



BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of }
DREYFUSS DEVELOPMENT } No. 84A-402-AJ
CORPORATION }
}

Appearances:

For Appellant: , Irving Kaufman
Certified Public Accountant

For Respondent: **Jon Jensen**
Counsel

O P I N I O N

This appeal is made pursuant to section 25666^{1/} of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Dreyfuss Development Corporation against a proposed assessment of additional franchise tax in the amount of \$5,411 for the income year ended October 31, 1980.

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

Appeal of Dreyfuss Development Corporation

The issue presented is whether appellant has established that the fair market value of a note received from the sale of real estate was less than its face value.

In November 1979, appellant sold 26.5 acres of land for \$705,000, receiving \$130,000 cash and a promissory note in the amount of \$575,000. The note was payable over 5 years with interest at 9 percent and was secured by the property. In the Agreement of Sale, appellant agreed to allow the deed of trust securing the note to be subordinated to liens securing construction loans if certain conditions were met. In 1982, the buyer defaulted and the property was reconveyed to appellant. When reporting the sale on its franchise tax return for the income year ended October 31, 1980, appellant valued the note at \$518,000 rather than its face value. Respondent determined that the note's fair market value was equal to its face value and recomputed appellant's reported gain on the sale. It issued a proposed assessment which it affirmed after considering appellant's protest. This timely appeal followed.

The amount realized from a sale or other **disposition** of property is "the sum of any money received plus the fair market value of the property (other than money) received." (Rev. & Tax. Code, § 18031.) The burden of proof is upon appellant to establish that the fair market value of the note received was less than its face value. In the absence of persuasive evidence to the contrary, a **secured, interest bearing, negotiable note, made by a maker** financially able to pay, is regarded as the equivalent of cash in the amount of its face value. (Bones v. Commissioner, 4 T.C. 415 (1944); Appeal of Roe C. and Rhoda M. Hawkins, Cal. St. Bd. of Equal., Jan. 10, 1963.)

The **note appellant received was secured by the property being sold and bore** interest at the market rate. Although the buyer eventually defaulted, there is no indication that he was not financially **able to** pay at the time the note was given. For these reasons, respondent contends that the note was worth its face value. Appellant contends that it was worth less than its face value for the reasons discussed below. We find **appellant's** arguments unpersuasive and agree with respondent's position.

Appellant contends that the buyer's obligation to pay the entire amount of the **loan** was contingent upon

Appeal of Dreyfuss Development Corporation

the buyer successfully subdividing the property. Although a subdivision of the property was clearly planned, there is no evidence to support appellant's contention that payment of the note was contingent upon that. In fact, the only evidence before us directly contradicts appellant. The Sales Agreement entered into by the parties states that the sales price of the property is \$705,000 and that "[t]he price is fixed and is not dependent on the number of acres included within the property, the number of residential units that may be constructed on the property, or any other variables or factors." (Appeal **Ltr.**, Ex. A at pp. 1, 2.) On the basis of this evidence, we must conclude that the buyer was unconditionally obligated to pay the full amount of the note.

Appellant next contends that its agreement to subordinate its lien in favor of construction loans reduced the fair market value of the note. Appellant has produced no evidence establishing that the subordination agreement affected the note's fair market value. There were several conditions to appellant's subordination including that only 42 lots be subject to construction loans at any one time and that the buyer guarantee lien-free completion of all construction. Finally, and most significantly, in exchange for appellant's subordination, the buyer **agreed to** assume personal liability for the balance of the note, including interest. Without evidence to the contrary, we assume that these conditions adequately protected appellant and that its agreement to subordinate its lien **did** not affect the note's value.

Finally, appellant contends that the note was actually not adequately secured, since the property was not worth the face value of the note. Appellant sold the property for \$705,000 or approximately \$26,600 per acre. It now contends that the property was worth substantially less than the purchase price. As evidence of this, appellant submitted a letter from a real estate agent, which placed a value of \$20,000 per acre **on the** subject property. Although the agent purported to base his appraisal on sales of comparative property, we find this evidence unpersuasive because he acknowledged that the other properties sold differed from the subject property in that only the subject property had been approved for subdivision. Appellant also points out that a government agency acquired 3.5 acres of the subject land by condemnation **in** 1978 **for** a price of \$10,000 per acre. This fact does not establish the value of the remaining 26.5 acres, since there is no indication that the condemnation price took into account the increase in the property's

Appeal of Dreyfuss Development Corporation

value which accompanied approval of the subdivision plans. Nor do we know that the 3.5 acres condemned were comparable to the rest of the parcel. Finally, appellant has offered no explanation as to why the buyer would pay \$705,000 for the property if it was not worth even \$575,000. We find, therefore, that the fair market value of the property was at least equal to the face amount of the note and that the note was, therefore, adequately secured.

Since appellant has not met its burden of **prov-**ing that the fair market value of the note it received was less than the note's face amount, respondent correctly treated appellant as having received cash in the amount equal to the note's face **value.** Respondent's action, therefore, must be sustained.

Appeal of Dreyfuss Development Corporation

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 **25667** of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of Dreyfuss Development Corporation against a proposed assessment of additional franchise tax in the amount of \$5,411 for the income year **ended** October 31, 1980, be and the same is hereby sustained.

Done at Sacramento, California, this 6th day Of May , **1986**, by the State Board of Equalization, with Board **Members** Mr. Nevins, Mr. Collis, Mr. Bennett, Mr. Dronenburg and Mr. Harvey present.

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

*For Kenneth Cory, per Government Code section 7.9