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7 **BOARD OF EQUALIZATION**  
8 **STATE OF CALIFORNIA**

9  
10 In the Matter of the Appeal of: ) **HEARING SUMMARY<sup>1</sup>**  
11 ) **PERSONAL INCOME TAX APPEAL**  
12 **ZONGRONG LIU AND YING MA** ) Case No. 796330

|  | <u>Years</u> | <u>Proposed Assessments</u> |
|--|--------------|-----------------------------|
|  | 2008         | \$4,303                     |
|  | 2009         | \$6,297                     |
|  | 2010         | \$4,406                     |

17 Representing the Parties:

18 For Appellants: Tax Appeal Assistance Program<sup>2</sup>  
19 For Franchise Tax Board: Brian C. Miller, Tax Counsel III

21 **QUESTIONS:** (1) Whether appellants qualified as traders in securities, as defined in Internal  
22 Revenue Code (IRC) section 475, for the years at issue.  
23 (2) Whether, if appellants were traders in securities for the years at issue, they made  
24 a valid mark-to-market election for the years at issue.

26 <sup>1</sup> This matter was originally scheduled for oral hearing at the Board’s October 27, 2015 Sacramento meeting, but was  
27 postponed at appellants’ request to allow them additional time to prepare for the hearing. This matter was then rescheduled  
for hearing at the Board’s January 26-28, 2016 Sacramento meeting.

28 <sup>2</sup> Appellants’ representation subsequent to the filing of their opening brief was provided by the Tax Appeals Assistance  
Program (TAAP), including a reply brief filed by Laura Hawkins and a supplemental brief filed by Yasmeen Quraishi.

1 HEARING SUMMARY

2 Background

3 Appellants filed timely California resident income tax returns for the years at issue.  
4 (Resp. Op. Br., exhibit A.) On their 2008 return, appellants reported state wages of \$114,212, but a  
5 federal adjusted gross income of negative \$131,441 after adjustments including claimed business losses  
6 of \$243,426 on their federal schedule C for the business or profession of “Securities Exchangee.” (*Id.* at  
7 exhibit A, pp. 1, 7, & 9.) Appellants reported no tax liability and received a refund of \$4,596 in income  
8 tax withheld, and claimed a net operating loss (NOL) carryover of \$129,214. (*Id.* at exhibit A, pp. 2 &  
9 6.)

10 On their 2009 return, appellants reported state wages of \$124,235, and a federal adjusted  
11 gross income of negative \$19,598 after adjustments including claimed business losses of \$15,239 on  
12 their federal schedule C for the business of “Securities Exchangee.” (Resp. Op. Br., exhibit A, pp. 13,  
13 22, & 24.) Appellants reported no tax liability and received a refund of \$4,832 in income tax withheld.  
14 Appellants reported using a NOL carryforward of \$105,342, and reported a NOL carryover of the  
15 remaining \$23,872 from 2008. (*Id.* at exhibit A, pp. 15 & 21.) On their 2010 return, appellants  
16 reported state wages of \$143,677, and a federal adjusted gross income of \$92,479 after adjustments  
17 including claimed business losses of \$23,012 on their federal schedule C for the business of “Securities  
18 Exchangee.” (*Id.* at exhibit A, pp. 31, 41, & 44.) Appellants reported a tax liability of \$3,607,  
19 payments of \$8,491 in the form of withholdings, and received a refund of \$4,884. Appellants also  
20 reported using the remaining \$23,872 of NOL carryforward from 2008. (*Id.* at exhibit A, pp. 31, 32, &  
21 40.)

22 Respondent examined appellants’ 2008, 2009, and 2010 state income tax returns. In  
23 response to a request for clarification from respondent as to why appellants were claiming losses for  
24 each year as Schedule C business losses rather than Schedule D capital losses, appellants provided  
25 information regarding their trading activities and asserted that they were active business securities  
26 traders. (Resp. Op. Br., exhibit B.) Respondent reviewed copies of appellants’ brokerage and trading  
27 account information provided for the years at issue and verified the amounts of gains and losses that  
28 were reported on the Schedule C’s. (*Id.* at p. 2.) Appellants also provided a declaration signed in April

1 of 2009, and filed with their 2008 tax return, in which they assert their intent to apply the mark-to-  
2 market accounting method to their securities transactions under IRC section 475, with a proposed  
3 effective year of 2008. (*Id.* at exhibit C.) Appellants later stated in a letter to respondent that they  
4 decided to take the mark-to-market election in 2008 after suffering trading losses in the first quarter of  
5 2008, and that their accountant advised them that they could make the election for the 2008 tax year  
6 with the filing of their 2008 return. (*Id.* at exhibit D.)

7 Respondent provides charts of appellants' trading activities produced by its auditor based  
8 on information provided by appellants. The charts report that the number of trades performed by  
9 appellants during the years at issue was 904 trades over 167 trading days for 2008, 883 trades over 172  
10 days for 2009, and 185 trades over 40 days for 2010 (only 1 trade after May of 2010). (Resp. Op. Br.,  
11 pp. 4-5.) Appellants provide substantially similar numbers on appeal when asserting that they made  
12 1,074 trades in 2008, 816 trades in 2009, and 164 trades in 2010.<sup>3</sup> (App. Op. Br., p. 4.) Appellants  
13 assert that appellant-husband spent an average of 7 hours per day trading during 2008 and 2009 and  
14 6 hours per day in 2010, and also worked full-time at a technology firm in a position unrelated to  
15 securities trading during all three years. Appellants contend that appellant-wife spent on average  
16 3.5 hours trading each day during 2008 and 2009 and 2.5 hours per day in 2010.<sup>4</sup> Appellants did not  
17 provide trading logs or any other recordkeeping documentation. (*Id.* at p. 4; Resp. Op. Br., exhibit B, p.  
18 2.)

19 Respondent's auditor determined that appellants did not make a valid mark-to-market  
20 election and, even if they had made a valid election, their activities did not classify them as securities  
21 traders who would qualify to apply for the mark-to-market election. (Resp. Op. Br., p. 6.) The  
22 auditor's determination resulted in the reclassification of the losses for each tax year as being capital  
23 losses to be reported on Schedule D rather than business losses to be reported on Schedule C, and  
24 ///

25 \_\_\_\_\_  
26 <sup>3</sup> The difference between respondent's calculated amount of total trades over all three years (i.e., 1,972) and appellants'  
27 asserted amount of total trades (i.e., 2,054) is 82 trades over the three years, which is a difference of approximately 4 percent.

28 <sup>4</sup> Appellants provided copies of books and journals that they state they studied to learn about investments, and indicated at  
protest that the average hours spent each day trading also involved "research and education." (Resp. Op. Br., exhibit G, p. 2.)

1 thereby limited the application of the losses to \$3,000 for each tax year.<sup>5</sup> These adjustments resulted in  
2 the denial of the claimed NOL carryforwards and instead the remaining losses were treated as capital  
3 loss carryovers, and the auditor's report listed a capital loss carryover amount of \$275,539<sup>6</sup> available  
4 for tax years after 2010.<sup>7</sup> (*Id.* at exhibit H.) The auditor recalculated appellants' taxable income based  
5 on the adjustments and, because capital losses cannot be used to offset wage income, the adjustments  
6 resulted in tax liabilities for all three years at issue. On July 19, 2012, respondent issued Notices of  
7 Proposed Assessment for each year, and then, on January 7, 2014, affirmed those notices with Notices  
8 of Action after considering appellants' protests. (*Id.* at exhibits G & I.) This timely appeal followed.

### 9 Contentions

#### 10 Appellants' Contentions

11 Appellants contend that taxpayers are eligible to elect the mark-to-market accounting  
12 method under IRC section 475 if they are engaged in business as securities traders, even though they  
13 may not be securities dealers. Appellants assert that any gain or loss recognized under the mark-to-  
14 market election is treated as an ordinary income or loss. (Int.Rev. Code, § 475(d)(3)(A)(i).) Appellants  
15 agree that the failure to make a proper election results in the losses being treated as capital losses, which  
16 are only deductible up to the amount of capital gains plus \$3,000. (Int.Rev. Code, §§ 165(a), (c), (f) &  
17 1211(b)(1).) Appellants contend that the proper taxation of gains and losses from securities activity  
18 depends on whether the taxpayers are dealers, traders, or investors, and assert that appellants were  
19 traders engaged in the business of trading in securities based on all of the facts and circumstances.  
20 (App. Reply Br., pp. 1-2; *Estate of Yaeger v. Commissioner* (2d Cir. 1989) 889 F.2d 29 (*Yaeger*); *King*  
21 *v. Commissioner* (1987) 89 T.C. 445, 458-459 (*King*).)

22  
23 <sup>5</sup> As explained in the applicable law section below, taxpayers can deduct capital losses up to the amount of capital gains, plus  
24 \$3,000. Since appellants had no reported capital gains for the years at issue, they are only able to claim \$3,000 of capital  
25 losses as deductions for each year at issue. The remaining unclaimed capital losses can be used in subsequent years.

26 <sup>6</sup> Pursuant to the auditor's report, appellants' capital loss carryover, totaling \$275,539, was generated as follows:  
27 (1) \$243,745 of excess capital losses in 2008; (2) \$12,410 of excess capital losses in 2009; and (3) \$19,384 of excess capital  
28 losses in 2010. (Resp. Op. Br., exhibit H.)

<sup>7</sup> If respondent's proposed assessments are sustained on appeal, respondent should be prepared to explain to appellants the  
steps they should take to properly report and utilize their capital loss carryover to future years (i.e., 2011 and beyond),  
including the standard statute of limitations for filing amended returns.

1 Appellants contend that the question of whether a person is engaged in a trade or  
2 business is a factual question, and that the case law offers examples but provides little general  
3 guidance. (App. Reply Br., p. 2; *Commissioner v. Groetzinger* (1987) 480 U.S. 23, 27 (*Groetzinger*);  
4 *Levin v. U.S.* (Ct. Cl. 1979) 597 F.2d 760, 762 (*Levin*)). Appellants provide the factors for determining  
5 whether taxpayers managing their own investments are in the trade or business as securities traders as  
6 being: (1) the taxpayers' intent; (2) the nature of the income to be derived from the activity; and (3) the  
7 frequency, extent, and regularity of the taxpayers' securities transactions. (*Moller v. U.S.* (Fed. Cir.  
8 1983) 721 F.2d 810 (*Moller*)). Appellants assert that their trading activity was substantial for 2008 and  
9 2009, that their intent was to "catch the swings of the daily market movements," and that their primary  
10 purpose for trading was to produce income. (App. Reply Br., pp. 2-3.)

11 Appellants contend that the holding period of their securities as well as the frequency  
12 and dollar amounts of the trades in the year show that they were in the trade or business as securities  
13 traders. Appellants assert that almost all of their daily trades in 2008 and 2009 were short-term  
14 holdings, with a majority of stocks held for 1 to 7 days, and only a few held for more than 31 days.  
15 Appellants contend that they were clearly trying to profit from short-term swings in the stock market  
16 during these two years. (App. Reply Br., p. 3 & exhibits A & B.) Appellants assert that their trading  
17 activity in 2008 and 2009 was substantial and the amount of money involved was large, asserting 1,074  
18 trades with sales totaling \$1,203,364 in 2008 and 816 trades with sales totaling \$1,130,797 in 2009.  
19 (*Id.* at pp. 3-4.) Appellants allege that their trading activity was not uniformly distributed in every day  
20 or month because they would use all of their trading funds to purchase stocks and then could not buy  
21 new stocks until the previous stocks were sold. (App. Op. Br., p. 1.)

22 Appellants recite the law as stating that mark-to-market elections must indicate the first  
23 taxable year for which the election is effective, provide the trade or business for which the election is  
24 made, and must be filed no later than the due date of the federal income tax return for the taxable year  
25 immediately preceding the election year and attached to that federal return. (App. Reply Br., p. 4;  
26 *Lehrer v. Commissioner* (2005) 90 T.C.M. (CCH) 20 (*Lehrer*)). Appellants contend that they should be  
27 allowed relief from the filing deadline requirement because they acted reasonably. Appellants contend  
28 that their experience and the complexity of the return should be considered when determining this issue.

1 (App. Reply Br., p. 4; App. Supp. Br., p. 1.) Appellants assert that they exercised due diligence but  
2 failed to make the election timely because they were unaware of the necessity for the election. (App.  
3 Reply Br., p. 4.)

#### 4 Respondent's Contentions

5 Respondent cites to *King* in stating that an individual who purchases and sells securities  
6 is a dealer, a trader, or an investor. Respondent contends that traders are usually individuals who are  
7 engaged in market transactions almost daily for a substantial and continuous period often exceeding  
8 one calendar year, and whose securities activity constituted their sole or primary income-producing  
9 activity. (See, e.g., *Levin, supra*, 597 F.2d 760; cf. *Paoli v. Commissioner* (1991) 62 T.C.M. (CCH)  
10 275.) Respondent provides Internal Revenue Service (IRS) Publication 550 and points to page  
11 72 where the IRS states that taxpayers attempting to take advantage of the mark-to-market election  
12 must perform substantial transactions in securities with continuity and regularity with the purpose of  
13 seeking profits from daily market movements in the prices of securities. (Resp. Op. Br., p. 9 & exhibit  
14 E.) Respondent contends that appellants' "investment activity" was not their primary income-  
15 producing activity, but was instead an activity taken up by appellant-husband based on concerns over  
16 employment security at his full-time job. Respondent states that appellant-husband was studying and  
17 trading only when he was not working at his job with the technology company, and asserts that  
18 appellant-husband's full-time job with the technology company was appellants' primary income-  
19 producing activity. (Resp. Op. Br., p. 9.)

20 Respondent asserts that a review of appellants' investment activity does not show that  
21 appellants engaged in market transactions almost daily to catch market swings and profit on a  
22 short-term basis. Respondent contends that, conversely, the record shows sporadic bursts of trading  
23 activity, followed by months of relatively little activity, and the activity was therefore not performed  
24 with continuity and regularity. Respondent reports that 69 percent of the trades in 2008 were  
25 performed during four months, and minimal activity was conducted in the four months of March  
26 through June. Similarly, 64 percent of the market activity in 2009 was conducted in four months, and  
27 54 percent of the activity in 2010 was conducted in just the month of January with only one trade being  
28 conducted in the second half of the year. Appellant stated that the low activity in some months is

1 attributable to traveling abroad to tend to family matters at the end of 2008 and at the beginning of  
2 2009, but this does not explain other months with very low activity (e.g., June and July of 2009 and  
3 March through June of 2008). Respondent asserts that appellants' trading activities were infrequent,  
4 irregular, and sporadic during the years at issue. Respondent contends that appellants were investors  
5 who held securities for a period of time, rather than traders seeking to profit from daily market  
6 movements. (Resp. Op. Br. pp. 9-10.)

7           Respondent states that an election under IRC section 475(f) must be made no later than  
8 the due date of the original federal income tax return for the preceding tax year. (Treas. Reg. § 1.475,  
9 subs. (f)-1; Rev. Proc. 99-17, § 5.) Respondent asserts that a failed attempt to make an election for one  
10 year cannot be considered a valid election for a later year. (*Knish v. Commissioner* (2009) 92 T.C.M.  
11 (CCH) 498; Rev. Proc. 99-17, § 6.01, subd. 4.) Respondent contends that, even if you assume that  
12 appellants' were considered securities traders under IRC section 475(f), appellants' attempted election  
13 for the 2008 tax year was still invalid because it was filed a year late, and the late-filed election for 2008  
14 cannot be considered valid for subsequent years such as 2009 and 2010. (Resp. Op. Br., p. 7.)  
15 Respondent contends that the instructions to the public on how to make a mark-to-market election are  
16 fairly straightforward, and filing dates are included in IRS Publication 550, which was updated for both  
17 the 2008 and 2009 tax years. (*Id.* at pp. 7-9 & exhibit E.)

18           Respondent asserts that California law conforms to IRC section 475, and states that a  
19 failure to file a valid election for federal purposes prevents appellants from claiming a valid election for  
20 state purposes. (Resp. Reply Br., p. 2; Rev. & Tax. Code, § 17570, subd. (2).) Respondent contends  
21 that appellants appear to be requesting an exception to the deadline for making an election under  
22 Treasury Regulation section 301.9100-3, subsection (b)(1)(iii), which can only apply when a taxpayer  
23 establishes that they acted reasonably and in good faith, and the grant of relief would not prejudice the  
24 interest of the government. However, respondent contends that relief is not granted if specific facts  
25 have changed since the due date for making the election that make the election advantageous to a  
26 taxpayer. (*Id.* at p. 4; Treas. Reg. § 301.9100-3, subs. (b)(3)(iii).) Likewise, the interests of the  
27 government are prejudiced if granting an extension of time to file the IRC section 475 election would  
28 result in a lower tax liability. (*Vines v. Commissioner* (2006) 126 T.C. 279 (*Vines*).) Respondent

1 contends that appellants' facts are similar to those in *Lehrer*, where the taxpayers attempted to file a  
2 late election using hindsight to their advantage after realizing they would sustain losses in the current  
3 and past years. Respondent contends that appellants are attempting to use hindsight to their advantage  
4 by claiming the election for 2008 after the year had ended and they discovered that they would suffer  
5 losses over the year. Respondent notes that appellants claim they decided to make the election after  
6 experiencing a trading loss in the first quarter of 2008. (Resp. Reply Br., pp. 4-5.)

### 7 Applicable Law

8 IRC section 475(f)(1)(A) provides generally that a person who is engaged in a trade or  
9 business as a trader in securities and who makes a mark-to-market election with respect to certain  
10 securities shall recognize a gain or loss (as ordinary income or loss) on those securities held at the end  
11 of the taxable year as if such securities were sold for fair market value on the last business day of that  
12 taxable year.<sup>8</sup> (Int.Rev. Code, § 475(d)(3)(A)(i).) IRC section 475 does not define the terms "trade or  
13 business" or "trader" for purposes of the statute.

14 In holding that a full-time gambler who made wagers solely for his own account was in a  
15 "trade or business" for purposes of IRC sections 162(a) and 62(a)(1), the United States Supreme Court  
16 commented that (1) the Internal Revenue Code has never contained a general definition of a "trade or  
17 business," (2) the Treasury has never promulgated a regulation expounding a meaning of that term for  
18 all purposes, and (3) a broadly applicable and authoritative judicial definition has never emerged.  
19 (*Groetzinger, supra*, 480 U.S. at p. 27 (*Groetzinger*)). The Court further stated that its task in  
20 *Groetzinger* was to ascertain the meaning of the term as it appeared in IRC sections 162(a) and 62(a)(1)  
21 and cautioned that it did not purport to interpret the term as it appeared in other contexts. (*Ibid.*)  
22 However, in discussing the distinction between a "trade or business" and other kinds of income-  
23 producing or profit-making activities, the Court stated that it accepts that, in order to be engaged in a  
24 "trade or business," the taxpayer must be involved in the activity with continuity and regularity and that  
25 a sporadic activity, a hobby, or a diversion for amusement does not qualify. (*Id.* at p. 35.)

26 The Tax Court discusses the term "trader" in the general context of the federal income  
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28 <sup>8</sup> California conforms to this IRC provision per R&TC section 17570, subdivision (d).

1 tax laws by contrasting that term with the terms “investor” and “dealer.” (*King, supra*, 89 T.C. at p.  
2 457-459.) The Tax Court stated in *King* that a “trader” seeks profits from short-term market swings and  
3 obtains income primarily from selling on an exchange rather than from dividends, interest, or long-term  
4 appreciation. (*Id.* at p. 458.) The Tax Court further stated that a “trader will be deemed to be engaged  
5 in a trade or business if his trading is frequent and substantial.” (*Ibid.*) The Tax Court then stated that  
6 an “investor,” on the other hand, buys for capital appreciation and income, generally without regard to  
7 short-term developments that would influence prices on a daily basis and is never considered to be in a  
8 “trade or business” with respect to his investment activities regardless of their extent. (*Id.* at p. 459.)  
9 The court in *Moller* aided in helping define whether taxpayers involved in securities transactions were  
10 engaged in the trade or business of being securities traders by providing the factors of (1) the taxpayer’s  
11 intent; (2) the nature of the income derived from the activities; and (3) the frequency, extent, and  
12 regularity of securities transactions. (*Moller, supra*, 721 F.2d at p. 813.)

13 Revenue Procedure 99-17 requires, in pertinent part, that a taxpayer seeking to make a  
14 mark-to-market election under IRC section 475(f) must file a statement with the IRS that describes the  
15 election being made, the first taxable year for which the election is effective, and the trade or business  
16 for which the election is made. The revenue procedure also requires that the statement must be filed no  
17 later than the due date (without regard to extensions) of the original federal tax return for the taxable  
18 year immediately preceding the election year and must be attached to that return or to a request for an  
19 extension of time to file that return.

20 In *Vines*, the taxpayer filed his mark-to-market election for the 2000 tax year on July 21,  
21 2000, shortly after discovering that the election existed but after the April 15, 2000 due date. The court  
22 determined that appellant incurred no further losses between the time he should have filed his election,  
23 April 15th, and the date he filed the election, July 21st, and therefore the government would not be  
24 prejudiced by the late election under Treasury Regulation section 301.9100-3, subsection (3)(c)(1)(i),  
25 “because granting petitioner an extension of time to file his section 475(f) election does not result in  
26 petitioner’s having a lower tax liability than he would have had if he had timely filed the election.”  
27 (*Vines, supra*, 126 T.C. at p. 295.) Conversely, the exception provided in Treasury Regulation section  
28 301.9100-3 is not allowed when facts have changed from the due date for the election to when the

1 election is filed that are advantageous to the taxpayer, or when taxpayers file late elections and through  
2 hindsight convert capital gains into ordinary losses. (*Lehrer, supra*, 90 T.C.M. (CCH) 20; *Knish, supra*,  
3 92 T.C.M. (CCH) 498.) “A trader has not acted reasonably and in good faith if the trader uses hindsight  
4 in requesting relief by attempting to make an [election] years after the election was due in order to  
5 convert capital losses into ordinary losses.” (*Kantor v. Commissioner* (2008) 96 T.C.M. (CCH) 500.)  
6 Furthermore, there is no legal authority allowing for a failed election for one year to be converted into a  
7 valid election for a subsequent year. (*Knish, supra*, 92 T.C.M. (CCH) 498.)

8 It is well established that a presumption of correctness attends respondent’s  
9 determinations as to issues of fact and that appellant has the burden of proving such determinations  
10 erroneous. (*Appeal of Oscar D. and Agatha E. Seltzer*, 80-SBE-154, Nov. 18, 1980.)

#### 11 STAFF COMMENTS

12 Appellants’ returns asserted business losses for each year based on the use of the  
13 mark-to-market accounting method for their securities activity and thereby offset ordinary wage income  
14 with stock losses to reduce or eliminate their tax liability for each year. Respondent contends that  
15 appellants’ attempted use of the mark-to-market election is invalid because (1) appellants did not  
16 properly make the election, and (2) the election can only be made by securities traders and appellants are  
17 not securities traders. Respondent asserts that the losses from securities activity must be considered  
18 capital losses, which results in a limit of \$3,000 of said losses that can be claimed as deductions for each  
19 year at issue. The questions before the Board are whether appellants have shown that they are traders in  
20 securities, as that term applies to IRC section 475, and whether they also properly made the mark-to-  
21 market election for 2008 in accordance with IRC section 475.

22 The difference between appellants’ reported tax liability for each year and respondent’s  
23 proposed assessments appears to be based mostly on the application of the mark-to-market accounting  
24 method to the 2008 tax year, which resulted in claimed ordinary losses of \$243,426. Appellants used  
25 these losses to offset all ordinary income for 2008, and then used the remaining \$129,214 of claimed  
26 ordinary losses from 2008 on their 2009 and 2010 returns to eliminate or greatly reduce the tax  
27 liabilities for those years. Appellants also claimed ordinary losses through the use of the mark-to-  
28 market election for 2009 and 2010 in the amounts of \$15,239 and \$23,012, respectively.

1           In discussing whether appellants were engaged in the trade or business of securities  
2 trading, the parties should be prepared to discuss the trading patterns of appellants and whether they  
3 meet the frequency, extent, and regularity that would be attributable to traders who are looking to profit  
4 from the daily fluctuations in price. In this discussion, the parties may wish to discuss the relevance of  
5 the irregularities in trading, such that over half of all trades in 2010 were conducted just in one month,  
6 and approximately two-thirds of all trades were conducted in just four months for both 2008 and 2009.  
7 Respondent asserts that individuals in the trade or business of securities trading need to have the intent  
8 that income from their trading activity will be their primary source of income. Appellant-husband had  
9 a full-time job unrelated to securities trading, and appellants asserted that securities trading was  
10 something they started doing when they became concerned over the security of appellant-husband's  
11 full-time job. The parties should discuss whether appellants' securities trading should be considered a  
12 substantial and frequent business activity or whether it was more akin to a hobby that was engaged in  
13 irregularly and supplemental to appellant-husband's primary employment.

14           Appellants only make arguments with regard to 2008 and 2009 in their reply brief, and  
15 should clarify whether they continue to contend that appellant-husband or appellants should be treated  
16 as being in the trade or business of securities trading in 2010.

17           Appellants' returns listed only appellant-husband on the Schedule C, provided a business  
18 or profession of "Securities Exchangee" in the singular, and listed the business name as his personal  
19 name. Throughout their supplemental brief, appellants only argue that appellant-husband was a  
20 securities trader, without mention of appellant-wife. Appellants should clarify whether they now  
21 contend that only appellant-husband was a securities trader for the years at issue. The parties may wish  
22 to discuss whether only appellant-husband was a trader in securities, and what effect that finding has on  
23 the analysis herein. For example, should the Board evaluate whether appellants were traders in  
24 securities based on only appellant-husband's claimed time spent trading and only include transactions  
25 conducted by appellant-husband?

26           Appellants filed their IRC section 475 election for the 2008 tax year approximately one  
27 year late, and therefore failed to file a timely election for the 2008 tax year; however, appellants  
28 contend that an exception should apply to them because they acted reasonably. At protest, appellants

1 indicated that they decided to make the mark-to-market election after they experienced losses in the  
2 first quarter of 2008. Appellants should explain further when they discovered these losses, when they  
3 learned about the mark-to-market election, and whether they reviewed the IRS Publication 550 when  
4 filing their returns for 2007 to learn about how to properly make an IRC section 475 election. The  
5 parties should discuss the requirements of Treasury Regulation section 301.9100-3, and whether  
6 appellants meet the requirements for that exception. Specifically, the parties should discuss whether  
7 appellants' late-filed election gave them the benefit of hindsight, allowing them to convert capital  
8 losses to ordinary losses, and therefore prejudiced the government in violation of the regulation's  
9 requirements. Similarly, the parties should discuss whether the fact pattern matches that of *Vine*, in  
10 which the late election was allowed after a finding that no further losses were recognized between the  
11 due date of the election and when the election was ultimately filed, or whether the facts here more  
12 closely match those of *Lehrer*, *Knish*, and *Kantor*, where taxpayers attempted to benefit from hindsight  
13 in turning capital losses into ordinary losses and thereby reduce their tax liability.

14 Case law provides that an election for one year, once it has been shown to be invalid,  
15 cannot constitute a valid election for a later year. Therefore, the issue of whether appellants have a  
16 valid mark-to-market election for the years at issue should focus only on whether the filed election  
17 attempt was valid for the 2008 tax year.

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