



BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
HUB CITY CONSTRUCTION COMPANY)

For Appellant: C. Paul Scott, Vice President

For Respondent: Burl D. Lack, Chief Counsel;
Israel Rogers, Junior Counsel

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FRANCHISE TAX BOARD

O P I N I O N

This appeal is made pursuant to Section 26077 of the Revenue and Taxation Code from the action of the Franchise Tax Board in denying the claim of Hub City Construction Company for refund of franchise tax in the amounts of \$556.59, \$556.59 and **\$295.29** for the taxable years ended November 30, 1952, 1953 and 1954, respectively.

Appellant is a California corporation which began doing business in this State on April 1, 1952. Its principal business activity is the construction and sale of tract houses. It reports on the accrual basis except that when the construction of one of these projects begins in one income year and the sale of the houses takes place the following year, all costs relating to the project are deducted in the year of sale. However, the total amount of officers' salaries is charged to general expense and deducted in the year that the liability to pay these salaries accrues.

The total salaries paid to the two officers were \$30,000 in the year ended November 30, 1952, and \$45,000 in the year ended November **30, 1953**. Appellant's two officers devoted **seventy** five percent of their time to the business during the period under appeal. These men spent considerable time negotiating the purchase of land, planning the subdivision and securing the acceptance of the subdivision plan, selecting or drawing up the plans for the houses and obtaining financing for the development of subdivisions. In no instance did Appellant hire an architect, although a draftsman was sometimes employed. During each of the years in question, Appellant completed and sold from thirty to forty houses. The actual construction of the houses, street improvements and other work in each tract was done by a contractor employed by Appellant. Appellant also employed a construction superintendent who was directed to some extent by the officers. The sale of houses **was** accomplished through a broker, Appellant's officers controlling the advertising. The officers spent considerable time at the office located away from the tract site, and

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devoted a portion of the time spent there to the daily routine of the business.

Respondent determined that a portion of the salaries of Appellant's officers deducted as general expenses in each of the years under appeal was related to uncompleted projects and should have been capitalized and deferred to the year of sale as part of the cost of construction. Respondent concluded that the amount to be deferred was that proportion of the total salaries which other deferred costs bore to total costs.

Compensation paid individuals for services incidental to the construction or improvement of buildings is a capital expenditure which should be added to the cost of the buildings and not deducted currently. (Acer Realty Co.; 45 B.T.A. 333, aff'd 132 F. 2d 512; Algernon Blair, Inc., 29 T.C. 1205; Gibbs & Hudson, Inc., 35 B.T.A. 205.) When the officers of a corporation perform services, the cost of which would be a capital expenditure if done by a specialist hired for the particular task, the cost of these services as rendered by the officers must be capitalized. (Acer Realty Co., supra.)

Based on the facts before us, we are of the opinion that a portion of the salaries of Appellant's officers was reasonably related to the uncompleted homes and should be capitalized as part of the cost of said homes. In the absence of evidence that it is erroneous, we accept the apportionment made by the Franchise Tax Board.

O R D E R

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 26077 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the claim of Hub City Construction Company for refund of franchise tax in the amounts

