



BEFORE THE STATE BOARD OF EQUALIZATION  
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of )  
ROBERT G. AND PATRICIA A. PFAU )

**Appearances:**

For Appellants: Lawrence S. **Branton**  
Attorney at Law

For Respondent: Brian W. **Toman**  
Counsel

O P I N I O N

This appeal is made pursuant to section 18594 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Robert G. and Patricia A. **Pfau** against a proposed assessment of additional personal income tax in the amount of **\$2,367.02** for the year 1968.

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The sole question presented by this appeal is whether the gains realized in 1968 by Robert G. Pfau (hereinafter referred to as appellant) from the sale of certain parcels of real property should be treated for tax purposes as capital gains or as ordinary income.

During 1968, and at all times relevant to this appeal, appellant was a real estate broker actively engaged in the trade or business of selling real estate. In December 1967, appellant purchased 289 acres of unimproved land located in San Diego County. Approximately seven months later, appellant sold the first of several parcels of the unimproved property and by the end of 1969 appellant had sold 216 of the original 289 acres. The record on appeal indicates that the land sales which occurred in 1968 were, with one exception, to "related taxpayers" of appellant. Appellant did not solicit customers or advertise, the San Diego property for sale during 1968. However, appellant did solicit customers for the sales which occurred in 1969.

On his federal and California personal income tax returns for the year 1968, appellant reported the **gains** realized from the San Diego property sales which occurred in that year as capital gains. Apparently, appellant reported the gains realized from the 1969 sales as ordinary income. After auditing appellant's 1968 federal return, the Internal Revenue Service determined **that** the sales involved property held by appellant primarily for sale to customers in the ordinary course of his real estate business and, therefore, that the gains derived from those sales must be taxed as ordinary income. Upon receipt of the federal audit report, and relying solely upon the information contained therein, 19 respondent issued the proposed assessment which gave rise to this appeal.

1/ Section 18161 of the Revenue and Taxation Code, **which** defines the term "capital asset," is substantially similar to section 1221 of the Internal Revenue Code of 1954. Both sections provide, in relevant part, that the term "capital asset" does not include "property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business."

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Appellant contends that he purchased and held the San Diego property as a personal investment, not primarily for sale to customers in the ordinary course of his real estate business, and that parcels of the property were sold in 1968 to realize a profit on the investment. In support of his position, appellant emphasizes the fact that the 1968 sales were made to unsolicited purchasers who were "related" to appellant.

The question of whether a person is engaged in the business of dealing in real estate with respect to particular property, and the subsidiary question of whether specific sales of the property are sales of property held primarily for sale to customers in the ordinary course of that business, are essentially **questions** of fact to be resolved on the basis of the totality of circumstances presented in each particular case. (See Austin v. Commissioner, 263 F.2d 460 (9th Cir. 1959); Appeals of Ben F. and Emily Moore, Cal. St. Bd. of Equal., Jan. 4, 1966.) The factors relevant to such inquiry include: the purpose for which the property was acquired: the purpose for which the property was held at the time of its sale: the frequency, continuity, and size of the sales: the nature and extent of the **taxpayer's** business; whether the taxpayer or his agents engaged in selling activities; and the proximity of the sale to the purchase. (See Robert W. Pointer, 48 T.C. 906, 915 (1967), aff'd, 419 F.2d 213 (9th Cir. 1969); Auda C. Brodnax, T.C. Memo., June 22, 1970; Appeal of James H. and Eula G. Arthur, Cal. St. Bd. of Equal., Aug. 3, 1960.)

Appellant maintains that he purchased and held the San Diego property as a personal investment, and not **primarily** for sale to customers in the ordinary course of his **real** estate business. **However, the** record on appeal does not indicate whether appellant, either as a real estate broker or in the ordinary course of his established real estate business, regularly engaged in the purchase, subdivision, and sale of large tracts of unimproved real property. Other than general assertions regarding his intent or purpose in purchasing and holding the San Diego property, appellant has made no attempt to distinguish that venture from the general **activities** of his real estate business.

While the record on appeal does not specify the number and sizes of unimproved lots sold by appellant

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in each of the years 1968 and 1969, it seems clear that the San Diego property sales occurred frequently and continuously during those years. Moreover, **other** than the **fact** that the 1968 sales involved unsolicited customers who were "related" to appellant, the record provides no basis for distinguishing the 1968 sales from those which occurred in 1969. To the contrary, the record contains virtually no information regarding the nature of the **transactions in question** or **the identities of the parties involved.**

Appellant, as **an active real estate broker** during the year in question, has the burden of **establishing** that specific properties sold by him were held for personal investment and not for sale to **customers in the ordinary course of his real estate business.** (Margolis v. Commissioner, 337 F.2d 1001, 1004, modified, 33.9 F.2d 537 (9th Cir. 1964) .) It is **our** opinion that appellant has not **sustained** that burden; accordingly, **respondent's action** in this matter must **'be sustained,**

