



BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
STEPHEN AND CIVIA GORDON)

For Appellants: R. Curtis Dalton
Certified Public Accountant

For Respondent: Kathleen M. Morris
Counsel

O P I N I O N .

This appeal is made pursuant to section 18593 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Stephen and Civia Gordon against a proposed assessment of additional personal income tax in the amount of \$2,909.62 for the year 1978.

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The issue for determination is whether appellants Stephen and Civia Gordon sustained a deductible casualty loss to their residence.

In 1970, appellants purchased a one-story house in El Cajon to use as their residence. The house has a foundation of reinforced concrete, and was built in 1961; a swimming pool was added in 1968. Prior to the end of 1977, appellants contacted a real estate broker to list the residence for sale, and received from the broker a preliminary market analysis valuing the home at \$165,000. The El Cajon area was drenched in January 1978 with unusually heavy rains which, appellants assert, caused extensive cracks to become prominent in the house's foundation, the patio slab, and the swimming pool area. On August 31, 1978, an unnamed local real estate office appraised the **property** and valued it at \$169,500. Appellants were unable to sell the residence at this price, however, after prospective buyers became aware of the crack damage.

On September 13, 1978, a damage report was submitted by Catlin and Company, Inc. (**Catlin**), a La Mesa firm of consulting engineers and geologists, that appellants had hired to inspect the cracks. The company reported that conversations with appellants led it to "understand that: ... b. Approximately three years ago a crack system was observed traversing the residence and pool. c. **No** further distress or advance of the crack(s) has been observed to date." Catlin found a north-south trending crack system which produced displacements of up to half an inch through the living room, around the pool and in the front walk, a 1.5-inch displacement through the patio slab, and a hairline crack through the pool bowl. Catlin discovered that originally the eastern portion of the property had naturally sloped downward, that this slope had later been filled, and that the present trend of the crack system follows the line between the fill soils and natural soils. It said the fill soils possibly had not been correctly placed and compacted so **as** to keep irrigation, rain, and runoff water from infiltrating the fill soils. Over a length of time, this seepage caused "differential settlement" of the fill and natural soils which resulted in the surface cracks at issue. The company opined that a complete repair of the property, by recompacting the soils, was probably "[e]conomically... unwarranted." It concluded, **however**, that further damage or danger would be minimal as long as appellants implemented certain "limited **repair[s]**" which included sealing

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permeable areas and repairing and altering the drainage system. By the end of the year, appellants had spent \$1,250 effecting some or all of the recommended limited repairs.

An appraiser named Kenneth C. **Copeland** inspected the property on November 30 and December 11, **1978**; he submitted his report to appellants on February 20, 1979. He estimated the residence's market value, "not considering any structural damage," at \$160,000 as of July 1, 1978. He calculated the "cost to cure" at \$1,550, comprising \$1,250 for the repairs appellants made and \$300 for **Catlin's** analysis and report. He estimated "incurable damage," in the form of buyer resistance, at \$20,000. He considered buyer resistance to be demonstrated by the facts that prospective purchasers withdrew their offers immediately after becoming aware of the differential settlement problems and that appellants finally sold their property on January 9, 1979, for much less than \$160,000. **Copeland** estimated from these circumstances that the market value as of January 1, 1979, "considering structural damage," was \$140,000, and that the total curable and incurable damage was \$21,550.

On their joint personal income tax return for 1978, appellants claimed a casualty loss deduction of \$21,450. Respondent disallowed the loss deduction, reduced their claimed deduction for payments to a Reogh retirement plan, and issued the subject assessment. In their protest and appeal, appellants have not objected to respondent's reduction of their Keogh contribution deduction. Thus, the sole issue before us is the validity of their claimed casualty loss.

Section 17206, subdivision (a), of the Revenue and Taxation Code allows a taxpayer to deduct "any loss sustained during the taxable year and not compensated for by insurance or otherwise." Subdivision (c)(3) provides that the deductible losses include "[l]osses of property not connected with a trade or business, if the losses arise from fire, storm, shipwreck, or other casualty, or from theft." This subdivision is substantially similar to, and was patterned after, section 165(c) of the Internal Revenue Code of 1954. Federal case law is therefore entitled to great weight in interpreting the California provision. (Meanley v. McColgan, 49 Cal.App.2d 203 [121 P.2d 45] (1942); Appeal of Richard and Barbara L. Knowdell, Cal. St. Bd. of Equal., May 21, 1980.)

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The burden is on the taxpayer to substantiate a claimed casualty loss deduction. The taxpayer must prove that in the year for which the deduction is claimed he or she suffered a measurable loss as a direct result of a casualty.- (David Axelrod, 56 T.C. 248 (1971); Appeal of George O. and Alice E. Gullickson, Cal. St. Bd. of Equal., June 29, 1982; Appeal of Jack Caplan, Cal. St. Bd. of Equal., June 28, 1977.) More particularly, the claimant is usually required to show that a sudden or unexpected force destroyed or damaged property. (Matheson v. Commissioner, 54 F.2d 537, 539 (2d Cir. 1931); Richard A. Hill, ¶ 78,098 P-H Memo. T.C. (1978).) In Fay v. Helvering, 120 F.2d 253 (2d Cir. 1941), the word "casualty" was defined as "an accident, a mishap, some sudden invasion by a hostile agency; it excludes the progressive deterioration of property through a steadily operating cause." (120 F.2d at 253.)

Appellants assert that the casualty which caused the crack damage to their residence was a series of heavy rainstorms in January 1978. According to the record, however, appellants told both Catlin and Copeland that the cracks first appeared in 1975. Catlin's report indicated that the fill soils, when first placed on the property's eastern slope, were not compacted sufficiently to prevent water saturation, causing the fill and natural soils to settle at different densities and levels over a period of years. In 1975 this differential settlement revealed itself in the foundation cracks at issue. Appellants told Copeland that the cracks became much more prominent after the 1978 rainstorms, yet Catlin stated in September 1978 that, since 1975, "no further distress or advance of the cracks has been observed to date." Moreover, the residence received a preliminary market analysis of \$165,000 prior to 1978 and an appraisal of \$169,500 on August 31, 1978; this does not indicate that the cracks became significantly more prominent after the storms.

From the evidence presented, it appears that the cracks were not suddenly caused by the 1978 storms. The most that may be claimed on appellants' behalf is that the storms provided additional moisture for a continuous process of soil shifting and deterioration that had been in progress for some time.

As stated, a loss due to the steady, progressive deterioration of property over time is not a deductible casualty loss. (Levy v. Commissioner, 212 F.2d 552 (5th Cir. 1954); Charlie L. Wilson, ¶ 63,188

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P-H Memo. T.C. (1963), affd., 340 F.2d 609 (5th Cir. 1965); Appeal of Lewis B. and Marian A. Reynolds, Cal. St. Bd. of Equal., Oct. 3, 1967.) This general rule includes cases where the cause of the extended deterioration is subsidence or shifting of earth (K. P. Carr, ¶ 79,400 P-H Memo. T.C. (1979), affd., 631 F.2d 730, reh. den., 633 F.2d 582 (5th Cir. 1980)) and where the cause is the normal operation of the elements upon a residence with poor drainage or faulty construction. (Portman v. United States, 683 F.2d 1280 (9th Cir. 1982); Matheson v. Commissioner, supra.) Appellants have not shown that the causes of the crack damage were the 1978 rainstorms rather than improper compacting of the fill soils and saturation of the soils over time. In this case, the development of the cracks over several years is not a "sudden event" which would entitle appellants to a casualty loss deduction. For these reasons, we will sustain respondent's determination.

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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 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of Stephen and Civia Gordon against a proposed assessment of additional personal income tax in the amount of **\$2,909.62** for the year 1978, be and the same is hereby sustained.

Done at Sacramento, California,, this 28th day of July , 1983, by the State Board of Equalization, with Board **Members** Mr. Bennett, Mr. Collis, Mr. Dronenburg, Mr. Nevins and Mr. Harvey present.

William M. Bennett , Chairman

Conway H. Collis , Member

Ernest J. Dronenburg, Jr. , Member

Richard Nevins , Member

Walter Harvey* , Member

*For Kenneth Cory, per Government Code **section 7.9**