BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of	)	
	)	No. 83A-68-KP
WILLIAM L. WALTERS	)	

For Appellant: William L. Walters, in pro. per.

For Respondent: Patricia I. Hart Counsel

O P I N I O N

This appeal is made pursuant to section 18593[1/] of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of William L. Walters against a proposed assessment of additional personal income tax in the amount of $1,541 for the year 1980.

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

The issue on appeal is whether appellant has satisfied his burden of proving that respondent's disallowance of a business expense deduction during the year at issue was mistaken.

Appellant is a certified public accountant. During 1980, appellant advanced about $3,000 to the owner of a business called Southwest Refining (Southwest). The owner of Southwest had informed appellant that his company was going to purchase a portion of a gold tailing pile in Mojave, California, with the hopes of refining and selling the gold in the tailing at a "substantial profit." In 1981, the owner of Southwest was convicted of fraudulent mining activities in connection with the Mojave tailings. Upon being informed of the conviction, appellant decided to take the loss of the $3,000 advance on his 1980 tax return as a business expense deduction.

Respondent audited appellant's return for the year in question in 1982. Respondent determined that appellant had overstated a loss from his accounting partnership, had taken a capital loss deduction in excess of statutory limits, and had mistakenly taken the $3,000 loss as a business expense deduction. It was determined that the loss was actually a theft loss that was not deductible until 1981, the year appellant learned of the loss. The appropriate assessment was issued. Appellant protested the assessment, respondent affirmed its determination, and this appeal followed.

Deductions are a matter of legislative grace and are allowable only where the conditions established by the Legislature have been satisfied. (New Colonial Ice Co. v. Helvering, 292 U.S. 435 (78 L.Ed. 1348] (1934).) Respondent's determination that a deduction should be disallowed is presumed to be correct and the taxpayer bears the burden of proving that he is entitled to the claimed deduction. (Appeal of J. T. and Mildred Bellew, Cal. St. Bd. of Equal., Aug. 20, 1985; Appeal of James C. and Monablanche A. Walshe, Cal. St. Bd.. of Equal., Oct. 20, 1975.) An unsupported assertion that respondent is incorrect in its determination does not satisfy the taxpayer's burden. (Appeal of James C. and Monablanche A. Walshe, supra.)

Appellant has objected to respondent's entire assessment but has produced evidence and argument only with respect to the disallowance of the $3,000 business expense deduction. As appellant has not presented any reason or evidence to overturn respondent's determination

regarding the partnership loss and the capital loss deduction, he has failed to carry his burden of proof and respondent's determinations on those matters must be upheld. (Appeal of James C. and Monablanche A. Walshe, supra.) Consequently, the only issue for us to consider is whether appellant has proven that respondent was incorrect in disallowing the claimed business expense deduction.

Section 17202 provides, in pertinent part, that "[t]here shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business." The concept of a trade or business does not encompass all activities engaged in for profit, but is used in the realistic and practical sense of' a going trade or business. (Appeal of Richard W. and Hazel R. Hill, Cal. St. Bd. of Equal., May 19, 1981.) Expenditures made preparatory to the establishment of a business do not constitute expenses incurred in carrying on a trade or business. (Appeal of Howard and Margaret Richardson, Cal. St. Bd. of Equal., Feb. 2, 1976; Appeal of the Estate of Samuel Cohen, et al., Cal. St. Bd. of Equal., Nov. 17, 1964.) Passive investing is not a trade or business. (Whipple v. Commissioner, 373 U.S. 193 [10 L.Ed.2d 288] (1963); Appeal of J. T. and Mildred Bellew, supra.)

Appellant's argument that the loss should be deductible as a business expense fails for two reasons. First, appellant has not established that Southwest was his trade or business. Appellant is an accountant and the mining of gold cannot be considered a regular activity of an accounting firm. (Cf. Appeal of Sherwood C. and Ethel J. Chillingworth, Cal. St. Bd. of Equal., July 26, 1978.) To be viewed as his trade or business, the activity must be one that appellant was actively engaged in (Appeal of Sherwood C. and Ethel J. Chillingworth, supra), and appellant has not presented any evidence of his involvement in the enterprise. Secondly, even if we assume that he changed his trade or business to that of mining for gold, appellant has failed to prove that the expenses he incurred were more than preparatory to the start of a business. (Appeal of Richard W. and Hazel R. Hill, supra; Appeal of Howard and Margaret Richardson, supra.) Appellant simply asks us to take his word at face value that the advance was a business expense, and this we cannot do. (Appeal of James C. and Monablanche A. Walshe, supra.)

The evidence presented in this appeal points to only one conclusion, that appellant invested his money in a fraudulent mining operation and that, for tax purposes, the money was "lost" when the fraud was discovered in 1981. Consequently, respondent's determination that the deduction is not a business expense in 1980 is supported by the record and appellant has failed to carry his burden of proving otherwise. (Appeal of J. T. and Mildred **Bellew**, supra; Appeal of James C. and Monablanche A. Walshe, supra.) Accordingly, respondent's action in this matter must be sustained.

Appeal of William L. Walters

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 William L. Walters against a proposed assessment of additional personal income tax in the amount of $1,541 for the year 1980, be and the same is hereby sustained.

Done at Sacramento, California, this 10th day Of June , 1986, by the State Board of Equalization, with Board Members Mr. *Nevins*, Mr. Collis, Mr. Bennett, Mr. Dronenburg and Mr. Harvey present.

Richard Nevins , Chairman

Conway H. Collis , Member

William M. Bennett , Member

Ernest J. Dronenburg, Jr. , Member

Walter Harvey* , Member

*For Kenneth Cory, per Government Code section 7.9