividends, at least to the extent that they exceeded the repayments. (See Berthold v. Commissioner, 404 F.2d 119 (6th Cir. 1968); William C. Baird, 25 T.C. 387 (1955); Appeal of Jack A. and Norma E. Dole, Cal. St. Bd. of Equal., Nov. 6, 1970.)

Appellant points to other factors which assertedly establish that the withdrawals were loans. He argues that there was a predetermined plan to repay the withdrawals by means of the salary and rental credits; that he had the ability to repay; and that substantial repayment was

in fact made. In this connection, however, it is important to recall that respondent treated the withdrawals as dividends only to the extent they exceeded the repayments. While we may concede that appellant had the ability and intention to repay part of the withdrawals through the salary and rental credits, this lends little support to the contention that he intended to repay the entire amount of the withdrawals. In fact, except for 1968, withdrawals exceeded repayments in each of the years 1967 through 1971, so that there was an outstanding balance of over $55,000 in the withdrawal account by the end of 1971. We therefore find it difficult to believe that appellant planned or intended that the salary and rental credits would ever entirely offset the withdrawals. (See William C. Baird, supra; Walter K. Dean, 57 T.C. 32, 37-38 (1971); Appeal of Goodwin D. and Bessie M. Key, Cal. St. Bd. of Equal., Dec. 15, 1966.)

Appellant also relies on the fact that the withdrawals were carried as loans on the corporation's books. As sole shareholder of the corporation, however, appellant was able to withdraw funds at his convenience and use them as he desired. He was also in a position to manipulate the corporation's affairs to obtain permanent use of the withdrawn funds under the guise of loans. Although he asserts that his actions were limited by the expected salary and rental credits' in each year, his withdrawals exceeded those "limits" during each of the appeal years. Accordingly, we cannot attach much significance to the treatment of the withdrawals as loans on the corporation's books. (See Elliott J. Roschuni, 29 T.C. 1193 (1958), aff'd per curiam, 271 F.2d 267 (5th Cir. 1959), cert. denied, 362 U.S. 988 [4 L. Ed. 2d 1021] (1960); Appeal of Richard M. and Beverly Bertolucci, supra.)

Finally, we have closely examined all the cases cited by appellant. Each of those cases was decided on its own particular facts, and is distinguishable from the instant appeal for that reason.

Appeal of Joseph J. and Lillian Vicini

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 Joseph J. and Lillian Vicini against proposed assessments of additional personal income tax in the amounts of $318.75, $754.60, and $618.54 for the years 1969, 1970, and 1971, respectively, be and the same is hereby sustained.

Done at Sacramento, California, this 15 day of December, 1976, by the State Board of Equalization.

_____, Chairman

_____, Member

_____, Member

_____, Member

_____, Member

ATTEST: _____, Executive Secretary