



BEFORE THE STATE BOARD OF EQUALIZATION
OF THE: STATE OF CALIFORNIA

In the Matter of the Appeal of }
WILLIAM F. AND SHIRLEY M. PARKER }

Appearances:

For Appellants: Benjamin Neuman
Attorney at Law
Martin Leance and Michael D, Kastner
Certffied Public Accountants
For Respondent: Gary Paul Kane
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 William F. and Shirley M. Parker against a proposed assessment of additional personal income tax in the amount of \$18,298.28 for the year 1964.

Two issues are raised by this appeal. The first concerns whether or not a certain agent's commission was deductible as an ordinary and necessary business expense of appellants. The second question is whether or not appellants properly reduced their reported gain on a corporate liquidation by the amount of taxes subsequently assessed against that corporation, although the assessment was not paid by appellants until a later taxable year.

Appellants are husband and wife. He is a motion picture producer and she is an actress, known professionally as Shirley MacLaine. Prior to January 17, 1964, appellants

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owned all of the stock of Sachiko Productions (hereafter referred to as "Sachiko" or "the corporation"). Sachiko employed Miss MacLaine to appear in five motion pictures to be made during the years 1959 through 1964. Rather than produce the films itself, Sachiko "loaned out" the services of Miss MacLaine to other filming companies. Under this arrangement receipts from Miss MacLaine's performances in each movie were paid to the corporation, which paid her a fixed weekly salary,

On January 17, 1964, Sachiko was dissolved. Among its corporate assets was a "loan-out" contract-with a motion picture production company calling for Miss MacLaine's performance in the film "Irma La Douce." Although that movie had not yet been made, the contract was valued at \$620,000 on the corporation's books at the time of Sachiko's liquidation. Ten percent of that value, or \$62,000, was payable to Miss MacLaine's agent under an artist's management contract.

Since receipts from "Irma La Douce" did not begin coming in until after Sachiko had been dissolved, appellants personally paid the \$62,000 to Miss MacLaine's agent. In their federal and state income tax returns for 1964 appellants deducted the \$62,000 as a business expense. The Internal Revenue Service determined that the agent's commission should be allowed as an offset in computing gain realized by appellants on the liquidation of Sachiko, rather than as a fully deductible business expense of appellants. Respondent acted in conformity with that federal determination, and that action, gave rise to the first issue presented by this appeal.

Shortly after the dissolution of Sachiko, the Internal Revenue Service issued deficiency assessments against that corporation. Appellants paid those assessments in 1966.

On their 1964 federal and state income tax returns appellants deducted the assessed federal deficiencies from the reported liquidation proceeds which they received from Sachiko. The Internal Revenue Service disallowed that reduction in gain, on the ground that tax liability as a transferee is not deductible until it is paid. After the appellants paid the deficiencies in 1966 they were permitted to recompute the liquidation proceeds received from Sachiko, under the provisions of section 1341 of the Internal Revenue Code of 1954. A federal refund was allowed on the basis of that recomputation.

In conformity with the federal action, respondent disallowed the federal deficiencies which were deducted in computing capital gain on appellants' 1964 state return. That action gave rise to the second issue presented here.

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It is well established that a determination by respondent based upon federal action is presumed to be correct and the burden is on the taxpayer to prove it erroneous. (Todd v. McColgan, 89 Cal. App. 2d 509 [201 P.2d 414]; Appeal of Harry and Tessie Somers, Cal. St. Bd. of Equal., Mar. 25, 1968.) Since respondent acted in accordance with the determinations of the Internal Revenue Service in the instant case, the presumption of correctness arises with respect to both issues.

I. Agent's Commission

Appellants contend that agents' commissions are ordinary and necessary business expenses of professional entertainers. They argue that since they personally received Miss MacLaine's share of the proceeds from the film, "Irma La Douce," and they in fact paid the \$62,000 due Miss MacLaine's agent with respect to that movie, they are entitled to deduct that amount as a business expense on their personal income tax return.

Respondent points out that the contract for Miss MacLaine's services in "Irma La Douce" was an asset of the corporation at the time of its liquidation. Respondent contends that the \$62,000 paid to Miss MacLaine's agent was an expense incurred with respect to that contract, and if it was to be treated as an expense at all it was an expense of the corporation and not of appellants as individuals, in spite of the fact that appellants themselves paid the commission after the corporate liquidation.

'For tax purposes a corporation is generally treated as an entity separate and distinct from its stockholders. (Burnet v. Clark, 287 U.S. 410 (77 L. Ed. 397).) It is well settled that one taxpayer may not deduct expenses properly belonging to another taxable entity. (Deputy v. du Pont, 308 U.S. 488 [84 L. Ed. 416].) Thus, where expenses have their origin in the business of a corporation, they are not deductible by a stockholder in that corporation, even though he may in fact pay them. (Deputy v. du Pont, supra; Walton O. Hewett, 47 T.C. 483; W. F. Strasburger, T.C. Memo., Oct. 30, 1962.)

Prior to its dissolution on January 17, 1964, Sachiko was in the business of "loaning out" Miss MacLaine's services to movie production companies. During the years 1959 through 1963 it had received the proceeds from her films and had in turn paid Miss MacLaine a weekly salary. Although Sachiko dissolved prior to the time "Irma La Douce" was filmed, it did hold the contract for that movie as a corporate asset.

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If it had continued in existence until that movie was released, the corporation would have received the income due Miss MacLaine from that film, as it had in the case of her earlier movies. Furthermore, at the time Miss MacLaine agreed to perform in "Irma La Douce," which was before Sachiko dissolved, she knew that under the artist's management contract with her agent she would owe him 10 percent of the proceeds from that film.

Under the circumstances, we conclude that the \$62,000 agent's commission had its origin in the corporation's contract to "loan-out" Miss MacLaine for that film. This conclusion is not changed by the fact that it was appellants who actually received the income from "Irma La Douce" and paid the commission, after Sachiko was dissolved. We must agree with respondent that appellants have failed to establish they were entitled to the \$62,000 deduction on their personal income tax returns for 1964. Respondent's action in this matter, conforming as it did to the federal determination on the same question, must therefore be sustained.

II. Tax Deficiencies on Liquidation

With respect to the second issue appellants reason that in 1964 they knew the amount of the federal deficiency assessment against Sachiko, and they knew they would be liable for those assessments as transferees of the assets of that corporation; therefore, their reportable gain from the corporate liquidation in 1964 was the total gain reduced by the amount of the federal deficiency assessments, notwithstanding the fact that appellants did not pay those assessments until a subsequent taxable year. Appellants concede that the Internal Revenue Service did not allow such a reduction in their reported gain in the year of liquidation. They contend, however, that the same result was reached under the provisions of section 1341 of the Internal Revenue Code of 1954, which allowed a recomputation of gain when the deficiency assessments were paid in 1966. Appellants urge that in the absence of any similar relief provision in California law respondent should not have acted in conformity with the federal action on this issue.

Prior to the enactment of section 1341 of the Internal Revenue Code of 1954 it was well settled that where the transferee of the assets of a liquidated corporation was required to pay a tax deficiency against the dissolved corporation in a later taxable year, the payment constituted a capital loss in the year of payment and could not be used as an offset against the capital gain in the year of dissolution. (Stanley Switlik, 13 T.C. 121, aff'd 184 F.2d 299; Roberta Pittman,

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14 T.C. 449.) This rule has its basis in the annual accounting concept (Burnet v. Sanford & Brooks Co., 282 U.S. 359 [75 L. Ed. 383]) and in the "claim of right" doctrine (North American Oil Consolidated v. Burnet, 286 U.S. 417 [76 L. Ed. 1197]).

Since section 1341 of the Internal Revenue Code of 1954 has no counterpart in California law, we must be governed by the above mentioned cases which were decided before the enactment of the federal relief provision. In refusing to allow appellants to reduce their gain from the corporate liquidation in 1964 by the amount of the assessed federal tax deficiencies paid in 1966, respondent clearly followed those cases. Appellants have failed to prove that action erroneous.

ORDER

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 William F. and Shirley M. Parker against a proposed assessment of additional personal income tax in the amount of \$18,298.28 for the year 1964, be and the same is hereby sustained.

Done at Sacramento, California, this 26th day of February, 1969, by the State Board of Equalization,

John W. Lynch, Chairman
Paul R. Keane, Member
Paul Keane, Member
_____, Member
_____, Member

Attest: [Signature], Secretary