BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
ABELARDO H. G. AND EDITH E. COOPER)

For Appellants: John M. Fleharty
Attorney at Law

For Respondent: Crawford H. Thomas
Chief Counsel

Peter S. Pierson
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 protest of Abelardo H. G. and Edith E. Cooper against a proposed assessment of additional personal income tax in the amount of $533.69 for the year 1962.

In 1958 appellants constructed a home in Carmel Valley, California, at a cost of $76,573.87. They lived in this residence until January 31, 1961, when they vacated and moved to a newly purchased home in Fresno, California. The primary reason for this move was Mrs. Cooper's asthma condition which had been aggravated by the Carmel Valley environment.

Appellants evidently made some attempts to sell the Carmel Valley property themselves and then on May 8, 1961, they listed it with Irene I, Baldwin, a local broker, and made it available to all broker members of the Carmel Board of Realtors, Inc. The listing was for sale, or for lease if a desirable sale could not be made., In a letter addressed to appellants* attorney, Mrs. Baldwin expressed the belief.' that the listing price of $85,000 was fair. Over the next year a number of prospective buyers looked at the property and some offers, a few at the asking price, were made. However, none of these offers were acceptable because they included

either small down payments, exchanges for other property, or an undesirable buyer credit standing. Similarly, over this period no acceptable tenants could be found, usually because prospects had small children who would be likely to damage the house.

Finally in May of 1962, acceptable tenants were found who desired to rent the property for a four-month period pending completion of a home they were building in the area. A lease was executed commencing on June 1, at a monthly rent of $275, with appellants reserving the right to terminate upon sixty days* notice if a buyer were found. Appellants state that upon the commencement of this lease they believed that the property might be rented to these and subsequent tenants for a long period of time, in view of their lack of success in finding a buyer.

However, shortly thereafter, a buyer was found and on July 31, 1962 a sale was concluded for $65,000. A large down payment was given and the buyer had a sound credit standing. Appellants state that they sold at this price even though it was lower than what they thought was the value of the property because it was the first financially responsible offer they had had in one and a half years, and they needed the funds to help pay for their new home in Fresno. Also, Mrs. Cooper, who had been managing the property, was busy caring for her ill mother and therefore did not have time to travel to Carmel in order to adequately supervise the care and preservation of the premises. Evidently the tenants vacated the property on approximately July 1, 1962.

Appellants have submitted into evidence a written appraisal made by Allen B. Coutchie, M.A.I. The report is dated November 30, 1966, and concludes that the market value of the property as of July 31, 1962 was $80,000.

In their 1962 return appellants claimed a loss deduction of $13,264.68 from the above sale. Whether such a deduction is available is the primary issue of this case.

Section 17206 provides a deduction for a loss incurred in any transaction entered into for profit. Regulation 17206(i), title 18, California Administrative Code, states that a loss on the sale of property used by the taxpayer as his personal residence up to the time of the sale is not deductible. However, the regulation then states:

> If property purchased or constructed by the taxpayer for use as his personal residence is, prior to its sale, rented or otherwise appropriated to income-producing purposes and is used for such

> purposes up to the time of its sale, a loss sustained on the sale of the property shall be allowed as a deduction under Section 17206(a).

In the instant situation the property had been rented for approximately one month before a buyer was found and the tenants consequently vacated. Respondent argues that this rental was insufficient to convert the property to income-producing purposes and states that Charles A, Foehl, Mem., T.C. Mar, 31, 1961, controls. There, the subject property, located in New Jersey, was unimproved except for a swimming pool. The property was rented for two to three months in the summer of 1951, and ultimately sold in 1954. The Tax Court concluded that this rental was too trivial to show a real intention on the part of the taxpayers to convert- the property to income-producing purposes.

We think that the Tax Court's later decision in Paul H. Rechnitzer, T.C. Memo,, Mar. 22, 1967, is more in point. There, the taxpayer vacated his personal residence and then leased it for three and a half months before the lessee exercised an option and purchased the property. The court allowed the loss and stated two tests: (1) the rental transaction must be profit inspired, and (2) the rental of the property must preclude reoccupancy by the owner of the premises as a residence at will, The case of Charles A. Foehl, Jr., supra, was distinguished, the court stating that there the taxpayer had not satisfied the second test.

In the instant situation appellants executed a four-month lease at $275 per month. Appellants state that they were resigned to a long period of rentals because of their difficulty in finding a buyer. Only when a buyer was found was the lease terminated. We think that this transaction was sufficiently profit inspired,

There can be little doubt that the lease precluded appellants from reoccupying the property as ,a residence at will. The lease ran for four months and-the only provision for termination, other than the usual lease covenants, was in case of sale. Furthermore, appellants had moved to a new home in Fresno, and Mrs. Cooper's health would have deterred a return to Carmel Valley,

Respondent also contends that appellants have not adequately proved the amount of the loss, if any, which they sustained from the sale of the property. Regulation 17206(i) states that the amount used to compute the loss shall be the lower of the fair market value or the adjusted basis, at the time of conversion. Also further adjustment shall be made for the period subsequent to the conversion, as prescribed

in regulation 18031. On June 1, 1962, the date of conversion of the property, appellants' adjusted basis was $74,404.30. They have introduced as evidence a written appraisal of the property which placed its market value at $80,000 on July 31, 1962. The realtor stated that she thought $85,000 was a fair price on May 8, 1961, In the absence of any contradictory evidence we think that appellants have. adequately proved that the fair market value of their property was higher than the adjusted basis which they used to compute their loss.

We conclude that appellants should be allowed a deductible loss under section 17206 from the sale of their Carmel Valley property.

ORDER

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 protest of Abelardo H. G. and Edith E. Cooper against a proposed assessment of additional personal income tax in the amount of $533.69 for the year 1962, be and the same is hereby reversed.

Done at Sacramento, California, this 9th day of May, 1968, by the State Board of Equalization.

, Chairman

, Member

, Member

, Member

, Member

ATTEST: , Secretary