



87-SBE-058

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeals of)
GERMAN A. POSADA) No. 84J-1133-MA
) 85J-1211

For Appellant: Michael T. Citata
Attorney at Law

For Respondent: Paul J. Petrozzi
Counsel

OPINION

These appeals are made pursuant to section 18646¹/₁ of the Revenue and Taxation Code from the action of the Franchise Tax Board in denying the petition of German A. Posada for reassessment of jeopardy assessments of personal income tax in the amounts of \$6,390.13 including penalty and \$1,726.00 for the year 1982, and \$7,425.88 and \$9,483.00 for the period January 1, 1983, through June 7, 1983.

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

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The sole issue to be resolved in these appeals is whether respondent's reconstruction clearly reflects appellant's unreported income for the years in question.

On June 7, 1983, appellant and a companion were stopped by **Marin** City, California, police for a speeding violation. Appellant was observed attempting to conceal a **large** envelope under the car seat. A subsequent search of appellant's vehicle revealed that the envelope contained \$90,000 in cash.

Upon a review of *its* records, respondent determined that appellant had not filed California tax returns **for** any of the years **for** which respondent had records. Respondent then concluded that collection of tax would be jeopardized by delay, estimated appellant's income for the years at issue, and issued jeopardy assessments. Subsequently, according to respondent, it was able to develop more accurate estimates of income, and it issued a second set of jeopardy assessments. Appellant's petition for reassessment of all of the jeopardy assessments was denied. These timely appeals followed.

Appellant argues that the assessments in **ques-**tion are inappropriate because: the figures determined by respondent reflect money which was not personal income, but rather the proceeds from the sale of inherited properties and income from investments made prior to 1982; appellant was not a resident of California during the period in question; and, even if appellant was a resident, the determinations by respondent were incorrect because appellant was not in California **as** long as respondent claims.

In the instant appeals, **respqndent** has used what is known as the cash expenditure method, a variant of the net worth method, in reconstructing appellant's income for the periods in question. This method, **approved** by the **court in** United States v. Johnson, 319 U.S. 503 [87 L.Ed. 15461 (1943)], **is used** to indirectly prove the receipt of unreported taxable income. The cash expenditure method is designed to reach the type of taxpayer who consumes his self-determined tax-free dollars during the year and winds up no wealthier than before. This method establishes the amount of the taxpayer's purchases of goods and services which are not attributable to resources at the beginning of the year or to nontaxable receipts acquired during the year. (Taglianetti v. United States, 398 **F.2d** 558, 562 (1st Cir. 1968).) However, whenever the government uses the cash expenditure

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method, the beginning and ending net worth positions must be identified with sufficient particularity to rule out **or' account** for the use of a taxpayer's capital to pay for his purchases. (Taglianetti v. United States, supra, 398 **F.2d** at 563.)

The courts have long recognized that the use of the cash expenditure method places the taxpayer at a distinct disadvantage; therefore, certain safeguards were established. (Holland v. United States, 348 **U.S.** 121 [99 **L.Ed.** 1501 (1954).] **One** of the safeguards is that the government is required to establish "with reasonable certainty ... an opening net worth, to serve as a starting point from which to calculate future increases in the **taxpayer's** assets." (Holland v. United States, supra, 348 **U.S.** at 132.) **Before the** government can show **the** existence of unreported income, it must compare the sum of available funds with the total expenditures. Only if the expenditures exceed the sources of available funds has the government established the existence of unreported income. The court in Dupree v. United States, 218 **F.2d** 781 (5th Cir. 1955), a case involving **income** tax fraud, defined "**available** funds" as including (1) the funds available to the taxpayer at the beginning of the period, (2) the income acquired during the period as reported on the taxpayer's return, and (3) the tax-exempt receipts received during the same period. Unless the government can show with a reasonable degree of certainty the **source** of a taxpayer's "available funds," it cannot conclude that a taxpayer, no matter how great his expenditures, has unreported income.

This standard has also been held to apply to civil cases in which the burden of proof is on the taxpayer rather than the government. (Thomas v. Commissioner, 223 **F.2d** 83, 86 (6th **Cir.** 1955).) **In** such cases, the burden of proof remains on the taxpayer, but the record must contain at least some proof which "makes clear the extent of any contribution which beginning **resources** or a diminution of resources over time could have made to expenditures." (Taglianetti v. United States, supra, 398 **F.2d** at 565.) If such proof is lacking, the government's determinations are **arbitrary** and cannot be sustained. (Thomas v. Commissioner, supra; Taglianetti v. United States, supra.)

In the appeals before us, respondent determined that (1) appellant had \$90,000 in cash when he was stopped by the police, and (2) appellant needed an income of \$78,450 in 1982 and \$168,008 for the period January 1,

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1983, to June 7, 1983, to cover his living expenses. Respondent has failed to provide any evidence which establishes appellant's net worth at the beginning of the period in issue. Respondent has not, like the government did in Ford v. United States, 210 F.2d 313 (5th Cir. 1954), contacted banks to determine if appellant had any checking accounts, savings accounts, or safe deposit boxes. It did not secure any witnesses who could testify as to appellant's expenditures or prior accumulations or lack thereof and it did not contact county officials to check for ownership of property or sales of property. As appellant correctly argues, respondent has failed to take into account proceeds from the sale of inherited property. As evidence of this, appellant has submitted various documents dealing with real estate transactions. (App's. Br., Ex. C.) Using the exchange rate offered by appellant, his share of the proceeds from the sale of one inherited property located in Colombia was approximately \$13,936. According to appellant the proceeds from the sales of various other inherited properties resulted in deposits of at least \$100,000 in various certificates of deposits and savings accounts. Appellant contends that he was able to live off the income from these investments.

In Holland v. United States, supra, the court stated that when the government rests its case solely on approximation and circumstantial inferences of a net-worth computation, as in this appeal, the cogency of its proof depends upon its effective negation of reasonable explanations by the taxpayer. In this case, appellant's assertions as to a large inheritance and his presentation of evidence of \$100,000 in various savings accounts and certificates of deposits, are weak: however, respondent has offered no evidence to prove that the money was not received from an inheritance, and instead from some income-producing activity. Respondent merely points to appellant's lifestyle at the time of his arrest, the amount of rent he paid on his apartment, and the large amount of cash in his possession at the time of his arrest as proof that he was not living solely off of his income from savings and, thus, must have had some sort of other income-producing activity. Taken as a whole, we must conclude that, based upon the cash expenditures method, respondent's determination that appellant had unreported income of \$78,450 during 1982 and \$168,008 for the period January 1, 1983, to June 7, 1983, is pure conjecture and its reconstruction of income based on that method is arbitrary.

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Our inquiry does not stop here, however. Despite respondent's failure to establish appellant's opening and closing net worth, thus, effectively **negating** the use of the cash expenditures method of **determining** appellant's income, the assessments must still stand. In the instant case, we have appellant's own admission on his apartment rental agreement that he earned **a gross** income of at least \$15,000 per month. (**Resp. Br.**, Ex. 1.) Appellant has offered no evidence to explain or refute his admission. In the absence of records upon which to make a more precise assumption, **the \$15,000** will be accepted as the basis for determining appellant's income for the period in question. (See Appeal of Ronald Lee Royer, Cal. St. Rd. of Equal., July 26, 1978, and the cases cited therein.) If the \$15,000 figure is used, appellant's income for the appeal period is \$258,750 (17 $\frac{1}{4}$ months x \$15,000). This amount is well in excess of the assessments actually issued by respondent.

Appellant also claims the assessments were improper because he was only in California for **a temporary or transitory purpose** and that he did not intend to **become** a California resident. At various times, appellant, **a United States** citizen, has resided in Colombia and Florida.' He came to California in March, **1982**, to explore various business opportunities. He stated he intended to remain in California for approximately six months, but because of his wife's subsequent health problems she was forced to stay for a longer period. **Appellant** claims that he returned to Colombia in May, **1983.**^{2/}

While we agree with appellant that he has few contacts with **California**, we do not agree that the facts presented fail to support a finding of residency during the appeal period. Appellant moved to California, obtained a California driver's **license**, registered his car, purchased and registered **a power boat (albeit** under an assumed name), and after living with friends for a **short** period, pre-paid six months rent on an apartment. Appellant's statement that his wife's illness delayed his departure is not supported by the evidence. The fact that appellant lacked some of the other indicia of residency such as voter's registration, bank accounts, church affiliations, and club membership, reflects more on his nomadic nature rather than on California nonresidency.

^{2/} This is somewhat confusing because appellant's **arrest** occurred in June, 1983.

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Additionally, while we may accept as true the statement that appellant did spend a great deal of time traveling between Colombia and California, this does not defeat a finding of residency because it is well-established that a person may have more than one residence for tax purposes. (Whittell v. Franchise Tax Board, 231 **Cal.App.2d** 278, 284 [**41 Cal.Rptr. 673**] (1964).)

Finally, appellant contends that respondent incorrectly estimated his 1982 income because he did not move to California until March, 1982, and because he did not pay any rent until June, 1982. We find no evidence to support this claim. We are unable to ascertain the exact date when appellant moved to California, however, appellant has offered no reasonable explanation to disprove the dates determined by respondent. (See Holland v. United States, *supra*.)

For the reasons stated above, respondent's action is sustained in all respects.

