

CLAIM OF RIGHT
MONEY EARNED



ONE YEAR, BUT ORDERED BY
BANKRUPTCY CRT. TO PAY BACK -

BEFORE THE STATE BOARD OF EQUALIZATION

IS THIS INCOME
IN YEAR RECEIVED

OF THE STATE OF CALIFORNIA

BY ATTY.

In the Matter of the Appeal of)
)
GEORGE M. AND ELIZABETH R. CUTHBERTSON)

For Appellants: George M. Cuthbertson, in pro. per.

For Respondent: Burt D. Lack, Chief Counsel
Crawford H. Thomas, Associate
Tax 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 protests of George M. and Elizabeth R. Cuthbertson against proposed assessments of additional personal income tax in the amounts of \$148.76 and \$119.93 for the years 1959 and 1960, respectively, and, pursuant to section 19059 of the Revenue and Taxation Code, from the action of the Franchise Tax Board in denying the claims of George M. and Elizabeth R. Cuthbertson for refund of personal income tax in the amounts of \$65.41 and \$193.79 for the years 1959 and 1960, respectively.

George M. Cuthbertson (hereafter referred to as "appellant") is an attorney practicing law in this state. He uses the cash basis method of accounting. In the timely California personal income tax returns which he and his wife filed for the years in question, appellant reported net professional income in the amounts of \$8,748.88 and \$16,947.26 for 1959 and 1960, respectively. A substantial portion of that income in both years was received from a bankrupt corporation which appellant had represented.

In 1962 the trustees in bankruptcy of that corporation filed an action against appellant in which they sought to recover judgment for the major portion of the fees paid to

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him during 1959 and 1960, on the ground that those fees were excessive. On January 18, 1965, an order was entered by the referee in bankruptcy authorizing the compromise of the suit upon payment by appellant of the sum of \$13,738.82 to the trustees. Insurance carried by appellant covered one-half of this judgment and in January 1965 appellant paid the remaining half, \$6,869.41. He also paid \$630.05 to a firm of attorneys for representing him in the suit.

Respondent made certain upward adjustments in appellant's taxable income for 1959 and 1960 on grounds which are not material here, and issued notices of proposed additional assessment. Appellant does not now contest the grounds for those adjustments but argues that his reported income for 1959 and 1960 should be reduced to the extent that he eventually had to repay the fees that he received in those years.

It is well settled that if a taxpayer receives payments under a claim of right, without restriction as to their disposition, such payments are includible in income in the year of receipt, even though the taxpayer's right to retain the money may be disputed and even though in a later year he may be adjudged liable to repay all or a portion of such payments. (North American Oil Consolidated v. Burnet, 286 U.S. 417 [76 L. Ed. 1197]; Healy v. Commissioner, 345 U.S. 278 [97 L. Ed. 1007].) This rule has its basis in the annual accounting concept. (United States v. Lewis, 340 U.S. 590 [95 L. Ed. 560], reh. denied, 341 U.S. 923 [95 L. Ed. 1356].) The taxpayer who finds himself obligated to return all or a portion of such receipts in a subsequent period is entitled to a deduction in the year of repayment. (See North American Oil Consolidated v. Burnet, supra.)

In the instant case it seems clear that the legal fees received by appellant in 1959 and 1960 from the bankrupt corporation which he represented constituted income to him in those years. He makes no contention that there were any restrictions placed on his use of those funds, and it appears that at all times after receipt appellant treated the money as his own. The fact that an action was subsequently instituted against him and that he was eventually required to return a substantial portion of those fees does not alter the conclusion that at the time they were received the fees did constitute income received under a claim of right which was taxable to him upon receipt.

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It is our opinion, therefore, that respondent has properly denied appellant's right to any refund or offset for the years in question, and we must sustain respondent's affirmation of the proposed additional assessments.

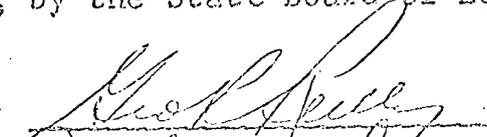
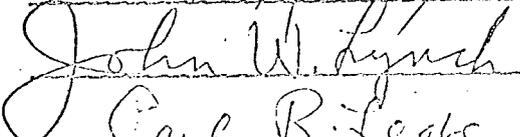
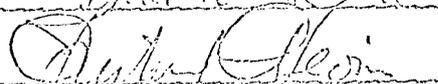
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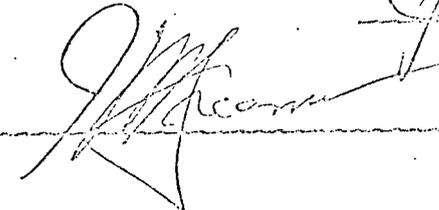
Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

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 protests of George M. and Elizabeth R. Cuthbertson against proposed assessments of additional personal income tax in the amounts of \$148.76 and \$119.93 for the years 1959 and 1960, respectively, be and the same is hereby sustained.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED, pursuant to section 19060 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the claims of George M. and Elizabeth R. Cuthbertson for refund of personal income tax in the amounts of \$65.41 and \$193.79 for the years 1959 and 1960, respectively, be and the same is hereby sustained.

Done at Sacramento, California, this 8th day of March, 1966, by the State Board of Equalization.

 , Chairman
 , Member
 , Member
 , Member
 , Member

ATTEST:  , Secretary