Mai C. Tran
Tax Counsel
Board of Equalization, Appeals Division
450 N Street, MIC: 85
PO Box 942879
Sacramento CA 95814
Tel: (916) 324-8244
Fax: (916) 324-2618

Attorney for the Appeals Division

BOARD OF EQUALIZATION

STATE OF CALIFORNIA

In the Matter of the Appeal of:	**HEARING SUMMARY**
	PERSONAL INCOME TAX APPEAL
KENT H. BAKER[1]	Case No. 551816

Year	Proposed Assessment
2006	$2,753

Representing the Parties:

For Appellant: Poonam Dayalji, Tax Appeals Assistance Program (TAAP)[2]

For Franchise Tax Board: Joanne A. Garcia, Senior Legal Analyst

QUESTIONS: (1) Whether respondent Franchise Tax Board (FTB) properly disallowed appellant's claimed casualty and theft loss deduction; and

[1] Appellant resides in Sacramento County.

[2] Appellant submitted his own appeal letter dated October 11, 2010 and reply brief dated February 24, 2011. Brandon Tang of TAAP submitted appellant's supplemental reply brief dated April 18, 2011. Poonam Dayalji, appellant's current TAAP representative, submitted appellant's second reply brief dated August 2, 2011.

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(2) Whether appellant has shown that the FTB abused its discretion by denying appellant's request for interest abatement.[3]

HEARING SUMMARY

Background

Appellant filed a timely California income tax return for 2006. On the return, appellant reported federal adjusted gross income (AGI) of $586,075, itemized deductions of $33,018, taxable income of $555,133 and total tax of $49,499. After applying withholding of $49,053, appellant reported a balance due of $446 which he remitted with the return. (Resp. Op. Br. p. 1; Exh. A.)

Upon review, respondent adjusted appellant's itemized deductions by disallowing appellant's claimed casualty and theft loss deduction of $31,810 on appellant's Schedule CA. As such, the FTB issued a Notice of Proposed Assessment (NPA) dated July 8, 2009, that disallowed the $31,810 claimed deduction on the basis that the deduction for personal casualty or theft loss is limited to the amount in excess of 10 percent of federal AGI after excluding $100 for each loss. The NPA also explained that the FTB allowed the standard deduction because the standard deduction exceeded the allowable itemized deductions after disallowing the claimed casualty and theft loss deduction. The NPA reported a revised taxable income of $584,741 and additional tax of $2,753, plus applicable interest. In addition, the NPA suspended interest accrual for the period October 16, 2008 to July 23, 2009 (15 days after the issuance of the NPA) pursuant to R&TC section 19116. (Resp. Op. Br., pp. 1-2; App. Ltr., Attachments.)

Appellant protested the NPA by letter dated September 1, 2009, stating that his loss was due to powderpost beetle damage which is considered a natural disaster and therefore, not subject to the two percent limitation. In response, respondent issued a letter dated August 3, 2010, stating that appellant may not deduct losses caused by "termites, moths, other insects, or disease." Respondent provided appellant with a copy of the 2006 Instructions for Form 4684 which was issued by the Internal

[3] According to respondent's records, total amount of interest accrued to the November 15, 2011 hearing date is $644.84. This amount includes: $342.38 of interest accrued from April 15, 2007 to October 15, 2008; $18.29 of interest accrued from July 23, 2009 to September 4, 2009; $126.18 of interest accrued from September 4, 2009 (date of respondent's receipt of appellant's protest) to August 3, 2010 (date of respondent's response to appellant's protest); and $157.99 of interest accrued from August 3, 2010 to November 15, 2011. Interest was suspended for the period of October 15, 2008, to July 23, 2009 under R&TC section 19116.

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Revenue Service (IRS). Respondent informed appellant that its notice was correct based on the law and the information provided by appellant. By letter dated September 1, 2010, appellant maintained that he disagreed with respondent's proposed assessment. Appellant stated that respondent's response was not timely. Appellant also continued to assert that he believed that he is entitled to the casualty loss deduction because the powderpost beetle infestation was unexpected and unusual. After considering appellant's protest, on September 13, 2010, respondent issued a Notice of Action (NOA) affirming the NPA. The NOA explained that the information provided by appellant did not substantiate appellant's contention that the proposed assessment is incorrect. The NOA also explained that the deduction for personal casualty or theft losses is limited to the amount in excess of 10 percent of federal AGI after excluding $100 for each loss or $58,607.[4] (Resp. Op. Br., p. 2; App. Ltr., Attachments.)

This timely appeal then followed.

Contentions

Appellant

In his appeal letter, appellant contends that he is entitled to the deduction because the California tax form he relied on indicates that "the deduction is not subject to even a 2% limitation." Appellant also asserts that he assumed his 2006 return was filed correctly since he did not receive another notice sixty days after his protest. Appellant notes that he received a notice 364 days after he submitted his protest and contends that this notice is not valid. Appellant asserts that the notice did not address appellant's contention that he was not subject to the federal 10 percent limitation. Appellant also asserts that the FTB took a new position that the powderpost beetle damage is not a casualty loss. Appellant asserts that his tax instructions indicate otherwise. Appellant further contends the FTB did not address any of his contentions and therefore, appellant asserts his 2006 return is correct. (App. Ltr., pp. 1-2.)

In his reply brief, appellant asserts that the Schedule CA supports his position. In addition, appellant contends there is conflicting information in the IRS instructions for Form 4684 and IRS publication 547 regarding whether powderpost beetle damage is considered a casualty loss.

[4] This amount was calculated by taking appellant's federal AGI of $586,075 x 10% = $58,607. $58,607-$100 = $58,507. Respondent notes that its NOA incorrectly listed an amount of $58,607. (Resp. Op. Br., p. 3.)

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Appellant appears to contend that the information indicates a deduction for losses is permitted if there is a sudden destruction due to an unexpected or unusual infestation of beetles or other insects. Appellant asserts that the damage to his home was not expected, particularly as he inspects his home bimonthly for termites. In addition, appellant asserts that this incident was unusual because he never heard of powderpost beetles until his neighbor notified him that they had their home fumigated due to a powderpost beetle infestation. As such, appellant contends the powderpost beetle damage was both unexpected and unusual. (App. Reply Br., p. 1.)

Appellant further contends that he should be entitled to interest abatement as the FTB took 364 days to respond to his protest while appellant only had 60 days to respond. Appellant asserts that the FTB may not hold an individual to a standard that they themselves cannot meet. Appellant maintains that once the 60-day timeframe lapsed for the FTB to respond, appellant's taxes should be deemed correct as filed. (App. Reply Br., p. 2.)

Regarding respondent's specific contentions regarding where the casualty loss should have been entered on appellant's tax return, appellant contends that he did not enter the casualty loss on line 41 of his Form 540. Rather appellant states that he entered the loss on line 8 of his Schedule CA. Appellant contends the form states that the losses are not subject to the two percent limitation. Appellant questions respondent's contention that the casualty loss must exceed 10 percent of his federal AGI because the Schedule CA does not provide for a 10 percent limitation. (App. Reply Br., p. 2; Ex. A.)

With respect to the homeowner's insurance policy issue raised by the FTB, appellant states that he did not receive an insurance settlement because his policy did not cover insect damage. In support, appellant provided a copy of a portion of his homeowner insurance policy. To support his claimed casualty loss, appellant also provides a copy of the pest report and billing statements for the fumigation showing the cost of the repairs. Appellant notes that he did not include any other cost items such as living expenses in the amount of the claimed loss deduction. Appellant further notes that, as he did not claim a loss in the fair market value of his home, it is unnecessary to provide appraisals. (App. Reply Br., p. 2; Exs. E & G.)

With respect to the FTB's explanation regarding workload constraints causing the ten

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month period between receipt of appellant's protest and the FTB's response, appellant contends that the FTB should not charge interest due to its own workload constraints. Appellant further contends that the FTB failed to follow R&TC sections 21002 and 21010 of the Taxpayer's Bill of Rights Act by being untimely and not responding to his protest with clarity. (App. Reply Br., pp. 2-3.)

In appellant's supplemental reply brief, appellant specifically addresses the issue of whether damage from a powder post beetle infestation can be classified as a casualty loss under IRC section 165. Appellant maintains that the damage suffered was both sudden and unexpected. Appellant notes that he provided evidence supporting his claim of beetle damage to real property in the amount of $31,810. (App. Supp. Reply Br., p. 1.)

Citing *Rosenburg v. Commissioner* (1952 8th Cir.) 198 F.2d 46, appellant contends the casualty due to the beetle infestation qualifies for the casualty loss deduction because it occurred suddenly. Moreover, appellant contends that he has met his burden in producing evidence of his claimed loss. Appellant notes that he contracted with Millennium Termite and Pest to diagnose and fix his powderpost beetle damage and he provided the billing statements to show the costs he incurred to fix the damage. Appellant also notes that the damage was unusual and unexpected and as such, is considered a "casualty," citing *United States v. Rogers* (1941 9th Cir.) 120 F.2d 244 and *Atlantic Greyhound Corp. v. United States* (1953 Ct. Cl.) 111 F. Supp. 953. (App. Supp. Reply Br., pp. 2-3.)

In response to the contentions discussed in respondent's reply brief, appellant asserts that he should not be subject to the additional tax because it is unreasonable and unfair for the FTB to disallow appellant's deduction due to the 10 percent floor. Appellant states that he had no choice in incurring the losses due to the beetle infestation. Appellant cites *Shearer v. Anderson* (1927 2d Cir.) 16 F.2d 995 for the contention that his loss meets the very definition of a casualty loss because it was sudden, unexpected, unusual and external to the owner. Appellant argues that the requirement that the loss must be more than 10 percent of his federal AGI is unfair because those expenses were necessary and he had no choice but to fix the damage his home sustained from the beetle infestation. As such, appellant contends he should be able to deduct the loss. (App. 2nd Reply Br., p. 1.)

Respondent

Respondent notes that pursuant to Internal Revenue Code (IRC) section 165(h)(2)(A)(ii)

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and R&TC section 17201, personal casualty and theft losses are limited to the amount in excess of 10 percent of federal AGI after excluding $100 for each loss. As such, respondent contends that appellant must show he sustained a loss in excess of $58,507 to be entitled to claim a casualty loss on his 2006 return. (Resp. Op. Br., p. 3.)

Respondent further contends that appellant has not provided any documentation to verify that he is entitled to a casualty loss of any amount. Respondent notes that IRC section 165(h)(5)(E) provides that, to the extent a personal casualty loss of an individual is covered by insurance, it will be taken into account in computing the deduction only if the individual files a timely insurance claim for it. Respondent notes that Treasury Regulation sections 1.165-7(a)(2) and 1.165-8(c) states that the basis of the property must be correctly adjusted when determining the loss. Respondent explains the amount deductible as a casualty loss is the lesser of the actual value of the property just before the casualty, less its value immediately after the casualty, or the adjusted basis of the property for determining the loss on a sale. Respondent asserts appellant failed to provide any documentation to verify his entitlement to the deduction. Respondent notes that acceptable documentation would include the date of the casualty and a detailed explanation of the events relating to the casualty loss, a copy of the insurance claims filed and the amount of insurance or other compensation received, and an appraisal of the fair market value of the property immediately prior to the casualty and the fair market value of the property immediately after the casualty, based on the written opinion of a qualified independent appraiser. Citing the Board's decisions in *Appeal of Ismael R. Manriquez*, 79-SBE-077, decided on April 10, 1979 and *Appeal of Robert R. Telles*, 86-SBE-061, decided on March 4, 1986, respondent asserts appellant failed to meet his burden of proof to demonstrate his eligibility for the casualty loss deduction. (Resp. Op. Br., pp. 3-4.)

With respect to appellant's argument that the FTB's assessment should be cancelled because respondent did not respond to appellant's protest within sixty days, respondent contends there is no specific time period in which the FTB must respond to a taxpayer's protest and workload constraints must be considered in determining if the time period was unreasonable. Respondent notes that appellant timely protested its NPA on September 1, 2009. Respondent notes that it began review of appellant's protest on July 6, 2010, and asserts that this ten month period from September 1, 2009 to July 6, 2010, was entirely attributable to workload constraints. Respondent further asserts that the one month period

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from July 6, 2010 to August 3, 2010, when the FTB issued its position letter, consisted of time needed for the FTB to review appellant's protest, do research regarding casualty/theft losses, prepare the position letter, have the position letter reviewed by a supervisor and approved for mailing. The FTB asserts that the passage of time due to workload constraints and review and analysis of appellant's case is not an unreasonable delay and was entirely attributable to workload constraints. (Resp. Op. Br., p. 4.)

In its reply brief, respondent clarifies that even if respondent determines that appellant is entitled to claim a casualty loss, appellant must have sustained a casualty loss in excess of $58,507. In response to appellant's contention that his deduction is justified by the information provided in the state forms he relied on in filing his taxes, respondent notes that the form is not one of respondent's forms, but appears to be a form included in the tax program provided by the software company appellant used to electronically file his 2006 tax return. In response to appellant's contention that this form demonstrates that casualty and theft losses are not subject to a two percent limitation, respondent notes this form is used only in regards to miscellaneous itemized deductions. Respondent explains that nonbusiness casualty losses are deductible only to the extent of the amount in excess of ten percent of federal AGI after excluding $100 for each loss, as shown in the 2006 Instructions for Schedules A and B. Respondent further notes that the instructions for miscellaneous deductions explain that casualty and theft losses of property used in performing services as an employee and casualty losses of income-producing property may be claimed under miscellaneous deductions. As such, respondent contends that appellant's casualty loss is limited to the amount in excess of ten percent of federal AGI after excluding $100 for each loss because appellant's claimed casualty loss was not from property used in performing services as an employee or income-producing property. (Resp. Reply Br., 1-2; Ex. C.)

Respondent further contends that taxes are due and payable as of the original due date of the taxpayer's return. Respondent notes that the law provides for the imposition of interest if respondent assesses additional tax and that assessment becomes due and payable. Respondent notes that the Board determined respondent's imposition of interest is mandatory and respondent may not abate interest except where authorized by law. Respondent contends that appellant's position that interest should be abated because respondent did not reply to appellant's protest within 60 days is unsupported by the law, citing R&TC section 19104. (Resp. Reply Br., p. 2.)

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Respondent contends that the timing of an NPA which is issued within the statute of limitations period, does not give rise to interest abatement. Respondent notes that it timely issued the NPA on July 8, 2009, within four years after the filing date of appellant's 2006 return. Respondent also asserts there is no basis to abate interest under R&TC section 19104, subdivision (a) as the ten month period from the date of appellant's protest to the date respondent began review of appellant's case was attributable to workload constraints and there were no irregularities in the treatment of appellant's case during the protest period. Respondent further contends that its examination of appellant's tax return and the determination of appellant's state deficiencies are discretionary acts that involve the application of tax law to the circumstances of this matter, citing *Appeal of Michael and Sonia Kishner*, 99-SBE-007, decided on September 29, 1999. As such, respondent contends there was no unreasonable delay attributable to the performance of a ministerial or managerial act. In addition, respondent notes that the first written contact relating to the deficiency was the NPA dated July 8, 2009. Accordingly, respondent contends it does not have any discretion to abate interest which accrued prior to that date pursuant to R&TC section 19104. (Resp. Reply Br., pp. 4-5.)

Applicable Law

Burden of Proof

The FTB's determination of tax is presumed to be correct, and a taxpayer has the burden of proving error. (*Todd v. McColgan* (1949) 89 Cal.App.2d 509; *Appeal of Aaron and Eloise Magidow*, 82-SBE-274, Nov. 17, 1982.)[5] Deductions from gross income are a matter of legislative grace and the taxpayer has the burden of proving entitlement to the deductions claimed; unsupported assertions are not sufficient to satisfy the taxpayer's burden of proof. (*New Colonial Ice Co. v. Helvering* (1934) 292 U.S. 435; *Appeal of James C. and Monablanche A. Walshe*, 75-SBE-073, Oct. 20, 1975.) To carry that burden, appellant must point to an applicable statute and show by credible evidence that he comes within its terms. (*Appeal of Robert R. Telles*, 86-SBE-061, Mar. 4, 1986.)

Casualty and Theft Loss Deduction

IRC section 165, as incorporated by R&TC section 17201, allows a deduction for losses

[5] State Board of Equalization cases (designated "SBE") can be viewed on this Board's website (www.boe.ca.gov).

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sustained during the taxable year and not compensated for by insurance or otherwise. In the case of a taxpayer who is an individual, IRC section 165(c) permits losses to be deducted by such a taxpayer only if they are incurred in a trade or business, a transaction entered into for profit, or are caused by "fire, storm, shipwreck, other casualty, or from theft." (Int. Rev. Code, § 165(c)(1)-(3).) IRC section 165(h)(1) provides that if property not connected with a trade or business or a transaction entered into for profit is damaged or destroyed by casualty or from theft, the amount of the loss thus sustained is deductible only to the extent it exceeds $100.[6] Moreover, IRC section 165(e) provides that any loss is deductible in the year incurred, regardless of the year in which payments for repairs or replacement are made. Furthermore, for purposes of this discussion, IRC section 165(h)(2) provides that if property not connected with a trade or business or a transaction entered into for profit is damaged or destroyed by casualty, the net amount of the loss is deductible only to the extent it exceeds 10 percent of the taxpayer's federal AGI. (Int.Rev. Code, § 165(h)(2)-(3)(B).)[7]

Treasury Regulation section 1.165-7(a)(2)(i) provides that, to calculate the deductible portion of the loss, the taxpayer shall generally use a competent appraisal to determine the difference between the fair market value of the property immediately before and immediately after the casualty. Treasury Regulation section 1.165-7(a)(2)(ii) further provides that the cost of repairs to the property damaged is acceptable evidence of the loss of value if (1) the taxpayer shows that the repairs are necessary to restore the property to its condition immediately before the casualty; (2) the amount spent for such repairs is not excessive; (3) the repairs only cover the damages suffered; and (4) the value of the property after the repairs does not exceed the value of the property immediately before the casualty as a result of the repairs.

With respect to the term "or other casualty" provided in IRC section 165(c)(3), the Board has construed the term to mean an identifiable event which is sudden, unexpected or unusual and similar in nature to fire, storm, shipwreck or theft. (*Appeal of Stephen L. and Beverly J. Kostka*, 75-SBE-076,

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[6] In 2008, IRC section 165(h)(1) was amended by P.L. 110-343, section 706(c) DivC, which substituted "$500 ($100 for taxable years beginning after December 31, 2009)" for "$100," effective for tax years beginning after December 31, 2008.

[7] In 2005, IRC section 165(h)(2) only referred to "personal casualty losses" and made no reference to personal theft losses, but IRC section 165(h)(3)(B) provided, "The term 'personal casualty loss' means any loss described in subsection (c)(3)." In 2005, IRC section 165(c)(3) included both casualty and theft losses.

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Nov. 19, 1975, citing *Purdy v. Commissioner* T.C. Memo 1966-186; *Appeal of Robert W. Ritchie*, 80-SBE-093, Aug. 1, 1980.) In the *Appeal of Stephen and Civia Gordon*, 83-SBE-164, decided on July 28, 1983, the Board, citing *Fay v. Helvering* (1941 2d Cir.) 120 F.2d 253, defined the term "casualty" as "an accident, a mishap, some sudden invasion by a hostile agency; it excludes the progressive deterioration of property through a steadily operating cause."

In *Hoppe v. Commissioner* (1965 9th Cir.) 354 F.2d 988, after taxpayers had their home inspected in 1956, the taxpayers claimed that the dry rot found in 1959 in their house was the result of the unusual rains in January through April, 1958, and that the ensuing damage occurred over the following period of some 18 to 22 months is sufficiently short to qualify as a casualty. There, the Ninth Circuit court determined that there was insufficient evidence to show that the home was dry rot-free as of the 1956 inspection because the inspection report did not cover the affected areas. As such, the Ninth Circuit court upheld the underlying Tax Court decision and found that there was substantial evidence for the Tax Court's factual finding that the rains did not cause the dry rot.

In *Fay v. Helvering*, *supra*, the Court held that where the taxpayers' house was built in 1913 and the taxpayers did not discover that termites had damaged their house until 1935, the damage caused by the termites was not a casualty loss. The court noted that the insects had obviously been at work for a long time, and the loss had therefore taken place gradually although it was not discovered until the damage was complete. (*Fay v. Helvering, supra*.) Accordingly, insect damage generally does not give rise to a deductible casualty loss because it does not occur suddenly, unexpectedly, or from an unusual cause. (*United States v. Rogers* (1941 9th Cir.) 120 F.2d 244; *Dodge v. Commissioner*, T.C. Memo 1956-1022; *Callahan v. Commissioner*, T.C. Memo 1996-65.)

However, in certain situations where damages from termite infestation occurred in a relatively short period of time, ranging, for example, from 3 to 12 months, a casualty loss has been sustained. (*Rosenberg v. Commissioner, supra*, 198 F.2d at 51.) There, the taxpayers purchased a property in April 1946 and discovered a termite infestation in a small area of the property in April 1947. (*Id.* at 47.) Prior to the purchase, the taxpayers had the property inspected and were told that the construction was sound. (*Ibid.*) The Eighth Circuit court determined that the facts demonstrated that the invasion of the colony of termites and the resulting damage was both accidental and sudden. (*Id.* at 51.)

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In *Appeal of Lewis B. and Marian A. Reynolds*, 67-SBE-057, decided on October 3, 1967, the taxpayers claimed a casualty loss on their 1962 California income tax return on the basis that their sundeck suffered damage from fungus which the taxpayers asserted was caused by heavy rain storms in 1962. The sundeck was built in 1957 and there was no outward evidence of destructive wood rot in December 1961. In April 1962, appellants were notified of dry rot damage to the sundeck, which included damage not visible on the surface. The FTB disallowed the deduction on the basis that the dry rot damage did not occur with sufficient suddenness to be a deductible casualty loss. The Board sustained the FTB, noting there was no basis to conclude that the dry rot damage caused by fungus occurred with sufficient suddenness to constitute a deductible casualty loss because there was insufficient evidence that the fungus began as a result of 1962 rains.

Interest Abatement

R&TC section 19101 provides in pertinent part, if any amount of tax imposed is not paid on or before the last date prescribed for payment, interest on that amount shall be paid for the period from that last date to the date paid. Interest is not a penalty but is merely compensation for the taxpayer's use of the money. (Rev. & Tax. Code, § 19101, subd. (a); *Appeal of Amy M. Yamachi*, 77-SBE-095, June 28, 1977; *Appeal of Audrey C. Jaegle*, 76-SBE-070, June 22, 1976.) To obtain interest abatement, appellant must qualify under one of the following three statutes: R&TC sections 19104, 19112 or 21012. It appears that R&TC section 21012 is not applicable because there has been no reliance on any written advice requested of respondent. Under R&TC section 19112, interest may be waived for any period for which respondent determines that an individual or fiduciary demonstrates inability to pay that interest solely because of extreme financial hardship caused by significant disability or other catastrophic circumstance. This section does not provide any authority for the Board to review the FTB's determination whether to abate interest for extreme financial hardship. Accordingly, appellant must show he qualifies under R&TC section 19104 for interest abatement.

Under R&TC section 19104, respondent may abate all or any part of interest on a deficiency to the extent that interest is attributable in whole or in part to any unreasonable error or delay committed by respondent in the performance of a ministerial or managerial act. (Rev. & Tax. Code, § 19104, subd. (a)(1).) Furthermore, an error or delay can only be considered as a basis for abatement

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when no significant aspect of the error or delay is attributable to appellant and after respondent has contacted appellant in writing with respect to the deficiency or payment. (Rev. & Tax. Code, § 19104, subd. (b)(1).) There is no reasonable cause exception to the imposition of interest. (*Appeal of Audrey C. Jaegle, supra*.)

In the *Appeal of Michael and Sonia Kishner,* 99-SBE-007, decided on September 29, 1999, the Board adopted the language from Treasury Regulation section 301.6404-2(b)(2), defining a "ministerial act" as:

> [A] procedural or mechanical act that does not involve the exercise of judgment or discretion, and that occurs during the processing of a taxpayer's case after all prerequisites to the act, such as conferences and review by supervisors, have taken place. A decision concerning the proper application of federal tax law (or other federal or state law) is not a ministerial act.

When a California statute is substantially identical to a federal statute (such as with the interest abatement statute in this case),[8] the Board may consider federal law interpreting the federal statute as highly persuasive. (*Appeal of Michael and Sonia Kishner, supra,* (citing *Douglas v. State of California* (1942) 48 Cal.App.2d 835.)) In this regard, Treasury Regulation section 301.6404-2(b)(1) defines a "managerial act" as:

> [A]n administrative act that occurs during the processing of a taxpayer's case involving the temporary or permanent loss of records or the exercise of judgment or discretion relating to management of personnel. A decision concerning the proper application of federal tax law (or other federal or state law) is not a managerial act.

Generally, respondent's decisions relating to the organization and prioritizing of the processing of tax returns involve general administrative decisions, which do not provide a basis for interest abatement. For example:

> A taxpayer claims a loss on the taxpayer's income tax return and is notified that the IRS intends to examine the return. However, a decision is made not to commence the examination of the taxpayer's return until the processing of another return, for which the statute of limitations is about to expire, is completed. The decision on how to prioritize the processing of returns based on the expiration of the statute of limitations is a general administrative decision. Consequently, interest attributable to a delay caused by this decision cannot be abated under paragraph (a) of this section.

(Treas. Regs., § 301.6404-2(c), example 8.)

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[8] R&TC section 19104, subdivisions (a) and (b)(2)(B) are substantially identical to IRC section 6404, subsections (e) and (h).

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However, one example of a ministerial act that could provide a basis for interest abatement is the following:

> A taxpayer contacts an IRS employee and requests information with respect to the amount due to satisfy the taxpayer's income tax liability for a particular taxable year. Because the employee fails to access the most recent data, the employee gives the taxpayer an incorrect amount due. As a result, the taxpayer pays less than the amount required to satisfy the tax liability. Accessing the most recent data is a ministerial act.

(Treas. Regs., § 301.6404-2(c), example 11.) (See also, e.g., Treas. Regs., § 301.6404-2(c), examples 1 & 2.) Also, decisions regarding personnel and case assignments, in addition to the misplacing of files, can be considered managerial acts, which can also provide a basis for interest abatement. For example:

> A revenue agent is sent to a training course for an extended period of time, and the agent's supervisor decides not to reassign the agent's cases. During the training course, no work is done on the cases assigned to the agent. The decision to send the revenue agent to the training course and the decision not to reassign the agent's cases are not ministerial acts; however, both decisions are managerial acts.

(Treas. Regs., § 301.6404-2(c), example 3.) (See also, e.g., Treas. Regs., § 301.6404-2(c), examples 4, 5, 6, & 10.)

The Board's jurisdiction in an interest abatement case is limited by statute to a review of respondent's determination for an abuse of discretion. (Rev. & Tax. Code, § 19104, subd. (b)(2)(B).) To show an abuse of discretion, appellant must establish that, in refusing to abate interest, respondent exercised its discretion arbitrarily, capriciously, or without sound basis in fact or law. (*Woodral v. Commissioner* (1999) 112 T.C. 19, 23.) Interest abatement provisions are not intended to be routinely used to avoid the payment of interest, thus abatement should be ordered only "where failure to abate interest would be widely perceived as grossly unfair." (*Lee v. Commissioner* (1999) 113 T.C. 145, 149.) The mere passage of time does not establish error or delay that can be the basis of an abatement of interest. (*Id*. at p. 150.)

STAFF COMMENTS

Casualty Loss Deduction

Appellant contends that he is entitled to a casualty loss deduction of $31,810 for the fumigation and construction repair costs of a powderpost beetle infestation of his home. Appellant asserts that the infestation was sudden and unexpected. Appellant contends that he was shocked by the discovery that his home was infested with powderpost beetles as he inspects his home bi-monthly for

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termites. In support, appellant provided a copy of a supplemental pest report from Millenium Termite and Pest dated October 6, 2006, which indicates that appellant's home had "beetle and dry rot(fungus)" damage, and billing statements for fumigation and construction repair costs. (App. Reply. Br., Exh. G.)

IRC section 165(c)(3) provides that a taxpayer may claim a deductible loss for losses caused by "fire, storm, shipwreck, other casualty, or from theft." Generally, to claim a casualty loss, taxpayers must show that the event occurred with some sudden and destructive force. (*Appeal of Robert W. Ritchie, supra*.) While there appears to be no case specifically discussing powderpost beetle damage, damage from insects has generally been found to be gradual rather than sudden, and therefore, has not qualified as a casualty loss under IRC section 165(c)(3). (See *Fay v. Helvering, supra*; *United States v. Rogers, supra.)* However, if the evidence shows that damage due to termite or other insect infestation occurred over period of time from 3 to 12 months, it may qualify as a casualty loss under IRC section 165(c)(3). (*Rosenberg v. Commissioner, supra,* 198 F.2d at 51.)

Based on the evidence provided by appellant, it does not appear to Appeals Division staff that there is enough information to determine the length of time over which the powderpost beetle damage occurred. Appellant should be prepared to discuss the nature of his claimed loss, when he first purchased the home, and when he first discovered the powderpost beetle damage. In addition, appellant stated that he had bimonthly termite inspections. (App. Reply Br., p. 1.) Appellant should be prepared to provide evidence of these inspections and to discuss the nature and extent of these bimonthly inspections and whether these inspections included the areas affected by the powderpost beetle infestation. In addition, it appears to Appeals Division staff that the October 6, 2006 inspection report also indicated there was damage due to "dry rot/fungus." Appellant should be prepared to clarify whether this damage is related to the powderpost beetle infestation.

If the Board determines that the claimed powderpost beetle damage qualifies as a casualty loss, then the Board must determine whether appellant has satisfied the limitation in IRC section 165(h), which provides that appellant may take a casualty loss deduction to the extent that the amount of the loss arising from each casualty exceeds $100 and to the extent that remaining amount exceeds 10 percent of the individual's AGI. In view of those express limitations, appellant should be prepared to provide authority supporting his contention that the Board should grant appellant's appeal on

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the basis that the 10 percent AGI floor is unfair and unreasonable.

Interest Abatement

The parties should be prepared at the hearing to address whether there was an unreasonable error or delay in a ministerial or managerial act performed by one of respondent's employees during the handling of appellant's protest. Respondent should be prepared to explain its general protest procedures during the period at issue and compare them to respondent's actions related to appellant's protest. Specifically, respondent should be prepared to discuss its typical timeframe for processing a protest and responding to a taxpayer about the protest. In addition, respondent should discuss whether there were any extraordinary circumstances involved in this protest.

Appellant should be prepared to discuss how respondent, in failing to abate interest, exercised its discretion arbitrarily, capriciously, or without sound basis in fact or law. Appellant should also be prepared to explain whether the "failure to abate interest would be widely perceived as grossly unfair." (*Lee v. Commissioner*, *supra*.)

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