BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
) No. 85J-590-MA
JOSEPH PORRAZZO)

Appearances:

For Appellant: J. Howard Sturman
Attorney at Law

For Respondent: Lorrie K. Inagaki
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 petition of Joseph Porrazzo for reassessment of a jeopardy assessment of personal income tax and penalties in the amount of $18,345 for the year 1982.

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

During taxable year 1982, appellant owned and operated an out-call massage service. Following an extensive police investigation appellant was arrested and convicted, after a plea of guilty, of conspiracy to commit pandering, a violation of section 182(1) of the Penal Code. Respondent reconstructed appellant's income using a per-transaction analysis which included both the cash and credit card receipts of the out-call service.

During the course of this appeal the parties stipulated to the amount of gross receipts received by the out-call business and to the fact that appellant was engaged in illegal activities proscribed by sections 266h or 266i of the Penal Code. There are two issues which remain to be resolved in this appeal: (1) whether section 17282, as amended, may be applied retroactively to disallow any deductions for the expenses of the out-call service, and (2) whether cash amounts received and retained by the party handling appellant's credit card services and by women performing out-call services should be allowed as exclusions from income.

Retroactive Application of Section 17282

Section 17282 generally disallows all deductions attributable to the income derived from various specified types of illegal activities. Appellant objects to the retroactive application of section 17282 in this case because the provisions relating to illegal income earned from pimping and pandering activities were not added until 1984. Appellant is correct that there is a general rule of statutory construction applicable to statutes and amendments alike, that unless the intention to make a statute retroactive clearly appears from the act itself, a statute will not be construed to have that effect. (In re Estate of Frees, 187 Cal. 150 [201 P.112] (1921).) However, appellant ignores the fact that subdivision (c) of section 17282 contains a retroactivity provision rendering the provisions of section 17282 applicable with respect to taxable years which have not been closed by a statute of limitations, res judicata, or otherwise. Such a provision clearly negates any presumption against retroactivity which would normally arise. (In re Marriage of Bouquet, 16 Cal.3d 583 [128 Cal.Rptr. 427] (1976).) In the instant appeal, the tax year under consideration has not been closed. As such, the provisions of section 17282, as amended to include pimping and pandering, are clearly applicable.

Gross Receipts

Appellant operated an out-call massage service which sent women to clients who arranged for "massage" services by

telephone. Clients could pay by cash or credit card. The standard fee was $50 for cash customers and $55 for credit card customers. It is conceded that some of the women who worked for appellant were guilty of prostitution (App. Br. at p. 1) and presumably collected more than the standard charge. The fee for "extra" services was termed a gratuity. According to appellant, when a client paid cash the out-call girl retained $20 as her portion of the fee and gave $30 to appellant. When a credit card was used, the entire amount of the credit card voucher was turned over to appellant. Appellant used a credit card "laundry" operation run by Scott Boswell in Texas. Mr. Boswell took appellant's credit card vouchers and ran them through the appropriate company under the names of W. T. Enterprises and/or Sydney's B.B.Q. When Boswell was paid by the credit card company, he kept a fee of approximately 20-30 percent and sent appellant a check for the remainder.

Appellant objects to the amount of gross income attributed to his business by respondent. Following a protest hearing, respondent's hearing officer recomputed appellant's income by using a per-transaction analysis. The hearing officer determined that when an out-call girl received cash for her services, the entire amount would be included in appellant's gross income. If the out-call girl received payment by credit card, the entire amount of the credit card charge was also included in appellant' gross income. Because section 17282 was applied, no deductions were allowed.

Appellant argues that $20 of each cash transaction should be excluded because this amount was retained by the out-call girls. He also argues that only the portion of the credit card charges paid to him by Mr. Boswell'should properly be considered part of his gross income since he did not receive the full amount paid by the customer.

We do not agree. It is clear that the out-call girls were "mere conduits" for appellant and that appellant was the beneficial owner of the money at the time it was paid by the customers. Even in cases where the taxpayer has no control of the funds and did not receive the cash in hand, he can be considered to have received the income. (O'Laughlin v. Helvering, 81 F.2d 269 (D.C. Cir. 1935).) Here, clearly the out-call employees were collecting the money for appellant and the total amount collected should be attributed to him. Mr. Boswell's fees were a cost of doing an illegal business which necessitated the use of a credit card "laundry" operation. Such expenses are clearly the type contemplated by the Legislature

under section 17282 and, as such, may not be deducted from any computation of appellant's gross income. (See also Automatic Cigarette, Sales Corp. v. Commissioner, 234 F.2d 825 (4th Cir. 1956).)2/

For the reasons stated above, respondent's actions in this matter will. be sustained in all respects.

2/ Both parties argued various aspects of the law regarding the "constructive receipt" of income. Strictly speaking this case did not involve constructive receipt (i.e., "when" the money was received), but rather "who" was the taxpayer with regard to the payments retained by the out-call girls and Mr. Boswell. (See generally, Mertens, Law of Federal Income Taxation, § 10.10.)

Appeal of Joseph Porrazzo

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 petition of Joseph Porrazzo for reassessment of a jeopardy assessment of personal income tax and penalties in the amount of $18,345 for the year 1982, be and the same is hereby sustained.

Done at Sacramento, California, this 6th day of April, 1989, by the State Board of Equalization,

Paul Carpenter, Chairman

Conway H. Collis, Member

William M. Bennett, Member

Ernest J. Dronenburg, Jr., Member

John Davies*, Member

*For Gray Davis, per Government Code Section 7.9.