BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of	)	
	)	Nos. 83A-846-SS
ROBERT F. AND HELEN R. ADICKES	)	84R-1294
	)	86A-1433

Appearances:

For Appellant: Cameron Faber and Richard D. Robins
Attorneys at Law

For Respondent: Anna Jovanovich
Counsel

OPINION

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 Robert F. and Helen R. Adickes against proposed assessments of additional personal income tax and fraud penalties in the total amounts of $8,411.94, $5,768.31 and $6,120.12 for the years 1976, 1977, and 1978, respectively, and pursuant to section 19057, subdivision (a), from the denial of their claim for refund of $3,963.00 for the year 1979.

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

The primary issue presented by this appeal is whether appellants were residents of California during the years 1976, 1977 and 1978, and, if so, whether the Franchise Tax Board correctly determined that appellants' filing of joint nonresident returns in those years constituted fraud. Secondary issues involve appellants' entitlement to claim deductions for expenses on alleged rental properties, partnership losses, employee business expenses, interest payments, medical payments, casualty losses, preference tax amounts, and other miscellaneous deductions disallowed by respondent's auditors.

Appellant-husband, during all of the appeal years, was a commercial airline pilot flying an international route. Until 1971 appellants lived together and filed joint resident income tax returns in California. Beginning with 1971 and continuing through 1978, appellants filed joint nonresident returns using a Nevada address. Appellants concede, despite the representation to the contrary on their nonresident returns, that Helen continued to reside in the family home at Thousand Oaks, California, during all of the appeal years. At this point in the proceedings, then, appellants are attempting to establish only Robert as a nonresident of California, and only for the years 1976 through 1978.

Appellants claim to have separated in 1970, the same year that Robert organized a Nevada corporation, Aviation Consultants, Inc., to provide consulting services relating to airplane crashes and development of new aeronautical prototypes. In subsequent years, while continuing to be employed by TWA, Robert entered into other business arrangements in Nevada (including a tax preparation service), obtained a Nevada driver's license, registered to vote in Nevada, opened bank and brokerage accounts and purchased real estate there.[2/] In 1977, Robert filed for divorce in Nevada. In 1979, he retired from TWA and moved back to the family home in Thousand Oaks.

In 1979, a private citizen informed respondent that Robert was bragging about not paying California taxes by using a

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2/ Appellant purchased a house in Nevada in May of 1976, sold it in March of 1978, and then purchased another house in February 1979.

false Nevada address.[3] This report led to an audit for the years within the statute of limitations, 1976 through 1979. The FTB thereupon determined that appellants were, in fact, California residents and assessed fraud penalties for each year. Appellants paid the basic assessment for 1979, conceding residency for that year, but filed a claim for refund on other grounds.

Although appellants concede on appeal that Mrs. Adickes was a California resident during all years at issue, they maintain that, prior to their reconciliation in 1979; Mr. Adickes was a resident of Nevada. They explain their filing of joint nonresident returns as resulting from their erroneous belief that Helen's California residency did not defeat their joint nonresident status because their only income was Robert's[4] and that income was his separate property because of their separation. The sincerity of this claim is at issue infra, in consideration of the fraud issue.

Revenue and Taxation Code section 17014, subdivision (a), defines the term "resident" to include:

> (1) Every individual who is in this state for other than a temporary or transitory purpose.
>
> (2) Every individual domiciled in this state who is outside the state for a temporary or transitory purpose:

Section 17014, subdivision (c), also states that:

> Any individual who is a resident of this state continues to be a resident even though temporarily absent from the state.

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[3] Information in 1976 from a similar source had resulted in an extensive investigation by respondent for failure to file in 1971-1975. The case was referred to the Ventura County District Attorney for criminal fraud prosecution. The District Attorney ultimately declined to prosecute, citing insufficient prosecutorial resources to pursue nonviolent crimes.

[4] According to appellants, Helen's horse breeding farm in Thousand Oaks generated only losses.

Respondent's regulation 17014 provides that the underlying theory of the residency sections "is that the state with which a person has the closest connection during the taxable year is the state of his residence." (Cal. Code Regs., tit. 18, reg. 17014.)

Respondent's determination of residency status and the proposed assessments based thereon are presumed to be correct, and the taxpayer bears the burden of proving respondent's actions erroneous. (Appeal of Robert J. Addinoton, Jr., Cal. St. Bd. of Equal., Jan. 5, 1982; Appeal of Patricia A. Green, Cal. St. Bd. of Equal., June 22, 1976.)

In another appeal by an airline pilot - this one having been reassigned to a base in Texas - we found that the appellant's admission that he spent between 82 and 118 days with his family in California during one of the appeal years was "significant in light of the fact that he only had 127 days during that year when he was not either flying or attending ground school." (Anneal of Warren L. Christianson, Cal. St. Bd. of Equal., Aug. 17, 1983. See also Appeal of Warren L. and Marlvs A. Christianson, Cal. St. Bd. of Equal., July 31, 1972.) We found that appellant Christianson's contacts with Texas, including living in a rented apartment in Dallas, owning rental property and a business, voting, maintaining a driver's license and actually serving on jury duty, were outweighed by his California contacts. Although appellant Christianson, like appellant Robert Adickes, indicated at one point in his appeal that he was separated from his wife during the appeal years, we found insufficient evidence thereof. Rather, we found that he was "[m]aintaining a family home and raising children in this state ... important indications of California residency. [Citation omitted.]"

In another airline pilot appeal, we held the taxpayer to be a resident of California despite his successive assignments to Saudi Arabia and New York and separation from his wife. (Appeal of Barrv H. Xeeling, Cal. St. Bd. of Equal., Oct. 9, 1985.) We noted that appellant Keeling kept his telephone listing and car in La Jolla, that he returned to California many times for his medical and business needs and claimed the homeowner's exemption on his La Jolla real property. We found, "appellant has not shown that his connections with any other location were greater than his connections with this state."

Appellant's claim of Nevada residency is substantially contradicted by sworn representations made by appellant himself at hearings on unrelated securities fraud litigation brought against him by a business associate. In affidavits executed in 1980, appellant Robert stated he was a "citizen and domiciliary of the City of Thousand Oaks, County of Ventura, State of California, from 1972 on." (Emphasis added.) (Resp. Br., Apr. 2, 1985, Ex. D.) In a 1980 deposition for the same case, he claimed to have been living at the family home at 747 Camino Las Conchas, Thousand Oaks, from 1975 on, "except for a period of about a year in 1976 or 1977." (Resp. Br., Ex. B, p. 11.) When questioned further about that year, he stated that he was in Texas and New York, where he at one time owned a residence, and he did not mention Nevada. He never filed income tax returns in any state other than California. Similar to appellant Christianson, Robert admitted in deposition that he spent an average of 6 days a month at the family home in California and 12-14 days a month flying for TWA. In another 1980 deposition, he stated that he had resided with his wife while in the United States. When questioned about his Nevada properties and post office box, he did not mention the house purchased in 1976, and he stated that he had never spent so much as one night at the other address. He explained that he used a Nevada address for TWA's emergency notification because it had an answering service. He claimed that the Nevada post office box was maintained not by him, but by a "company I'm associated with." (Resp. Br., Ex. B, at 23). At the federal court hearing, an associate testified to forwarding Robert's mail during the appeal years from the Nevada post office box to appellants' home in Thousand Oaks. 5/

5/ Appellant makes much of the fact the statements made in the affidavits and deposition referred to above were intended to establish California residency not for tax purposes but in order to defeat federal diversity jurisdiction in an unrelated case. Appellant analogizes to the different standards required to establish residency for divorce jurisdiction and income tax liability. While we agree that the test for the conclusion of residency in different legal settings may differ, the facts elicited in the diversity proceeding are clearly relevant to our inquiry and constitute "the sort of evidence upon which responsible persons are accustomed to rely in the conduct of serious affairs." (Cal. Code Regs., tit. 18, reg. 5035, subd. (c).)

Like appellants Christianson and Keeling, Robert's contacts with Nevada appear to us to be significantly outweighed by his continuing contacts with California, where he (1) owned a personal residence in Thousand Oaks inhabited by his wife and children, as well as three other houses inhabited by relatives; (2) maintained five bank and three brokerage accounts, and actually opened new bank accounts in California during the appeal years, giving his Thousand Oaks, California, address, as his "current residence"; (3) owned interests in and served as director and manager of several corporations licensed to do business in California; and (4) held a California driver's license and maintained a California-registered vehicle.

With respect also to appellant Robert's claim to have been separated from his wife during the appeal years, this case parallels the Christianson appeal. The record does not support the claim - but not simply as a matter of omission as in Christianson. In the instant case, the claim of marital rupture, although somewhat buoyed by evidence of an actual divorce filing in 1977, is laced with questions and contradictions. The separation is not mentioned 'in the federal diversity proceedings, and, when asked in 1980 if he had been contemplating divorce in 1975-1976, Robert answered that he "could not recall." (Resp. Br., Ex. B., p. 17.) In light of the evidence, detailed infra, that appellants were engaged in a long-term scheme to evade California income taxes, we are unable to credit appellants' attempt to portray their relationship as estranged. Regardless, however, of the state of his relationship with Helen, Robert, like appellant Keeling, has not shown that his connections with any other location are more substantial than his connections with this state. (Cal. Code Regs., tit. 18, reg. 17014.)

We find that appellants have not met their burden of proving that Robert was not a California resident during the appeal years. The question of fraud, however, is a separate matter, involving analysis and evaluation of additional facts and evidence and a higher standard of proof for which the burden rests upon respondent.

Respondent alleges fraud in appellants' continuing misrepresentation of facts relating to Robert's residency status and concededly erroneous representation of Helen Adickes' residency status in the declaration submitted with the nonresident returns. The burden of proving fraud is upon the respondent, and it must be established by clear and convincing evidence, something more than a slight preponderance of the evidence.

"Clear and convincing" has been defined as "explicit and unequivocal," leaving "no substantial doubt," and "sufficiently strong to command the unhesitating assent of every reasonable mind." (In re Jost, 117 Cal.App.2d 379, 383 [256 P.2d 71] (1953).) The taxpayer must have "the specific intent to evade a tax believed to be owing." (Appeal of George W. Fairchild, Cal. St. Bd. of Equal., Oct. 27, 1971.) Intent is of course rarely susceptible of direct proof and must usually be inferred from the totality of facts and circumstances in a case. (People v. Kuykendall, 134 Cal.App.2d 642, 645 [285 P.2d 996] (1955).) We have repeatedly found that circumstantial evidence may be used by respondent to meet its burden of proving fraud. (See e.g., Appeal of Garv 0. Armstrong, Cal. St. Bd. of Equal., Dec. 10, 1981.)

When appellants filed returns with respondent during the years on appeal, they signed a certification under penalty of perjury that they were both nonresidents of California and that they were both living in Nevada. The address they provided on their nonresident returns was a Nevada post office box. Now appellants concede that Helen Adickes was in fact living in California during all of the appeal years and that Robert was a California resident in 1979. The tax rate for nonresidents filing jointly is lower than the rate for a nonresident filing separately from his resident spouse. Absent some credible explanation for the contradiction, then, we find that the FTB has presented clear and convincing evidence of a fraudulent attempt to evade taxes. Appellants' argument that Robert's income during the appeal years was separate income is unavailing for several reasons: (1) it is based on the tenuous, if not discredited, claim that appellants were separated, with no intent to reconcile, during those years; (2) even if appellants were separated, the evidence indicates that they were continuing to hold themselves out as a married couple during the years at issue, making Robert's income community income (see In re Marriage of Marsden, 130 Cal.App.3d 426 [181 Cal.Rptr. 910] (1982)); and (3) even if they were separated and Robert's income were considered separate income, he should have filed a separate nonresident return at a higher tax rate. Section 18685 provides that fraud is established "[i]f any part of any deficiency is due to fraud with intent to evade tax." (Emphasis added.) To defeat this third point, appellants have intimated in their briefs that their decision to file joint nonresident returns was made pursuant to legal advice. At the hearing before this board, however, appellants' tax attorney denied having given any such advice, leaving the clear and convincing appearance of fraud intact.

Even if a joint return had not been filed and Helen Adickes had not been misrepresented as a nonresident of California, we would find a fraudulent intent on the part of Robert to evade income tax by his own false claim to be a Nevada resident. Appellants argue that Robert relied on legal advice in arranging his affairs, in making contacts in Nevada and in filing as a nonresident of California, and he is therefore immune from fraud penalties. However, clear and convincing expert testimony presented by respondent at the hearing established to our satisfaction that the four documents submitted by appellant to prove his reliance on professional advice were themselves fraudulent.

Appellants also contest respondent's disallowance of various deductions claimed on their nonresident returns. The principle is well established that deductions are a matter of legislative grace. (New Colonial Ice Co. v. Helvering 292 U.S. 435, 440 [78 L.Ed. 1348] (1934).) Moreover, respondent's determinations of tax are presumptively correct, and appellants bear the burden of proving them to be erroneous. (Appeal of K. L. Durham, Cal. St. Bd. of Equal., Mar. 4, 1980.)

With respect to the deductions claimed by appellants for maintenance expenses on properties characterized as "residential rentals," respondent's audit disclosed that the properties were the principal residences of Helen's mother, also listed as a "dependent" of appellants, and Robert's mother, who was found to be paying rent at far below fair market value. Respondent's auditors allowed the deduction for taxes and interest but disallowed the expenses and depreciation pursuant to Revenue Ruling 75-14, 1975-1 C.B. 90.[6/]

[6/] Because Revenue and Taxation Code section 17233 is similar in content to section 183 of the Internal Revenue Code, federal interpretations of that section are highly persuasive in interpreting the California law. (Cf. Rihn v. Franchise Tax Board, 131 Cal.App.2d 356) [280 P.2d 893] (1955).) Revenue Ruling 75-14, 1975-1 C.B. 90, provides that, when a home is rented to a relative at less than fair market value, interest and taxes are fully deductible, but the operating expenses are deductible only to the extent the gross income from the rental exceeds the interest and taxes, and depreciation is deductible only to the extent the gross income from the rental exceeds the interest, taxes and operating expenses.

Appellants' unsubstantiated assertions do not meet their burden of proving respondent's determination to be erroneous, and we therefore sustain respondent's disallowance of rental expenses.

Respondent disallowed appellants' deductions for certain partnership losses due to appellants' written refusal to provide information requested by respondent. Appellants' representative based the refusal on the specious claim that appellants were under no obligation to provide income information on the partnerships because the partnerships themselves were not under audit. We agree with respondent that the statutory provisions for individual tax liability of partners clearly impose on appellants the obligation to provide the information requested, and we accordingly sustain respondent's disallowance of the partnership losses.

Appellants claimed a deduction of $20,050 in expenses related to Robert's job as a pilot for T.W.A., amounting, according to the calculations of respondent's auditor, to approximately $120 per day. Respondent, pursuant to its own determination of reasonable living expenses, disallowed all but $75 per day, and appellants have failed to produce evidence that more was expended or required. Accordingly, appellants have not met their burden of proof, and respondent's disallowance of this deduction is sustained.

Appellants claimed deductions for interest paid on funds allegedly borrowed from relatives and from a "trust" for which appellants were the sole trustors, trustees and beneficiaries. Respondent determined that some of the borrowed money was used to pay the debts of one of Robert's corporations, debts relating to the purchase of certain harvest machines from which the corporation received rental income. Appellants never explained how they as individuals would be personally liable for the corporate debts. Respondent determined that the interest was subject to the limitations of section 17203 on investment interest. Respondent also disallowed alleged interest payments to appellants' relatives and the "trust" because appellants failed to provide substantiation that any real debts existed. Again, based on inadequate proof of indebtedness, we uphold the action of respondent.

Other deductions disallowed by respondent include medical expenses in excess of the statutory limit of section 17253, State Disability Insurance deducted in violation of section 17204, and unsubstantiated charitable contributions and excessive casualty losses. In their brief of June 1985,

appellants assured this board that they could "provide documentation to support any disallowed deductions." No such documentation has been provided. Accordingly, we find that appellants have not met their burden of proof with respect to the above-mentioned deductions.

For the reasons stated, respondent's action in assessing additional personal income tax and fraud penalties and denying appellants' claim for refund will be sustained.

Appeal of **Robert F. and Helen R. Adickes**

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 sections 18595 and 19060 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of Robert F. and Helen R. Adickes against proposed assessments of additional personal income tax and fraud penalties in the total amounts of **$8,411.94, $5,768.31,** and **$6,120.12** for the years 1976, 1977, and 1978, respectively, and in denying their claim for refund of **$3,963.00** for the year 1979, be and the same is hereby sustained.

Done at Sacramento, California, this 27th day of November, 1990, by the State Board of Equalization, with Board Members Mr. Collis, Mr. Dronenburg, Mr. Bennett, and Mr. Davies present.

Conway H. Collis, Chairman

Ernest J. Dronenburg, Jr., Member

William M. Bennett, Member

John Davies*, Member

_____, Member

*For Gray Davis, per Government Code section 7.9