BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
GILBERT AND MERLE GARDNER)

For Appellants: Robert G. Carter,
Attorney at Law

For Respondent: Crawford H. Thomas, Chief Counsel
Peter S. Pierson, Associate Tax
Counsel

OPINION

This appeal is made pursuant to section 19059 of the Revenue and Taxation Code from the action of the Franchise Tax Board in denying the claim of Gilbert and Merle Gardner for refund of personal income taxes in the amounts of $418.03 and $257.34 for the years 1959 and 1960, respectively.

Appellants, who are husband and wife, filed joint personal income tax returns for the years in question. They paid deficiency assessments issued by respondent for the years 1959 and 1960 and filed a timely claim seeking refund of that portion of the assessments which represented adjustment of their depreciation deductions for these years. The adjustment involved depreciation deductions for property hereafter described.

On October 1, 1959, appellants purchased six acres of land located in Firebaugh, California, together with improvements consisting mainly of cabins which were rented to farm laborers. Appellants executed a noninterest bearing contract of sale which provided for payment of the price in 240 monthly installments of $1,000 each.

Based upon adjustments which are not material here, appellants computed a net cost of $233,520.10 for the property. Of this amount, $5,778.74 was allocated to land and the balance of $227,741.36 was considered the cost basis of the improvements for purposes of computing depreciation deductions.

Respondent computed a total cost basis Of $241, 619.30 for the property by adding certain additional costs to the gross contract price of $240,000.00. It allocated $78,405.46 of this cost to the land and adjusted appellants' depreciation deductions for the years 1959 and 1760 by using $163,213.84 as a basis for the improvements.

It is appellants' contention that respondent's use of $163,213.84 as a basis for the improvements deprived them of proper depreciation deductions. Respondent's additions to the total cost basis of the entire property are not contested.

Section 17208 of the Revenue and Taxation Code provides:

> (a) There shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence)--
>
> (1) Of property used in the trade or business; or
>
> (2) Of property held for the production of income.

The cost of the property is the basis upon which appellants' depreciation must be computed. (Rev. & Tax. Code, §§ 17211, 18041, 18042.) Appellants have the burden of establishing the portion of the sales price allocable to the depreciable property. (Camp Wolters Land Co., 5 T.C. 336, aff'd, 160 F.2d 84; Salinas Valley Ice Co., T. C. Memo., Dkt. Nos. 106734 and 106741, Nov. 9, 1942; Appeal of Kung Yo Co., Cal. St. Bd. of Equal., May 5, 1953.) The basis of the depreciable property is required to be determined in accordance with respondent's regulations (Cal. Admin. Code, tit. 18, reg. 17208(e)) which provide in material part as follows:

> In the case of the acquisition ... of a combination of depreciable and non-depreciable property for a lump sum, as for example, buildings and land, the basis for depreciation cannot exceed an amount which bears the same proportion to the lump sum as the value of the depreciable property at that time. (Underscoring added.)

The sole evidence submitted on behalf of appellants consists of an appraisal dated August 3, 1964, which places a market value of $24,000 on the land, exclusive of all improvements, *as of* October 1, 1959. Appellants' claim is founded on the premise that the appraisal establishes the market value and, therefore, the *cost of the* land and that the balance of the purchase price represents the cost of improvements. On this premise, the cost of the improvements would be $217,619. **30**.

The force of the appraisal as evidence of the value of the land is weakened because the appraisal was made approximately five years after the sale. A retrospective appraisal is not entitled to great weight as evidence. (Huron Building Co., 15 B.T.A. **1107**, aff'd, **53** F.2d **575**; Old Mission Portland Cement Co., 25 B.T.A. 305, aff'd, 69 F.2d 676.)

Appellants' proposed allocation of the purchase price, moreover, rests on the assumption that the stated price for the land and improvements was equal to their combined fair market value. *That* assumption is not necessarily correct.

Since the present vaiue of a. dollar payable in a future year is less than its face value, the stated price of property may be influenced by terms requiring payment over a period of years. The stated price must Se consiriere-3 in connection with t'he terns of payment. (M. Pauline Casey, 38 T.C. 357.) In Marcus Schlitt, T. C. Memo., Dkt. Nos. 12399-12402, June 9, 1948, property which sold for a stated price *of* $75,000 payable over a five-year term without interest was held to have a market value of only $60,000 three days before the sale, One reason for the court's refusal to recognize fair market value as being equal to the stated price was that no interest was charged.

In the case before us, the purchase price was influenced by terms providing for payment over a twenty-year period without interest. It is reasonable to assume, therefore, that the stated price was considerably greater than the actual value of the land and improvements. Thus, *even* if the value *of the* land was $24,000 *as* appellants contend, the value of the improvements was substantially less than the balance of the total price. In other words, the share of the total price allocable to the improvements on the basis of relative values was much less than the share which appellants propose to allocate to those improvements.

Since appellants have not established that respondent's action was erroneous, we approve respondent's allocation of the price and its adjustment of appellants' depreciation deductions for the years 1959 and 1960.

Appeal of Gilbert and Merle Gardner

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 19060 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the claim of Gilbert and Merle Gardner for refund of personal income taxes in the amounts of $418.03 and $257.34 for the years 1959 and 1960, respectively, be and the same is hereby sustained.

Done at Sacramento, California, this 15th day of December, 1966, by the State Board of Equalization.

_____, Chairman

Paul R. Leake, Member

John W. Lynch, Member

_____, Member

_____, Member

ATTEST: _____, Secretary