STATE OF ALABAMA DEPARTMENT OF REVENUE, § STATE OF ALABAMA DEPARTMENT OF REVENUE ADMINISTRATIVE LAW DIVISION

v. § DOCKET NO. INC. 86-135

BERNARD & PAULINE (Deceased) GOUSE §
2305 Manassas Drive
Birmingham, AL 35213, §

Taxpayers. §

ORDER

This case involves a preliminary assessment of income tax entered by the Department against Bernard and Pauline (Deceased) Gouse. Mr. and Mrs. Gouse are hereinafter referred to jointly as "Taxpayers", individually as "Taxpayer" and "wife", respectively. The Taxpayer has also requested a refund for the years 1978, 1979 and 1980. A hearing was conducted before the Administrative Law Division on February 3, 1987. The Hon. Christopher R. Murvin was present and represented the Taxpayers. Department assistant counsel Mark Griffin appeared on behalf of the Department. Based on the evidence submitted at said hearing, the following findings of fact and conclusions of law are hereby made and entered.

FINDINGS OF FACT

At issue in this case is whether the Taxpayer should be allowed a casualty or theft loss deduction of $107,000.00 for the year 1981. The claimed loss is based on the theft or embezzlement of the Taxpayer's money by his wife prior to her death in 1981.

The Taxpayer and his wife were married in approximately 1964. The Taxpayer operated a business in Birmingham and was responsible

for the business's financial affairs. Accordingly, to relieve the Taxpayer from further responsibilities, it was understood and agreed that the wife would handle the couple's personal finances and investments, such as bank accounts, certificates of deposit, etc. It was further agreed by the couple that the Taxpayer would not be responsible for or contribute to the support of the wife's children by a prior marriage.

In addition to the Taxpayer's salary from his business, prior to 1981 the Taxpayer also borrowed on the cash value of his life insurance policy and received approximately $75,000.00 from the sale of a former residence. Those amounts were remitted to the wife for investment and safekeeping.

The wife died in March, 1981. The evidence indicates that from 1978 until the wife's death in 1981, the wife had on various occasions and without the knowledge of the Taxpayer secreted various amounts of the Taxpayer's money for the benefit of her son by a previous marriage. It is uncertain exactly how much was secretly given by the wife to the son, but at least $107,000.00 was surreptitiously transferred, as evidenced by two promissory notes signed by the son.

The Taxpayer learned of the missing funds only after his wife's death, whereupon he filed a claim against her estate in the amount of $107,000.00. The Taxpayer also claimed a casualty loss on the couple's 1981 return, which was subsequently disallowed by

the Department and which is the basis of the subject dispute.

CONCLUSIONS OF LAW

Code of Alabama 1975, §40-18-15(6) provides in part for a deduction for losses sustained during the tax year as a result of theft. That section is modeled after the federal law on the subject, 26 U.S.C. §165, and accordingly, federal authorities interpreting the section should control. Best v. State, Department of Revenue, 417 So.2d 197; State v. Gulf Oil Corporation, 256 So.2d 172.

Two issues are raised by the instant case. The first and primary question is whether the wife's actions in secretly taking the Taxpayer's money and transferring it to her son was a "theft" so as to qualify for the deduction. The second issue is whether the loss, which occurred over the period from 1978 to 1981, can be claimed in full in 1981. That is, must a theft loss deduction be claimed in the year in which the theft actually occurred, or in the year in which the loss was discovered.

On the first question, the federal courts have defined "theft", as used in §165, to broadly include all criminal appropriations of another's property. Bagur v. C.I.R., 603 F.2d 501; Edward v. Bromberg, 232 F.2d 107. As stated in Bagur:

> The term "theft" as used in the statute is defined broadly to encompass all criminal appropriations of another's property. See Edwards v. Bromberg, 5 Cir. 1956, 232 F.2d 107, 110; Treas. Reg. §1.165-8(d). A taxpayer is not foreclosed from claiming a theft loss deduction even though he is closely related to the thief.

> Indeed, the crime of embezzlement often presupposes a special relationship of trust between the victim and the thief. Scott & LaFave, Criminal Law, 455 (1966). For example, a deduction was allowed when money was entrusted to a faithless trustee and, thereafter, appropriated by the trustee for his own use. Vincent v. Commissioner of Internal Revenue, 9 Cir. 1955, 219 F.2d 228, 231. It was allowed when a taxpayer was forced to pay a sum of money for the return of securities withdrawn by the taxpayer's son for his own use. Earle v. Commissioner of Internal Revenue, 2 Cir. 1934, 72 F.2d 366. Again, when a wife, the co-owner of a joint bank account with her husband, withdrew money from the account in circumstances constituting embezzlement, a theft loss was allowed. Saul M. Weingarten, 1962, 38 T.C. 75. To our mind, a taxpayer-wife who owns income that is appropriated by her husband-manager for his own use should be permitted to claim similar tax treatment.

The American Heritage Dictionary, (2nd College Edit.), defines "theft" as "[T]he act or an instance of stealing." "Steal" is defined as "[T]o take (the property of another) without right or permission; To move, carry or place surreptitiously." Clearly the wife's actions fit within the above definition. It would also appear that the wife's actions in surreptitiously taking the Taxpayer's money constituted an unlawful act under one or more sections of the Alabama Code, Title 13A, chapters 8 and 9, see specifically §13A-9-51, "Misapplication of Property", commonly known as embezzlement. As stated in the Weingarten case, cited in the above quote, the fact that there was no conviction or even prosecution in the case, which under the circumstances would have been impossible against the wife, should not defeat a theft loss deduction. The Taxpayer entrusted his assets to his wife with the understanding that none of the money would be used to support his

stepchildren. Yet, against the Taxpayer's expressed prohibition and without his knowledge, the wife secretly took the Taxpayer's assets for use by her son.

The second issue is whether the loss was "sustained" in 1981. The nature of embezzlement or the illegal misappropriation of funds is such that the perpetrator's actions would normally not be discovered until some years after the actual taking. In recognition of that fact, the courts have allowed a theft loss deduction due to embezzlement in the year in which the theft was discovered, especially where there is no way to determine with exactness the actual year in which the loss actually occurred. Stevenson-Chislett, Inc. v. United States, 98 F.Supp. 252; Alison v. United States, 73 S.Ct. 191, 344 U.S. 167; United States v. Kleifgen, 557 F.2d 1293. Accordingly, the Taxpayers should be allowed to claim the entire amount of the loss in the year in which the wife's unlawful actions were uncovered, 1981.

The above considered, it is hereby determined that the preliminary assessment in issue is incorrect and that said assessment should be reduced to be made final in the amount of zero. It is further recommended that the refunds for 1978, 1979 and 1980 which are based on the subject theft loss deduction should be granted.

Done this 27th day of March, 1987.

BILL THOMPSON
Chief Administrative Law Judge