

Appeal of Richard M. Nederostek and
Catherine C. Carney

The issue presented for our decision is whether appellants were entitled to a claimed energy conservation tax credit for the year 1982.

In December 1982, appellants installed a new furnace in their residence in San Mateo, California. Appellants claim that they purchased the replacement furnace based on the advice of a representative from their utility company but concede that they did not receive a Residential Conservation Service (RCS) audit recommendation at that time.

In April 1983, while preparing their 1982 tax return, appellants discovered that an RCS audit was required to establish the eligibility of their replacement furnace for the energy conservation tax credit. Appellants promptly requested an RCS audit from their utility company. On April 18, 1983, an auditor inspected the furnace and made the following report: "The new furnace was replaced in December of 1982. This audit was run to show that a new furnace was cost effective to replace. [sic]" (Appeal Ltr., Feb. 7, 1984, Ex. A.) Appellants filed a joint California tax return for 1982 in which they claimed an energy conservation tax credit of \$1,115. On respondent's energy conservation credit schedule (form FTB 3514), appellants described the qualifying conservation measure as a new heating system purchased at an installation cost of \$3,370. Appellants noted a federal credit of \$233.

After reviewing appellants' return, respondent disallowed the claimed credit on the basis that appellants had not obtained an RCS audit prior to the installation of the replacement furnace. Subsequently, appellants filed a claim for refund in the amount of the disallowed credit. Respondent denied the refund claim, and this timely appeal followed.

For the year in question, section 17052.4^{2/} provided for a tax credit in an amount equal to 40 percent of the costs incurred by a taxpayer for an energy conservation measure installed on the taxpayer's premises in

^{2/} All of our references are to former section 17052.4, entitled, "Energy Conservation Tax Credit," which was renumbered section 17052.8 by Statutes 1983, chapter 323, section 83, No. 3 Deering's Advance Legislative Service, page 987.

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California. The maximum allowable credit was \$1,500 for each premise. The term "energy conservation measure" was defined as any item with a useful life of at least three years falling within a specified generic category of measures which met the minimum standards established for that category. (Rev. & Tax. Code, § 17052.4, subd. (h)(6).) For existing dwellings, certain energy conservation measures were required to have been approved and adopted as part of a Residential Conservation Plan and recommended as the result of an audit conducted under the auspices of such a plan. (Rev. & Tax. Code, § 17052.4, subd. (h)(6)(H).) The Energy Resources Conservation and Development Commission (Energy Commission) was authorized to establish the minimum standards regarding the eligibility of any item of a generic category of energy conservation measures. (Rev. & Tax. Code, § 17052.4, subd. (f).)

Regulations promulgated by the Energy Commission defined three classes of energy conservation measures which were eligible for the tax credit in 1982 when installed in existing residences.^{3/} First, certain listed conservation measures, such as ceiling insulation, weatherstripping, and water heater insulation, qualified for the tax credit without an RCS audit when installed on any premise. (Cal. Admin. Code, tit. 20, reg. 2613.) Second, after January 1, 1982, other specified measures required an RCS audit to be eligible for the credit if the taxpayer's dwelling was located in a region where operational RCS plan provided energy audits. (Cal. Admin. Code, tit. 20, reg. 2614, subd. (a).) The specified measures requiring an RCS audit recommendation included electrical or mechanical furnace ignition systems, devices modifying the openings of heating and cooling systems, storm or thermal windows and doors, ventilation cooling systems, heat absorbing or heat reflective windows or door materials, exterior shading devices, movable insulation, heat pumps, load management devices, and floor and wall insulation. (Cal. Admin. Code, tit. 20, reg. 2615; see reg. 2612 for definitions of these devices.) Conversely, these measures were exempt from the RCS audit requirement only in the event that no RCS energy audits

^{3/} Unless otherwise specified, all references to Regulations are to the California Tax Credit Regulations, California Administrative Code, title 20, chapter 2, subchapter 8, article 2, effective January 1, 1981, amendment filed Feb. 11, 1982 (Register 82, No. 7).

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were available in the region. (Cal. Admin. Code, tit. 20, reg. 2614, subd. (a).) Third, all other energy conservation measures were eligible for the credit if "approved and adopted as part of a Residential Conservation Service (RCS) plan and recommended as the result of an audit pursuant to the plan." (Cal. Admin. Code, tit. 20, reg. 2614, subd. (b).) Any eligible energy conservation measures were required to meet both the applicable definition and eligibility criteria. (Cal. Admin. Code, tit. 20, reg. 2612.)

Replacement furnaces were not included among the first category of conservation measures eligible for the tax credit without an RCS audit nor were they listed among the second category of devices that specifically required an RCS audit recommendation after January 1, 1982. Therefore, under the regulations adopted by the Energy Commission, replacement furnaces belonged to the third category of general conservation measures which, when recommended as the result of an audit pursuant to an RCS plan, qualified for the energy conservation tax credit. (See Appeal of John and Linda Coreschi, Cal. St. Bd. of Equal., Nov. 11, 1984.)

It is well settled that determinations of the Franchise Tax Board in regard to the imposition of taxes are presumptively correct, and the taxpayer has the burden of demonstrating error in those determinations. (Todd v. McColgan, 89 Cal.App.2d 509 [201 P.2d 414] (1949); Appeal of Myron E. and Alice Z. Gire, Cal. St. Bd. of Equal., Sept. 10, 1969.) In the instant appeal, the record indicates that RCS audits were available in the San Mateo region in 1982, but appellants did not obtain an RCS audit before installing their new furnace in their home. Appellants contend that their replacement furnace nevertheless qualified for the energy conservation tax credit since a post-installation audit verified that the furnace was energy efficient and cost effective. Appellants argue that the purpose of the audit requirement was to provide homeowners with information on energy-saving ideas and devices and to ensure that only approved energy conservation measures qualified for the tax credit. It is appellants' position that a post-installation audit confirming the energy savings and efficiency of their furnace fulfilled the goals of the audit requirement.

Appellants have made a concise and thoughtful argument in support of their case. Unfortunately, we have no choice but to conclude that respondent properly

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disallowed appellants' claimed energy conservation tax credit. In Appeal of John and Linda Coreschi, supra, we held that a replacement furnace qualified for the tax credit under the applicable law and regulations only if recommended by an RCS audit conducted prior to installation of the unit. (See also Appeal of Ladislov and Noeleen Snyder, Cal. St. Bd. of Equal., May 8, 1985; Appeal of Paul D. and Katherine Y. McAfee, Cal. St. Bd. of Equal., Aug. 20, 1985.) The requirement that the RCS audit take place before installation was clearly intended by the Legislature, for section 17052.4, subdivision (h)(6)(H), defined energy conservation measures for existing dwellings as those devices which were not only approved and adopted as part of an RCS plan as "residential energy conservation measures" but also recommended by an RCS audit. In other words, a device or measure for the home was not to be considered an energy conservation measure eligible for the tax credit unless it was first recommended by an RCS auditor. As the agency charged with the interpretation of the section, the Energy Commission has always subscribed to the rule that RCS audit recommendations occur before installation of the measure. (See "California Plan for the Residential Conservation Service," California Energy Commission Publication P400-81-001, January 1981; "California Conservation Tax Credit," California Energy Commission Publication P400-84-014, November 1984.)

Here, unlike the taxpayers in the aforementioned appeals, appellants recognized that their new furnace was subject to the audit requirement and requested an audit. However, appellants still failed to obtain the recommendation of an RCS auditor prior to the installation of the furnace. "The fact that an RCS auditor would have recommended the furnace does not alter the fact that the audit was not obtained prior to the installation of the furnace as required by the applicable law and regulations." (Appeal of John and Linda Coreschi, supra.)^{4/}

Based on the foregoing, we must find that appellants have not proven that respondent's determination to disallow the credit was erroneous. Accordingly, respondent's action in this matter must be sustained.

^{4/} For purposes of this appeal, we need not decide whether appellants received an actual RCS audit from their utility company since it is clear that a prior RCS audit was not performed.

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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 19060 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the claim of Richard M. Nederostek and Catherine C. Carney for refund of personal income tax in the amount of \$1,115 for the year 1982, be and the same is hereby sustained.

Done at Sacramento, California, this 9th day of October , 1985, by the State Board of Equalization, with Board Members Mr. Dronenburg, Mr. Collis, Mr. Bennett, Mr. Nevins and Mr. Harvey present.

<u>Ernest J. Dronenburg, Jr.</u>	, Chairman
<u>Conway H. Collis</u>	, Member
<u>William M. Bennett</u>	, Member
<u>Richard Nevins</u>	, Member
<u>Walter Harvey*</u>	, Member

*For Kenneth Cory, per Government Code section 7.9