GARRETT N. & CAMILLE M. HATCHER § STATE OF ALABAMA
12323 Marguerite Drive DEPARTMENT OF REVENUE
Coden, AL 36523, § ADMINISTRATIVE LAW DIVISION

Taxpayers, § DOCKET NO. INC. 00-417

v. §

STATE OF ALABAMA §
DEPARTMENT OF REVENUE.

FINAL ORDER

The Revenue Department assessed 1996 and 1997 income tax against Garrett N. and Camille M. Hatcher ("Taxpayers"). The Taxpayers appealed to the Administrative Law Division pursuant to Code of Ala. 1975, §40-2A-7(b)(5)a. A hearing was conducted on November 14, 2000. CPA Byron Sherman represented the Taxpayers. Assistant Counsel David Avery represented the Department.

The issue in this case is whether the Department correctly computed the Taxpayers' 1996 and 1997 casualty losses based on the best information available.

The Taxpayers purchased a house and property on the Fowl River in Mobile County, Alabama in 1995 for $150,000. The property and house were flooded in 1996.

The Taxpayers claimed a casualty loss on the house pursuant to Code of Ala. 1975, §40-18-15(a)(6). They computed the loss to be the $85,000 they spent repairing the house after the flood, less the $23,000 they received in insurance proceeds, for a net loss of $62,000.

The Department recomputed the allowable loss on the house by first determining what part of the original $150,000 purchase price related to the house. Using an appraisal provided by the Taxpayers, the Department examiner determined that the Taxpayers' basis in the house was $63,000. The examiner then increased the basis by $40,000, which is what the Taxpayers claim they spent remodeling the house before the flood. The examiner determined that the fair market value of the house after the flood was $71,781.87, for a net loss of $31,218.13 ($103,000 - $71,781.87). Insurance reimbursement of $24,475.01 was then deducted to arrive at an allowable loss of $6,743.12. The Department made other changes to the 1996 casualty loss that are not disputed by the Taxpayers.

Alabama's casualty loss provision is modeled after the federal casualty loss provision, 26 U.S.C. §165. Under the federal statute, a casualty loss is measured by the difference between the fair market value of the property immediately preceding the casualty, and the fair market value of the property immediately after the casualty. IRC Reg. §1.165-7.

The Taxpayers argue that in computing the loss on the house, the fair market value before the casualty should include the value of the land. I disagree.

The fair market value on the Taxpayers' home before the 1996 flood was its allocated cost basis of $63,000, plus the $40,000 the Taxpayers claim they spent remodeling the house before the flood.[1] The fair market value of the house after the flood was approximately $72,000. Thus, the difference in the fair

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[1]The Department generously allowed the $40,000 increase in basis even though the Taxpayers failed to provide evidence that they had spent that amount remodeling the house.

market value of the house before and after the flood was approximately $31,000, as computed by the Department.

The Taxpayers could have claimed a casualty loss on any damage to the property. However, there is no evidence that the property was damaged. Allowing the Taxpayers to include the value of the property in the fair market value of the house before the casualty would in effect allow a deduction for the value of the property, even though it was not damaged. That cannot be allowed.

The Taxpayers' house flooded again in 1997. The Taxpayers claimed a casualty loss on their 1997 Alabama return. The loss related to both the house and the furniture in the house. The Department reviewed the return, disallowed the loss on the house, and reduced the loss on the furniture. The Taxpayers dispute only the adjustment for the furniture.

The Taxpayers computed their basis in the furniture to be $225,000. They received $100,000 in insurance proceeds, which reduced their claimed loss to $125,000.

The Department determined that the Taxpayers' basis in the furniture was $127,515.92 based on information received from the Taxpayers' insurance company. The Department thus reduced the loss on the furniture to $27,515.92 ($127,515.92 - $100,000 insurance reimbursement).

The Taxpayers argue that in computing the value of the furniture, their insurance company failed to consider what they spent repairing the furniture after the 1996 flood. The Taxpayers' CPA offered several examples at the November 14 hearing. Unfortunately, the Taxpayers failed to present any evidence, other than the CPA's unsupported testimony, as to what they spent repairing the furniture after the 1996 flood. The burden was on the Taxpayers to verify the amount of the claimed deduction. *McDonald v. CIR*, 114 F.3d 1194

(1997). They failed to do so. Consequently, the Department's adjustments must be affirmed.

The final assessments are affirmed. Judgment is entered against the Taxpayers for 1996 tax and interest of $2,933.31, and 1997 tax and interest of $2,129.97. Additional interest is also due from the date of entry of the final assessments, June 21, 2000.

This Final Order may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, §40-2A-9(g).

Entered January 4, 2001.