87-SBE-063

BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
) No. 85J-678-SW
ELBERT B. POPPELL)

Appearances:

For Appellant: Elbert B. Poppell
in pro per.

For Respondent: Grace Lawson
Counsel

O P I N I O N

This appeal is made pursuant to section 18646[1/] of the Revenue and Taxation Code from the action of the Franchise Tax Board in denying the petitions of Elbert B. Poppell for reassessment of jeopardy assessments of personal income tax in the amounts of $19,213 and $3,153 for the year 1982 and the period January 1, 1983, to March 11, 1983, respectively.

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

The first issue presented in this appeal is whether respondent properly reconstructed appellant's income for the periods in issue. If appellant does have unreported income, the second issue is whether he has documented any claimed expenses pursuant to section 17233.

Appellant is a San Diego resident who is a pastor of the Universal Life Church. He is also active in the Sexual Freedom League and has organized and operated a number of party clubs. During the periods in issue, appellant operated a club called THAD's. The club was designed to provide a location where sexually uninhibited persons could go and enjoy a party atmosphere. The club furnished a buffet of hors d'oeuvres, music, television, and privacy rooms. However, alcoholic beverages were not sold. Guests of the club would fill out a membership card at their first visit and pay a $25 admission fee. On subsequent visits, the members would pay the same fee, but were only required to sign the guest register.

Because of the sexual activities occurring at the club, a police raid was carried out and appellant was arrested for operating a house of prostitution. Appellant was eventually vindicated when an appellate court found that the parties were personal affairs and not criminal activities. During this period, appellant did not file tax returns. Respondent, therefore, determined that the collection of taxes owed by appellant was in jeopardy and had jeopardy assessments issued. In computing these assessments respondent reviewed records held by the police. Respondent found that during an eight-month period in 1983, 2,350 persons filled out membership cards and 3,469 persons used the facility after becoming members. In computing appellant's 1982 income, respondent used the following formula:

3469 ÷ 8 = 434 guests per month	
434 x 12 = 5208 guests per year	
5208 x $25 =	$130,200
2,350 actual membership cards purchased in 1982 x $25	58,750
	$188,950

In computing appellant's income for the first two months of 1983, respondent used the following formula:

434 guests per month x 2 months x $25 = $21,700
850 actual membership cards x $25 = 21,250

$42,950

Two hearings were held between appellant and respondent in which appellant maintained that the income projections made by respondent were inaccurate. Appellant, however, did not present any evidence to refute respondent's findings.

Section 18401 requires individuals to file returns with the Franchise Tax Board which specifically state that individual's income. For the taxable periods in question, appellant did not file California personal income tax returns. When appellant was arrested for operating a house'of prostitution, respondent was notified by law enforcement authorities of the unreported income seized from appellant. Using the records seized during this raid of appellant's club, respondent reconstructed appellant's unreported income. It is settled law that respondent's determinations of tax are presumptively correct and that the taxpayer bears the burden of proving them erroneous. (Appeal of Robert E. Le Doux, Cal. St. Bd. of Equal., May 21, 1980.)

Each taxpayer is required to maintain such accounting records as will enable him to file an accurate return. (Appeal of Glen Alexander, Cal. St. Bd. of Equal., Feb. 4, 1986.) In the absence of such records, the taxing agency is authorized to compute a taxpayer's income by whatever method will, in its judgment, clearly reflect income. (Rev. & Tax. Code, § 17561, subd. (b).) The existence of unreported income may be demonstrated by any practical method of proof that is available in the circumstances of the particular situation. (Davis v. United States, 226 F.2d 331, 336 (6th Cir. 1955); Appeal of Carl E. Adams, Cal. St. Bd. of Equal., Mar. 1, 1983.) Mathematical exactness is not required. (Harbin v. Commissioner, 40 T.C. 373, 377 (1963).)

In this case, respondent did an actual count of all the membership cards filled out by guests at their first visit to appellant's club. It also used appellant's guest register and counted the signatures of guests for eight months of 1982. We must conclude that respondent acted reasonably in basing its reconstruction of appellant's income on this evidence. We have previously held that in order to ensure that a reconstruction of income does not lead to injustice, each element

of the reconstruction must be based on fact rather than conjecture. (Appeal of Burr McFarland Lyons, Cal. St. Bd. of Equal., Dec. 15, 1976.) In this case, respondent used credible evidence in the record to support its reconstruction. Appellant has not presented evidence which can refute this finding or lead us to conclude that the assessment is arbitrary.

Likewise, appellant has failed to support his contention that he was not the owner of the club. Appellant's name was used to obtain the necessary permits for the club; his name was used in promoting the club; he was managing the club: he had possession of the money from the club; and he leased the property for the club. Without evidence that some other party owned the club, the findings of respondent cannot be reversed.

Finally, appellant claims certain deductions under section 17233 for an activity not engaged in for profit.[2/] In support of these deductions, appellant has submitted an unaudited listing of cash disbursements for the periods in issue. No receipts or other supporting documents were submitted despite numerous requests from respondent. Mere conclusionary listings without supporting evidence are unpersuasive. We must conclude that because deductions are a matter of legislative grace and because the one claiming the deductions bears the burden of proving the right to such deductions (New Colonial Ice Co. v. Helvering, 292 U.S. 435 [78 L.Ed. 1348] (1934)), appellant has failed to meet his burden of proof. The action of respondent must be sustained.

2/ For taxable years beginning on or after January 1, 1983, the state deductions for activities not engaged in for profit are the same as those allowed by the Internal Revenue Code in section 183. (Rev. & Tax. Code, § 17201.)

Appeal of Elbert B. Poppell

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 in denying the petitions of Elbert B. Poppell for reassessment of jeopardy assessments of personal income tax in the amounts of $19,213 and $3,153 for the year 1982 and the period January 1, 1983, to March 11, 1983, respectively, be and the same is hereby sustained.

Done at Sacramento, California, this 18th day of August, 1987, by the State Board of Equalization, with Board Members Mr. Collis, Mr. Dronenburg, Mr. Bennett and Mr. Carpenter present.

Conway H. Collis, Chairman

Ernest J. Dronenburg, Jr., Member

William M. Bennett, Member

Paul Carpenter, Member

_____, Member