



Appeal of Custom Component Switches, Inc..

The question presented is whether, in computing its income subject to taxation by California, appellant, a California corporation, may deduct the entire amount of the distributive partnership losses incurred by a partnership in which appellant is a general partner.

Appellant's major corporate business activity is the manufacture and sale of specialized electrical switches and related components. Appellant is also a general partner in a partnership known as Plymouth Realty Company (**Plymouth**). The sole activity of Plymouth is the ownership and rental of real property, primarily factory buildings and shopping centers. The properties are located both within and without California. None of Plymouth's properties were rented to appellant or used in connection with appellant's business.

During each of the years in issue, Plymouth incurred substantial losses from its business operations. These losses were generated, primarily, by depreciation expenses associated with Plymouth's rental properties. Appellant included its distributive share of Plymouth's business losses in its return of income for the years in issue. Respondent allowed the partnership losses to the extent that they were **generated** by property located within the state and, therefore, attributable to a California source. However, to the extent the partnership losses were **attributable to** property located out of state, respondent denied the deductions on the basis that they were from sources outside California.

The net **income** by which the franchise tax is measured is restricted to net income from California sources. (Rev. & Tax. Code, **§ 25101.**) Income from California sources includes income from tangible or intangible property located or having a **situs** in this state, and any income from activities carried on here. (Rev. & Tax. Code, **§ 23040.**) Conversely, any losses from California sources are deductible while losses attributable to out of state sources are not deductible. (See Appeal of H. F. Ahmanson & Co., Cal. St. Rd. of Equal., April 5, 1965.)

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The Appeal of H. F. Ahmanson & Co., supra, presented a very similar issue. In Ahmanson the corporate appellant was primarily engaged in **the insurance** business. However, the appellant was also a limited partner in two partnerships engaged in oil exploration in Turkey. The partnerships incurred losses in the oil venture and appellant attempted to deduct those losses from its California income. In denying the appellant's claim, this board concluded that the source of a partner's income is where the property of the partnership is located and where the partnership activity is carried on.

The only difference between Ahmanson and **the** present appeal is that in the former none of the partnership property was located in California while in the latter some property was located in this state. However, as noted above, allowance was made for that portion of the partnership's losses associated with partnership property located within California.

In view of the principles announced in Ahmanson, it is apparent that only income or loss attributable to California sources can be included in determining income taxable by California. Since the deductions in question arose only from partnership property located outside California, it follows that respondent's action in disallowing the deductions was correct and must be sustained.

ORDER

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

