

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
JOHN T. AND DIANNA SHERHICK) No. 84A-543

For Appellants: John T. Sherrick,
in pro. per.

For Respondent: Patricia I. Hart
Counsel

O P I N I O N

This appeal is made pursuant to section 18593^{1/} of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of John T. and Dianna Sherrick against a proposed assessment of additional personal income tax in the amount of \$427.95 for the year 1982.

1/ Unless otherwise specified, all section references are to sections of the Revenue and Taxation Code as in effect for the year in issue.

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The sole issue presented for our decision is whether respondent properly disallowed appellants' energy conservation tax credit claimed in 1982.

Sometime during the appeal year, appellants put in an evaporative cooler with ducts in their Ridgecrest home located in the high desert area of southern California. On their joint California tax return for 1982, appellants claimed an energy conservation tax credit for installation of the cooling system.

On November 10, 1983, respondent issued a notice of proposed assessment which informed appellants of the disallowance of the claimed credit. On December 10, 1983, appellants filed a written protest against the proposed assessment of additional tax corresponding to the amount of the disallowed credit. In a notice of action dated March 15, 1984, respondent affirmed the proposed assessment based on its determination that the duct system was not an eligible energy conservation measure and the evaporative cooler required a Residential Conservation Service (RCS) audit recommendation prior to installation to qualify for the credit. Appellants thereupon filed a timely appeal with this board.

In these proceedings, appellants first point out that the duct work was an essential part of their evaporative cooling system. Appellants then concede that they did not obtain an RCS audit prior to installing the evaporative system but explain that was because they did not know of the audit requirement at that time. Appellants nevertheless contend that the energy conservation tax credit should be allowed since a "home energy analysis" conducted by the Southern California Edison Company on December 10, 1983, indicated that the evaporative cooler was a perfect energy-saving device for their area and the best conservation measure they could have installed in their residence. Since the evaporative cooler clearly resulted in energy **savings** as measured by their use of kilowatt hours, appellants assert that they complied with the spirit of the law by having received the favorable post-installation audit report from their utility company.

In defense of its action, the Franchise Tax Board has characterized appellants' evaporative cooler and accompanying duct system as a device modifying the opening of a cooling system. Respondent argues that this type of energy-saving device required in 1982 an RCS audit recommendation prior to installation to qualify as an energy conservation measure eligible for the tax credit.'

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Even though we do not agree with respondent's categorization of appellant's device as one modifying the opening of a cooling system, we must conclude that respondent made the proper decision to disallow the claimed credit for lack of a prior RCS audit.

For 1982, 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 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).) Included within this generic category of measures was ventilation cooling which substantially reduced the energy needed for space cooling. (Rev. & Tax. Code, § 17052.4, subd. (h)(6)(H)(iii).) 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 set forth three classes of energy conservation measures eligible for the tax credit when installed in existing residences in 1982.^{3/} First, certain

^{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.

^{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 February 11, 1982 (Register 82, No. 7).

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listed conservation measures, such as a 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 complying with predetermined energy standards required an RCS audit to be eligible for the tax credit unless the taxpayer's residence was located in a region of the state **where** home energy audits were not available through an RCS program. (Cal. Admin. Code, tit. 20, reg. 2614, subd. (a).) Third, all other energy conservation measures not specifically listed in the regulations must have been recommended for installation as the result of an RCS audit to be eligible for the credit. (Cal. Admin. Code, tit. 20, reg. 2614, subd. (b).) Any energy conservation measure was required to meet both the applicable definition and eligibility criteria set forth for the device. (Cal. Admin. Code, tit. 20, reg. 2612; reg. 2614, subd. (b).) Under the applicable regulations, ventilation cooling was defined as "utilizing outdoor air to cool conditioned areas or to reduce temperatures in unconditioned spaces adjacent to living areas." (Cal. Admin. Code, tit. 20, reg. 2612, subd. (n).) Ventilation cooling devices were, in turn, specifically listed among the second category of measures that qualified for the tax credit if recommended by an RCS audit. (Cal. Admin. Code, tit. 20, reg. 2615, subd. (d).) **Evaporative coolers were eligible as a form of ventilation cooling when installed to provide space cooling which would otherwise have been provided by an existing air refrigeration system.** (Cal. Admin. Code, tit. 20, reg. 2615, subd. (d)(3).)^{4/} Thus, under both the statute and regulations, an evaporative cooler qualified for the 1982 energy conservation tax credit only when its installation was recommended by an RCS audit report.

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 2. Gire, Cal. St.

^{4/} A device modifying the opening of a cooling system, on the other hand, was defined as a device which recovers waste heat from refrigeration condensing equipment and uses the heat to supplement space or water heating. (Cal. Admin. Code, tit. 20, reg. 2612, subd. (w).)

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Bd. of Equal., Sept. 10, 1969.) In the present appeal, it appears from the record that the appellants are **correct** when they argue that the duct system was an essential component of the evaporative cooler. Similarly, we do not doubt that this evaporative cooling system was the most energy-efficient measure for appellants' desert home. However, we are compelled in this appeal to follow the letter of the law, not merely abide by its spirit, and must therefore reject appellants' argument that a post-installation audit was sufficient for the credit.

Here, the law as stated by section 17052.4 and interpreted by the regulations required that taxpayers obtain a prior RCS audit recommending installation of an evaporative cooler to receive the energy conservation tax credit for the device in 1982. In Appeal of Richard M. Nederostek and Catherine C. Carney, decided on October 9, 1985, we held that the Legislature clearly intended that the RCS audit take place before installation of the energy-saving unit. (See also Appeal of John and Linda Coreschi, Cal. St. Bd. of Equal., Nov. 14, 1984.) Our holding in that appeal was based on the language of section 17052.4, subdivision (h)(6)(H), which defined an eligible energy conservation measure as one recommended by an RCS audit, and the interpretation given the statute by the Energy Commission, which has always subscribed to the rule that the audit be conducted prior to installation of the device. Since appellants in the present matter **did** not receive an RCS audit recommendation before installing their evaporative cooler, the measure was not eligible for the tax credit in 1982.

Based on the foregoing, we must find that appellants have not established error in respondent's determination to disallow their claimed energy conservation tax credit for failure to obtain a prior **RCS** audit. Accordingly, respondent's action in this matter must be sustained.

