



BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
ALEXANDER F. AND JOSEPHINE ZABOSKI)

Appearances:

For Appellants: Alexander F. Zaboski, in pro. per.
For Respondent: F. Edward Caine, Senior Counsel

O P I N I O N

This appeal is made pursuant to Section 18594 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Alexander F. and Josephine Zaboski to proposed assessments of additional personal income tax in the amounts of \$948.86, \$2,352.06 and \$804.85 for the years 1952, 1953 and 1954, respectively.

Appellant Alexander F. Zaboski (hereinafter called Appellant) conducted a coin machine business in the Gardena area. During 1952, 1953 and part of 1954, Appellant owned about eight multiple-odd bingo pinball machines, five flipper pinball machines and three music machines. The equipment was placed in eight or nine locations and the proceeds from each machine, after exclusion of expenses claimed by the location owner in connection with the operation of the machine, were divided equally between Appellant and the location owner.

The gross income reported in tax returns was the total of amounts retained from locations, Deductions were taken for depreciation, phonograph records, and other business expenses* Respondent determined that Appellant was renting space in the locations where his machines were placed and that all the coins deposited in the machines constituted gross income to him. Respondent also disallowed all expenses pursuant to Section 17359 (now 17297) of the Revenue and Taxation Code which read:

In computing net income, no deductions shall be allowed to any taxpayer on any of his gross income derived from illegal activities as defined in Chapters 9, 10 or 10.5 of Title 9 of Part 1 of the Penal Code of California; nor shall any deductions be allowed to any taxpayer on any of his gross income derived from any other

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activities which tend to promote or to further, or are connected or associated with, such illegal activities.

The evidence indicates that the operating arrangements between Appellant and each location owner were the same as those considered by us in Appeal of C. B. Hall, Sr., Cal. St. Bd. of Equal., Dec. 29, 1958, 2 CCH Cal. Tax Cas. Par. 201-197, 3 P-H State & Local Tax Serv. Cal. Par. 58145. Our conclusion in Hall that the machine owner and each location owner were engaged in a joint venture in the operation of these machines is, accordingly, applicable here. Thus, only one-half of the amounts deposited in the machines operated under the arrangements was ~~includible~~ in Appellant's gross income.

In Appeal of Advance Automatic Sales Co., Cal. St. Bd. of Equal., Oct. 9, 1962, CCH Cal. Tax Rep. Par. 201-984, 2 P-H State & Local Tax Serv. Cal. Par. 13288, we held the ownership or possession of a pinball machine to be illegal under Penal Code Sections 330b, 330.1 and 330.5 if the machine was predominantly a game of chance or if cash was paid to players for unplayed free games, and we also held bingo pinball machines to be predominantly games of chance.

It was the general practice to pay cash to players of Appellant's multiple-odd bingo pinball machines for free games not played off. Accordingly, the bingo pinball phase of Appellant's business was illegal, both on the ground of ownership and possession of bingo pinball machines, which were predominantly games of chance and on the ground that cash was paid to winning players. Respondent was therefore correct in applying Section 17359.

Appellant's coin machine business was highly integrated with Appellant collecting from all types of machines and the repairman servicing all types of machines. There was therefore a substantial connection between the illegal operation of bingo pinball machines and the legal operation of flipper pinball machines and music machines and Respondent was correct in disallowing all the expenses of the business.

There were no records of amounts paid to winning players on bingo pinball machines, and Respondent estimated these unrecorded amounts as equal to 60 percent of the total amounts deposited in those machines. Respondent's auditor testified that the 60 percent payout figure was based upon estimates given by Appellant and a location owner when interviewed at the time of the audit. Two location owners having Appellant's bingo pinball machines testified at the hearing of this matter. One testified that cash payouts to winning players for unplayed free games constituted about 60 percent of the proceeds in the machine. The

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other testified that cash payouts averaged about 50 percent. Appellant testified that most of the time cash payouts were over 50 percent. The testimony is consistent with the 60 percent estimate used by Respondent and it must be sustained.

In connection with the computation of the unrecorded payouts it was necessary for Respondent's auditor to estimate the percentage of Appellant's recorded gross income arising from the multiple-odd bingo pinball machines since Appellant's records did not segregate the income from the various kinds of coin machines. When interviewed during the audit, Appellant estimated that the receipts from bingo pinball machines constituted 50 percent of the total receipts from the various machines in 1952 and 75 percent in 1953 and 1954. These estimates were used in Respondent's computation and Appellant reaffirmed his estimates at the hearing. Accordingly, we can see no reason to disturb them.

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 Alexander F. and Josephine Zabolski to proposed assessments of additional personal income tax in the amounts of \$948.86, \$2,352.06 and \$804.85 for the years 1952, 1953 and 1954, respectively, be modified in that the gross income is to be recomputed in accordance with the opinion of the Board. In all other respects the action of the Franchise Tax Board is sustained.

Done at Sacramento, California, this 18th day of June, 1963,
by the State Board of Equalization.

John W. Lynch, Chairman

Paul R. Leake, Member

Richard Nevins, Member

_____, Member

_____, Member

ATTEST: Dixwell L. Pierce, Secretary