

BEFORE THE STATE BOARD OF EQUALIZATION  
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of )  
MARSHALL D. AND **UNA F. JOELSON**) NO. **84A-1147-SW**

Appearances:

For Appellants: Charles Stuhr  
Attorney at Law

For Respondent: **Lorrie K.** Inagaki  
Counsel

O P I N I O N

This appeal is made pursuant to section **18593<sup>1/</sup>** of the Revenue and Taxation Code from the action of the Franchise Tax **Board on** the protest of Marshall D. and Una F. **Joelson** against a proposed assessment of additional personal income tax in the amount of \$1,427 for the year 1980.

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

Appeal of Marshall D. and Una F. Joelson

This appeal is made by Marshall D. and Una F. **Joelson**; however, Mrs. **Joelson** is a party to this action solely because of her filing a joint return with her husband. Consequently, "appellant" will hereinafter refer to Mr. **Joelson**.

The issue presented in this appeal is whether appellant has shown that he is entitled to a bad debt deduction for taxable year **1980**.

In late 1971, appellant was a practicing certified public accountant with offices in Daly City, California. Among appellant's more important clients were Richard and Mary **Bywater** of **Bywater** Construction Company. At this time, appellant loaned Mr. **Bywater** **\$6,500**. In February 1972, a second loan of \$7,000 was made. Shortly after the second loan, appellant made two more loans totaling \$12,000.

On October 1, 1972, appellant accepted a position as controller of the **Bywater** Construction Company. Appellant also made another loan of \$5,000 after he became controller which served as an advance for initial working capital for a small construction equipment repair company newly formed by appellant and Mr. **Bywater**. None of these loans were evidenced by a note. No interest was provided for and no collateral **was** secured.

In the winter of 1972, the **Bywater** Construction Company began to experience severe financial difficulties due to losses and penalties sustained on a large construction contract. Appellant was subsequently dismissed from his controller position.

On June 16, 1974, Mr. **Bywater** acknowledged his **debt to appellant** in the form of an executed note for **\$35,500.**<sup>2/</sup> The amount was to be paid in monthly installments of **\$500** beginning on August 1, 1974, and continuing until July **1**, 1979, when the entire unpaid balance with interest would be paid. The interest rate was set at 7.5 percent per annum.

<sup>2/</sup> The available facts show loans of \$6,500 in 1971; **\$7,000** in February of 1972; \$12,000 later in 1972; and \$5,000 after becoming controller. These amounts total \$30,500. The note was in the amount of \$35,500. There is no evidence in the record which accounts for the \$5,000 difference.

Appeal of Marshall D. and Una F. Joelson

By mid-1976, Mr. **Bywater** had left the country to take a construction job in Africa. No legal action was taken to force payment even though no money or assets were received in payment of the note.

On his 1980 personal income tax return appellant claimed a bad debt loss deduction of \$30,500. Respondent denied the deduction and issued a proposed assessment.

Appellant contends that the loans were bona fide business loans because they were made to create additional work for appellant's firm from **Bywater** Construction Company and to promote further contact with Mr. Bywater's numerous relatives and business acquaintances. Appellant further contends that several of the loans were made so that he could secure the position of controller with **Bywater** Construction Company, a then-expanding business.

Appellant alleges that no payments were made to him during late 1972 and 1973 because the heavy rains that winter prevented the company from completing a large contract. When appellant began to demand payment; hard feelings developed and his job with the company was terminated. Before Mr. **Bywater** took his job in Africa, appellant alleges that he told appellant that he would pay the obligation as soon as he could accumulate the money from his job in Africa. **Mrs. Bywater** allegedly reiterated these intentions until 1980, when her attitude toward repayment changed. Finally, appellant contends that he and his attorney made numerous efforts to enforce collection. They did not take formal legal action because of fears that such action would alienate Mr. **Bywater** and counteract his then-professed good intentions. Since Mr. **Bywater** left for Africa, appellant has been unable to determine his whereabouts. In a letter to appellant, dated October 15, 1981, appellant's attorney, Charles Stuhr, advised appellant that procedures to enforce collection would be a waste of time and money.

Business bad debt losses are fully deductible in the year sustained whereas nonbusiness bad debt losses are regarded as short-term capital losses. (Rev. & Tax. Code, § 17207, subd. (d)(1)(B).) The term "nonbusiness debt" is defined in section 17207, subdivision (d)(2)(A) and (B), as a debt other than:

(A) A debt created or **acquired (as the case may be)** in connection with a trade or business of the taxpayer; or

Appeal of Marshall D. and Una F. Joelson

(B) A debt **the loss** from the **worthlessness** of which is incurred in the taxpayer's trade or business.

The provisions of section 17207 are substantially the same as section 166 of the Internal Revenue Code. It is well settled in California that when state statutes are patterned after federal legislation on the same *subject*, the interpretation and effect given the federal provisions by the federal courts and administrative bodies are relevant in determining the proper construction of the California statutes. (Andrews v. Franchise Tax Board, 275 Cal.App.2d 653, 658 [80 Cal.Rptr. 403] (1969).)

Respondent's position is that appellant's contentions should fail because (1) the debt is not bona fide, and (2) appellant has not shown that the debt became worthless during the year in which the deduction is claimed. Appellant, however, disputes both of respondent's findings. Assuming, without deciding, that the loans were bona fide loans, we cannot conclude that appellant has shown that the loans became worthless in the year in issue.

In order to be entitled to a deduction for a nonbusiness bad debt, appellant must demonstrate that the debt became totally worthless during the taxable year. **Whether a debt is totally worthless within a particular taxable year is a question of fact.** (Perry v. Commissioner, 22 T.C. 968 (1954); Mellen v. Commissioner, ¶ 68,094 T.C.M. (P-H) (1968).) **The burden is on appellant to prove that** the debt for which the deduction is claimed had some value at the beginning of the year in which the deduction is claimed, and that it became worthless during that year. (Cittadini v. Commissioner, 139 F.2d 29 (4th Cir. 1943); Appeal of Knollwood West Convalescent Hospitals, Inc., Cal. St. Bd. of Equal., Mar. 3, 1987, ¶ 193.) **The worthlessness must be fixed by an identifiable event or events in the period in which the deduction is claimed which furnish a reasonable basis for abandoning any hope of future recovery.** (United States v. White Dental Mfg. Co., 274 U.S. 398 [71 L.Ed. 1120] (1927); Appeal of B&C Welding, Inc., Cal. St. Bd. of Equal., Oct. 26, 193.)

Appellant has stated that in 1980 Mrs. **Bywater**, whose attitude toward repayment of the loans had been **generally positive**, changed her attitude to one of general hostility. Appellant further stated that this

Appeal of Marshall D. and Una-F. Joelson

change in attitude convinced, Mr. Stuhr, his attorney, to advise him, in a letter dated October 15, 1981, to cease collection efforts. The letter by Mr. Stuhr, however, does not support appellant's allegations that Mrs. **Bywater** had a change of attitude. **His** letter does suggest that it would be a waste of time and money to pursue collection, but he states that in October of 1980, Mrs. **Bywater** visited his office and once again reiterated their intentions to pay the amount owed. The loans were made in 1971 and 1972, and no payments on these loans were made. No legal action was ever taken by appellant to enforce collection even after **Mr. Bywater** left the country in 1976 to take a job in Africa. Given all these facts, we cannot conclude that the debt had any value at the beginning of 1980 or that there was any identifiable event that made the loans worthless in 1980. For the reasons discussed above, the action **of** respondent will be sustained.

