

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
ALBERT HAKIM) No. 85A-0074-PS

Appearances:

For Appellant: Karen L. Hawkins
Attorney at Law

For Respondent: A. Kent Summers
Counsel

O P I N I O N

This appeal is made pursuant to section 18593¹/₁ of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Albert Hakim against proposed assessments of additional personal income tax in the amounts of \$2,918.65 and \$216,648.70 for the years 1980 and 1981, respectively.

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

Appeal of Albert Hakim

The issue for determination is whether appellant is entitled to deduct stock losses that resulted from the expropriation of the assets of two foreign corporations owned by appellant.

Appellant Albert Hakim relocated from Iran to the United States in 1979, and became a permanent resident of California in the same year. In 1972 appellant formed Multicorp International (MCI), an Iranian corporation, and in 1975 established Multicorp International Services (MCIS), also an Iranian corporation. MCI and MCIS sold, installed and maintained in Iran high technology equipment (computer systems, radar devices, medical equipment, and radio receiving equipment) manufactured outside Iran, some of which was sold to the Iranian government. When appellant left Iran in 1979 he owned 50 percent of the capital stock of MCI and 100 percent of the capital stock of MCIS.

In 1979 revolutionary forces overthrew Shah Mohammed Reza Pahlevi (Shah of Iran) and a new regime came to power (revolutionary committee). Appellant states that, in 1980, he was contacted by a local revolutionary committee seeking his return to Iran to resume overseeing MCI and MCIS, and in fear of his life appellant refused to return to Iran. Appellant also states he was told by other U.S. Iranian exiles that the revolutionary committee expropriated the property of MCI and MCIS in 1981. Appellant further states that he has not and will not receive compensation for the expropriated property of MCI and MCIS, and at the time of the expropriation his investment in MCI and MCIS was no less than \$600,000 and \$2,000,000, respectively. Appellant claims that, because he was forced to abandon his books and records when he left Iran, he cannot establish the value of his investment in MCI and MCIS by direct evidence.

On August 22, 1984, a former MCIS employee (Holger Schlotmann) gave a sworn deposition in which he stated among other things that: (1) from 1977 to 1978 he was an executive with MCIS which gave him access to basic information and discussions concerning MCIS' business affairs; (2) that appellant was the major shareholder of MCI and MCIS; (3) that MCI and MCIS were affiliated corporations; (4) that appellant contributed additional capital to MCIS; (5) that appellant made direct advances to MCIS to purchase marketing equipment, spare parts, and for the training of personnel (an example was a \$100,000 expenditure for a plotting system and other tools); and (6) that MCIS owned a laboratory for the maintenance of medical and industrial electronic equipment (Mr. Schlotmann stated eight engineers worked in the laboratory, and the

Appeal of Albert Hakim

equipment was worth approximately \$150,000). Mr. Schlotmann also gave a detailed statement of some of MCIS's in-progress negotiations and completed sales transactions.^{2/}

On November 7, 1986, appellant gave another deposition which he stated supplemented his August 24, 1984, deposition (the earlier deposition was in fact dated August 31, 1984). (App. Reply Br., Ex. D.) Appellant stated in part that all of his books and records were confiscated by the revolutionary committee when the Ayatollah Khomeini took power in 1979; that appellant feared he would place his life in danger if he inquired about the confiscated assets of MCI and MCIS; that appellant cannot establish when the assets of MCI and MCIS were actually taken by the revolutionary committee, but his belief was that the confiscation occurred in 1981; that appellant would attempt to gather additional evidence regarding the year in which the assets of MCI and MCIS were confiscated; and that to date appellant has not submitted a claim for compensation with the Iranian Government.

For 1980, appellant claimed a loss carryover of \$44,728, and for 1981 claimed worthless stock losses totaling \$2,600,000 for his investments in MCI and MCIS. Respondent Franchise Tax Board disallowed the amount claimed for both years. Appellant subsequently accepted respondent's action for 1980, but protested respondent's action for 1981, which protest was denied, and this timely appeal followed.

Before proceeding with our discussion regarding the deductibility of appellant's worthless stock losses, we first address a question raised by appellant as to his burden of proof. Appellant argues that in order to establish his losses he may rely on circumstantial evidence as did the taxpayer in Popa v. Commissioner, 73 T.C. 130 (1979). We agree with the rationale of Popa that in unusual circumstances, such as this, it is not fair or reasonable to require appellant to eliminate all possible noncasualty causes of his loss. We have previously held that, due to the difficulty of proving a confiscatory loss in a foreign country, the date of such loss may be established by whatever evidence is available, including circumstantial evidence. (See Appeal of Zorik and Artimis

^{2/} Respondent concedes that appellant was the major shareholder of MCI and the sole owner of MCIS, and that the assets of each corporation were expropriated by the revolutionary regime. (Resp. Reply Br. at 1.) Thus, respondent implicitly concedes that appellant suffered some form of economic loss when the assets of MCI and MCIS were expropriated by the revolutionary regime.

Appeal of Albert Hakim

Soulkanian, 87-SBE-077, Dec. 3, 1987.) In Appeal of Zorik and Artimis Soulkanian, supra, we held that the evidence presented by the appellants, although circumstantial, was sufficient for application of the Cohan rule to approximate the amount of appellants' loss.

It is well settled that deductions are a matter of legislative grace and are allowable only where the conditions established by the legislature have been satisfied. (New Colonial Ice Co. v. Helvering, 292 U.S. 435 [78 L.Ed. 1348] (1934); Appeal of Frederick A. Sebring, Cal. St. Bd. of Equal., Dec. 9, 1980.) Respondent's determination that a deduction should be disallowed is presumed correct (Welch v. Helvering, 290 U.S. 111 [78 L.Ed. 212] (1933); Appeal of John A. and Julie M. Richardson, Cal. St. Bd. of Equal., Oct. 28, 1980), and appellant must prove his entitlement to the claimed deductions. (Appeal of Ambrose L. and Alice M. Gordos, Cal. St. Bd. of Equal., Mar. 31, 1982; Appeal of Zorik and Artimis Soulkanian, supra.)

Respondent's concession that appellant was the major owner of the stock of MCI and MCIS, and that the assets of each corporation were expropriated by the Iranian government, narrows appellant's burden of proof to: (1) The amount of appellant's stock loss resulting from the expropriation, and (2) establishment of the year in which the expropriation of the assets of MCI and MCIS occurred.

Section 17206 provides in part that:

(a) There shall be allowed as a deduction any loss sustained during the taxable year and not compensated for by insurance or otherwise.

(b) For purposes of subdivision (a), the basis for determining the amount of the deduction for any loss shall be the adjusted basis provided in section 18041 for determining the loss from the sale or other disposition of property.

* * *

(g)(1) If any security which is a capital asset becomes worthless during the taxable year, the loss resulting therefrom shall, for purposes of this part, be treated as a loss from the sale or exchange, on the last day of the taxable year, of a capital asset.

Appeal of Albert Hakim

(2) For purposes of this subdivision, the term "security" means--

(A) A share of stock in a corporation.

* * *

Section 17206 is patterned after section 165 of the Internal Revenue Code (I.R.C.).^{3/} It is well settled that when a California statute is patterned after a federal statute on the same subject, the interpretations and effect given the federal statute by the federal courts and administrative bodies are relevant in determining the proper construction of the California statute. (Andrews v. Franchise Tax Board, 275 Cal.App.2d 653 [80 Cal. Rptr. 403] (1969); Appeal of Zorik and Artimis Soukhanian, supra.)

In general, the adjusted basis for determining gain or loss from the sale or other disposition of property is cost, as provided by section 18042, and such cost is adjusted for capital expenditures as provided in section 18052.^{4/} Treasury regulation section 1.165-1(c)(1) provides in part that:

(c)(1) The amount of loss allowable as a deduction under section 165(a) shall not exceed the amount prescribed by § 1.1011-1 as the adjusted basis for determining the loss from the sale or other disposition of the property involved. . . .

^{3/} Senate Bill No. 1192 (Stats. 1981, ch. 714), operative January 1, 1982, made minor technical corrections to section 17206 which are not relevant here. Section 17206 was repealed by Assembly Bill No. 482 (Stats. 1989, ch. 362), in effect and operative September 12, 1989. IRC section 165 was made applicable in California by section 17201 (added by Assembly Bill No. 36 (Stats. 1983, ch. 488), operative for taxable years beginning on or after January 1, 1983).

^{4/} Sections 18042 and 18052 were repealed by Assembly Bill No. 36 (Stats. 1983, ch. 488), operative for taxable years beginning on or after January 1, 1983. Section 18031 was enacted to provide that gain or loss on disposition of property is determined as provided by the Internal Revenue Code, and section 18052 was reenacted as section 18036, subdivision (a) (added by Assembly Bill No. 36 (Stats. 1983, ch. 488), operative for taxable years beginning on or after January 1, 1983.)

Appeal of Albert Hakim

With respect to the amount of the stock loss, appellant argues that under the rule established in Cohan v. Commissioner, 39 F.2d 540 (2d. Cir. 1930), provided there is a reasonable basis for an estimate, a court will allow as a deduction a "reasonable approximation" of the loss, based on whatever evidence the taxpayer is able to present. The rule of Cohan, however, does not require us to allow a loss based on mere speculation, unsupported allegations or mere inference. (Appeal of George O. and Alice E. Gullickson, Cal. St. Bd. of Equal., June 29, 1982; Appeal of Costa Zmay, 87-SBE-078, Dec. 3, 1987.) In order to be entitled to the claimed deduction, appellant must prove, by circumstantial evidence or otherwise, the amount of his investment in MCI and MCIS. (See Appeal of Seymour and Arlene Grubman, Cal. St. Bd. of Equal., Aug. 20, 1986; Appeal of Estate of Amir Natan, Deceased, and Estate of Roohi Natan, Deceased, Cal. St. Bd. of Equal., Sept. 10, 1986.)

Here, appellant states that, when the property of MCI and MCIS was expropriated, his investments in MCI and MCIS amounted to \$600,000 and \$2,000,000, respectively, but does not state how he arrived at these amounts. Appellant also states that his initial investment in MCI came from the sale of stock in Telcom, Ltd., an Iranian corporation, but does not give us a single clue what price the stock was sold for. Appellant also provided a detailed listing of transactions engaged in by MCIS, which is meaningless to us for a determination of the cost or adjusted basis of appellant's investment in MCIS; the listing does support appellant's position that he was engaged in a business for profit, but this is not the issue before us.

As further support, appellant directs us to Mr. Schlotmann's deposition of August 22, 1984, in which Mr. Schlotmann, among other things, states that at various times in 1975 and 1976, appellant contributed additional funds to MCIS, invested money in MCIS to support various MCIS operations, and the laboratory owned by MCIS contained equipment worth about \$150,000. However, other than the laboratory equipment, Mr. Schlotmann does not attach an amount to any of the aforementioned transactions. We have allowed an approximation of similar type expenditures where it was readily apparent that "something was spent", and where the taxpayer's records were inadequate to the extent that it was impossible to make an accurate determination of how much was spent for deductible business purposes. (See Appeal of Zorik and Artimis Soukhanian, supra.) However, there must be some basis upon which an estimate can be made. (Polyak v. Commissioner, 94 T.C. No. 20 (Mar. 12, 1990); Vanicek v. Commissioner, 85 T.C. 731, 743 (1985).) Here, appellant has offered no evidence other than generalized statements of the expenditures.

Appeal of Albert Hakim

Consequently, there is no foundation upon which to approximate the claimed deductions. (See e.g. Appeal of William B. and Sally Spivak, Cal. St. Bd. of Equal., Feb. 26, 1969.) While we have allowed some appellants to estimate their deductions under the rule of Cohan v. Commissioner, supra, we are not convinced that the use of the rule would be justified in the instant matter. (See Appeal of Costa Zmay, supra.)

Even if we could, somehow, establish a value for appellant's investment in MCI and MCIS, we do not believe it would be of benefit to appellant, because we do not believe appellant has sufficiently established that the expropriation of MCI and MCIS's assets occurred in 1981. It has been previously held that the time for determination of the worthlessness of an asset must be fixed by some identifiable event or events in the year in which the deduction is claimed. (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, 1983.) Here, the only evidence offered by appellant, as to the year in which the expropriation of the assets occurred, is appellant's statement of such information received from other Iranian exiles in this country. However, appellant does not state how this information was obtained by these individuals or why it should be regarded as reliable.

In Appeal of Zorik and Artimis Soulkanian, supra, the appellant established the year of expropriation of his property by the Iranian Government through the production of a confiscation notice issued by the Iranian Government in March 1981. In Appeal of Estate of Amir Natan, Deceased, and Estate of Roohi Natan, Deceased, supra, we were also confronted by a confiscation of the taxpayers' property by the Iranian Government, but there we sustained the Franchise Tax Board because the taxpayer failed to produce evidence sufficient to establish ownership and value of the property in question, and proof of the year in which the property was confiscated.

We sympathize with appellant regarding his loss, but we are constrained because appellant has failed to establish the value of his investment in MCI and MCIS's stock, or to establish the year in which the assets of these corporations were expropriated. We have no idea what appellant's initial investments in MCI and MCIS were. We cannot conclude with any confidence that appellant contributed the amounts Mr. Schlotmann apparently believes were contributed. With respect to the \$150,000 of laboratory equipment, appellant has not convinced us that the equipment was not purchased with operating funds, or that the equipment had any undepreciated value in 1981. We also cannot conclude that the confiscation of the property of MCI and MCIS occurred in 1981 as claimed by

Appeal of Albert Hakim

appellant. (All things considered, it is at least as likely that the Iranian Government expropriated the assets of MCI and MCIS in 1980, the year when the government requested appellant to return to Iran, and appellant refused to do so).

Accordingly, we must sustain respondent's action in this matter.

