BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
ESTATE OF HOWARD W. CHASE,)
DECEASED, AND ESTATE OF)
GLADYSC. CHASE, DECEASED)

For Appellants: H. Spencer St. Clair
Attorney at Law

For Respondent: James W. Hamilton
Acting Chief Counsel

Steven S. Bronson
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 the Estate of Howard W. Chase,

Deceased, and the Estate of Gladys C. Chase, Deceased, for refund of personal income tax and interest in the amount of $11,109.38 for the year 1969. The Estate of Gladys C. Chase, Deceased, is involved in this appeal solely because Howard W. and Gladys C. Chase filed a joint return for the year in question.

The issue presented is whether Howard W. Chase is entitled to defer recognition of a gain realized upon the involuntary conversion of certain real property.

For some time prior to the year in question, Howard W. Chase owned slightly more than five acres of unimproved real property in Playa Del Rey, California. The parties to this appeal agree that the land was held for "investment," by which they apparently mean that Mr. Chase hoped to secure a future profit from appreciation in the property's value. On July 31, 1969, Mr. Chase sold the Playa Del Rey property to the State of California under threat of condemnation, realizing a gain of $360,076.57. He deposited the proceeds of the sale in various bank accounts and, assisted by his attorney, began to search for suitable property in which to reinvest the funds. He was unable to find suitable replacement property immediately, however, in part because he became seriously ill and had to be hospitalized.

Information concerning the sale of the Playa Del Rey property was submitted with Mr. and Mrs. Chase's 1969 joint California personal income tax return. Included on the schedule of sales data was the statement "Gain is deferred pending reinvestment of all or a portion of the proceeds from the condemnation."

Mr. Chase died on July 19, 1970. A trust company and Mr. Chase's daughter, Carmen Miller, were appointed co-executors of his estate. They were also appointed co-trustees of two trusts which Mr. Chase had created in his will. Carmen Miller and the trust company thereafter continued to search for property to replace the Playa Del Rey land, and on December 17, 1970, in their capacities as co-trustees, they purchased a four-sevenths interest in a parcel

of real property in Compton, California. 1/ This parcel was improved with a 72,000 square foot industrial building. At the time of the purchase, it was leased to a corporation manufacturing automobile parts and farm equipment.

After examining the 1969 and 1970 personal income tax returns filed by or on behalf of Howard W. Chase and his wife, respondent determined that the gain realized on the sale of the Playa Del Rey land should have been recognized in 1969, the year the property was sold. It therefore issued a proposed assessment of additional tax for that year. The proposed assessment was subsequently paid, plus interest, and the claim for refund at issue here was filed. This appeal followed respondent's denial of that claim.

Appellants rely on sections 18082 and 18083 of the Revenue and Taxation Code. Section 1.8082 provides, in relevant part:

> . If property (as a result of its destruction in whole or in part, theft, seizure, or requisition or condemnation or threat or imminence thereof) is compulsorily or involuntarily converted- -
>
> * * *
>
> (c) Into money. . . the gain (if any) shall be recognized except to the extent hereinafter provided in Section 18083.

The pertinent provisions of section 18083 are:

> If the taxpayer; .. for the purpose of replacing the property so converted, purchases other property similar or related in service or use to the property so converted, ... at the election of the taxpayer the gain shall be recognized only to the extent that the

1/ The remaining three-sevenths interest was purchased by Carmen Miller, individually, and is not involved in this appeal.

> amount realized upon such conversion.. . exceeds the cost of such other property. ...

These sections are substantially identical to section 1033(a) of the Internal Revenue Code of 1954.

Respondent contends that the deferral provisions of section 18083 do not apply under the facts of this case for two reasons: First, the Playa Del Rey land and the replacement property were not "similar or related in service or use"; and second, the replacement property was not purchased by "the taxpayer. "

Respondent's first contention is based on the prior rule that unimproved real property is not "similar or related in service or use" to improved real property. (See Cal. Admin. Code, tit. 18, reg. 18082-18088(b), subd. (3)(I)(i).) With respect to certain classes of real property, however, this rule was changed in 1961 with the adoption of Revenue and Taxation Code section 18090. 2. Subdivision (a) of that section provides:

> For purposes of Sections 18082 through 18086, if real property (not including stock in trade or other property **held primarily for sale) held for** productive use in trade or business or for investment is (as a result of its seizure, requisition, or condemnation, or threat or imminence thereof) compulsorily or involuntarily converted, property of a like kind to be held either for productive use in trade or business or for investment shall be treated as property similar or related in service or use to the property so converted. (Emphasis added.)

Respondent's regulations, furthermore, explain the phrase "like kind" as follows:

> . . . the words "like kind" have reference to the nature or character of the property and not to its grade or quality. ... The fact that any real estate involved is improved or unimproved is not material,

> for that fact relates only to the grade or quality of the property and not to its kind or class. Unproductive real estate held by one other than a dealor for future use or future realization of the increment in value is held for investment and not primarily for sale. (Emphasis added.) (Cal. Admin. Code, tit. 18, reg. 18081(a), subd. (2).)

Because of the special rule for real property contained in section 1.8090. 2, we must reject respondent's first contention. There is apparently no doubt that the Playa Del Rey land and the replacement property were both held for investment and not primarily for sale within the meaning of that section, and that the, properties were of "like kind. " (See E. R. Braley, 14 B. T. A. 1153; Biscayne Trust Co., Executor, 18 B. T. A. 1015; Ramey Investment Corp., T. C. Memo., Jan. 11, *1967.*) Accordingly, the properties were "similar or related in service or use" for purposes of Revenue and Taxation Code section 18033. Our decision in the Appeal of Andrew I,. Andreoli, decided January 5, 1971, is not to the contrary, since that case dealt with a purchase of *corporate* stock not covered by section 18090.2. (See Rev. & Tax. Code, § 18090.2, subd. (b)(1).)

As its second ground for urging that section 18083 does not apply, respondent points out that the replacement property was not purchased by Mr. Chase, but by the co-trustees under his will. Respondent concedes that trustees and executors who purchase replacement property on behalf of a deceased taxpayer may qualify as "the taxpayer" for purposes of section 18083, citing In Re Goodman's Estate, **199** F. 2d **895,** and Estate of John E. Morris, 55 T. C. 636, affirmed, 454 F. 2d 208. It contends, however, that the co-trustees in this case were not acting on Mr. Chase's behalf. For the reasons expressed below, we disagree.

In Goodman's Estate, supra, the taxpayer owned an undivided interest in a building. When the building was condemned he deposited the condemnation proceeds in several bank accounts, and two days after the condemnation his attorney reinvested some of the funds. That same day the taxpayer died. The executor of his estate then

continued purchasing replacement properties, completing the rci nvestment' within sixteen months after the taxpayer's death. 'The Court of Appeals held that the executor was acting "on behalf of" the taxpayer in purchasing the replacement properties, and therefore allowed him to defer recognition of the gain realized on the condemnation. (199 F. 2d at 898.)

A similar issue was presented to the Tax Court in the Estate of John E. Morris, supra. There the taxpayer had made detailed plans for reinvesting condemnation proceeds, but died before the plans could be carried out. The co-trustees of a testamentary trust created by the taxpayer reinvested the condemnation proceeds according to the taxpayer's plans. Although the reinvestment was made by co-trustees under the will, rather than by the decedent taxpayer's co-executors, the Tax Court applied the rationale of Goodman's Estate. Since the co-trustees had merely completed the taxpayer's plan for reinvestment, the Tax Court held that they were acting "on his behalf". (55 T. C. at 642.)

Neither Goodman's Estate nor Estate of John E. Morris clearly sets forth the standards to be used in deciding if an executor or trustee is acting on the taxpayer's behalf. Respondent urges us to construe those cases as holding that a representative is acting on the taxpayer's behalf only where the taxpayer himself selects the replacement property and makes detailed arrangements for its purchase before- he dies. In Goodman's Estate, however, the first reinvestment was made by the taxpayer's attorney on the date of the taxpayer's death (199 F. 2d at 897, note 5), and there is nothing in the court's opinion to suggest that the taxpayer was personally involved in the selection of any of the replacement properties. In Estate of John E. Morris, although the replacement property had been chosen before the taxpayer died, the taxpayer had taken no action commiting himself to the replacement. (55 T. C. at 644, dissenting opinion of Kern, J.) The Tax Court pointed out in its opinion, moreover, t-hat the provisions allowing nonrecognition of gain on involuntary conversions are to be liberally construed. (55 T. C. at 642.) Therefore, while the question is not entirely free from doubt, we read the Estate of John E. Morris as holding that 'the trustee of a testamentary trust created by the taxpayer may be considered to have acted on the taxpayer's behalf, in purchasing replacement

property, if the evidence shows that the taxpayer intended to replace the condemned property and the trustee merely carried out that intent.

In this case, Mr. Chase and his attorney actively searched for property to replace the Playa Del Rey land, but their search was delayed in part because Mr. Chase had to be hospitalized. Furthermore, before he died Mr. Chase filed a statement with respondent indicating his intent to purchase replacement property. Under these circumstances we have no doubt that Mr. Chase in fact intended to reinvest the proceeds from the sale of the Playa Del Rey land, and that the co-trustees were carrying out that intent when they purchased the replacement property. Accordingly, we conclude that the co-trustees were acting on Mr. Chase's behalf and therefore qualify as "the taxpayer" for purposes of section 18083.

For the above reasons, we reverse respondent's action.

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 19060 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the claim of the Estate of Howard W. Chase,. Deceased, and the Estate of Gladys C. Chase, Deceased, for refund of personal income tax in the amount of $11,109.38 for the year 1969, be and the same is hereby reversed.

Done at Sacramento, California, this 22nd day of. June, 1976, by the State Board of Equalization.

_____, Chairman

_____, Member

_____, Member

_____, Member

_____, Member

ATTEST: _____, Executive Secretary