76-SBE-059

BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
J. ARTHUR WIDMER)

Appearances:

For Appellant: Sam Cianciola
Tax Accountant

For Respondent: David M. Hinman
Counsel

OPINION

This appeal is made pursuant to section 18594 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protests of J. Arthur Widmer against proposed assessments of additional personal income tax in the amounts of $2,475.42 and $669.87 for the years 1970 and 1971, respectively.

The issue is whether losses on the sales of certain securities were capital losses or ordinary losses.

Appellant- J. Arthur Widmer holds a full-time, salaried position as a photo engineer. He also operates a small photographic business, invests in real estate, and participates in some limited partnerships. In addition, appellant trades extensively in stocks, bonds, mutual funds and options. Appellant is not licensed as a broker or dealer, and he sells these securities solely on his own account through a local brokerage house.

Appellant suffered net losses from sales of securities during 1970 and 197 1. He deducted those losses in full on his state and federal personal income tax returns for those years. Respondent determined that the securities sold by appellant were capital assets, and that the losses were therefore capital losses deductible in the appeal years only to the extent of the gains plus $1,000. It adjusted appellant's returns accordingly and issued the proposed assessments in question.

Revenue and Taxation Code section 18161 defines the term "capital asset" as "property held by the taxpayer, " subject to various exceptions. The exception involved in this appeal is contained in subdivision (a) of that section, which excludes "property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business" from the definition of "capital asset. " Appellant argues that this exception applies here because his dealings in securities were so extensive as to constitute a trade or business. Respondent assumes, arguendo, that appellant may have been in a trade or business, but contends that he did not hold securities primarily for sale "to customers" in the ordinary course of that business. For the reasons expressed below, we agree with respondent.

In order to determine whether securities are held primarily for sale "to customers," the courts have developed a distinction between "dealers" and "traders. " The distinction wag explained as follows by the Tax Court in George R. Kemon, 16 T. C. 1026:

> Those who sell "to customers" are comparable to a merchant in that they purchase their stock in trade, in this case securities, with the expectation

> of reselling at a profit', not because of a rise in value during the interval of time between purchase and resale, but merely because they have or hope to find a market of buyers who will purchase from them at a price in excess of their cost. This excess or mark-up represents remuneration for their labors as a middle man bringing together buyer and seller, and performing the usual services of retailer or wholesaler of goods. (Citations.) Such sellers are known as "dealers. "
>
> Contrasted to "dealers" are those sellers of securities who perform no such merchandising functions and whose status as to the source of supply is not significantly different from that of those to whom they sell. That is, the securities are as easily accessible to one as the other and the seller performs no services that need be compensated for by a mark-up of the price of the securities he sells. The sellers depend upon such circumstances as a rise in value or an advantageous purchase to enable them to sell at a price in excess of cost. Such sellers are known as "traders. " (16 T. C. at 1032- 1033.)

In this case; appellant clearly was not a "dealer" in securities. He sold securities solely through a broker for his own account. Although his portfolio may have been extensive 'and his sales numerous, he was merely engaged in stock market speculation and at best can be classed as a "trader. " Consequently, he did not hold securities primarily for sale "to customers. " (George R. Kemon, supra; Frank B. Polachek, 22 T. C. 858; Harry M. Adnee, 41 T.C. 40.) We therefore sustain respondent's action.

ORDER

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

Appeal of J. Arthur Widmer

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protests of J. Arthur Widmer against proposed assessments of additional personal income tax in the amounts of $2,475.42 and $669.87 for the years 1970 and 1971, respectively, be and the same is hereby sustained.

Done at Sacramento, California, this 4th day of May, 1976, by the State Board of Equalization.

_____, Chairman

_____, Member

_____, Member

_____, Member

_____, Member

ATTEST: _____, Executive Secretary