



BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
THE **ESTATE** OF GEORGE E. P. GAMBLE,)
CROCKER NATIONAL BANK, EXECUTOR')

Appearances:

For Appellant: Conrad F. Gullixson
Attorney at Law

For Respondent: Mark **McEville**
Counsel

O P I N I O N

This appeal is made pursuant to section 18593 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of the Estate of George E. P. Gamble, **Crocker** National Bank, Executor, against proposed assessments of additional personal income tax in the amounts of **\$4,217.83** and \$49.20 for the taxable years ended January 31, 1974 and January 31, 1975, respectively.

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The issue presented for determination is whether respondent properly determined that appellant was precluded from using capital losses arising from the sale of securities as an "offset" against income for income tax purposes when the same capital losses had previously been deducted on the **inheritance** tax return filed on appellant's behalf.

Appellant, an estate, was created on May 20, 1972, upon the death of George E. P. Gamble. In July 1972, appellant's executor sold securities for the purpose of raising the funds necessary to pay debts, taxes, and administration expenses. The entire loss of **\$560,030.12** resulting from this sale was taken as a capital loss deduction in the inheritance **tax** return later filed on appellant's behalf.

The first fiduciary income tax return filed on appellant's behalf for the taxable year ended January 31, 1973, reflected a loss of **\$560,030.12** from the sale of securities in 1972. Appellant claimed a capital loss deduction to the extent of the statutory limit of \$1,000.

On the fiduciary **income** tax return filed for appellant for the taxable year ended January 31, 1974, capital gains of \$42,117 **were subtracted from the** capital loss carryover of \$363,038 that appellant claimed from the previous year. An additional \$1,000 of the remaining capital loss carryover was **claimed as** a deduction from other income. On the fiduciary income tax return for the taxable year ended January 31, 1975, \$1,000 of the capital loss carryover from 1974 was claimed as a deduction from income.

Upon examination of the aforementioned returns, respondent determined that **appellant's use** of its capital loss carryover to "offset" income of \$43,117 and \$1,000 for the taxable years ended January 31, 1974 and 1975, respectively, was improper in that the entire capital loss had previously been deducted on its inheritance tax return. Respondent subsequently issued the proposed assessments in issue.

Appellant contends that the capital losses claimed in 1974 and 1975 were "offsets" against income it earned during those years. Appellant asserts that, during the years in issue, Revenue and Taxation Code section 17746 permitted the use of its capital loss carryover as an "offset" for income tax purposes even

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though the same capital losses had previously been deducted on the inheritance tax return filed on its behalf. After a careful review of the record on appeal, and for the specific reasons set forth below, it is our opinion that respondent acted **properly** in this matter and that its determination must be upheld.

Revenue and Taxation Code section 17746 currently provides as follows:

Amounts allowable, under Section 13988 or 13988.1 of this code, as a deduction in determining the net amount subject to inheritance tax shall not be allowed as a deduction (or as an offset against the sales price of property in determining gain or loss) **in** computing the **taxable** income of the estate, or of any other person, unless there is filed, within the time and in the manner and form prescribed by the Franchise Tax Board, a statement that the amounts have not been allowed as deductions under Section 13988 or 13988.1 and a waiver of the right to have such amounts allowed at any time as deductions under Section 13988 or 13988.1. This section shall not apply with respect to deductions allowed under **Article 7** (relating to income in respect of decedents)-. (Emphasis added.)

Section 17746 was amended in 1977 to include the parenthetical phrase **in the** first sentence. This amendment, operative for taxable years beginning in 1977, was ineffective for the years in issue here. Appellant **argues**, however, that the amendment indicates by implication that, for taxable years beginning prior to January 1, 1977, use of a capital **loss** carryover as an "offset" against income **was proper** even though the identical capital loss had previously been deducted for inheritance tax purposes. Appellant, while readily acknowledging that no authority exists to support this interpretation of section 17746 prior to its 1977 amendment, maintains that the only possible explanation for the 1977 amendment is that the Legislature intended to eliminate the use of such capital loss "offsets!" when a capital loss had previously been deducted for inheritance tax purposes. Consequently, appellant argues, respondent's disallowance of its "offsets" is a retroactive application of section 17746 as it read subsequent to its 1977 amendment.

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Appellant has acknowledged that section 17746 was amended in 1977 following the adoption of an identical parenthetical phrase in that section's federal counterpart, section 642(g) of the Internal Revenue Code, in 1976. The legislative history of **the federal** statute reveals that Congress determined the parenthetical language was necessary solely to prevent the double deduction of items, such as selling expenses, which had been termed "offsets" by some courts. (H.R. Conf. Rep. No. 94-1515, 94th Cong., 2d Sess. p. 625 (1976); [1976 U.S. Code Cong. & Ad. News 4263].) As noted in the House Conference Report, section 642(g) had been interpreted in several court decisions to permit items which reduce the sale price, such as selling expenses, to be deducted for estate tax purposes as well as to reduce the sales price for income tax purposes.

A review of several of these decisions confirms that appellant's use of its capital loss carryover cannot be construed as an "offset" **within** the criteria of those decisions. In The Estate of Viola E. Bray, 46 T.C. 577 (1966), affd., 396 F.2d 452 (6th Cir. 1968), the court held that selling expenses incurred by an estate upon the sale **of** securities could be subtracted as an offset from the proceeds of the sale, notwithstanding the deduction of the same expenses in computing the estate tax liability. The Tax Court ruled that the selling expenses could be used as an offset because such expenses did not qualify as deductions for income tax purposes. The court noted that selling expenses are actually capital expenditures which are not deductible for income tax purposes but which can be **utilized as a setoff** against the selling price. (See also Estate of Walter E. Dorn, 54 T.C. 1651 (1970); Kreher v. United States, 25 Am. Fed. Tax. R.2d 938 (1970); Commerce Trust Co., Executor v. United States, 24 Am. Fed. Tax. R.2d 5918 (1969).)

Appellant's contention that its capital loss constituted an allowable "offset" for income tax purposes is, in view of the manner in which that term was interpreted by the above cited decisions, without foundation. Those decisions characterized an "offset" as a capital expenditure which could not be deducted for income tax purposes. Appellant's subject capital loss was not a capital expenditure nor was it nondeductible for income tax purposes. The capital loss could have been used as a deduction in computing the taxable income of the estate had it not previously been deducted **for**

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inheritance tax purposes. While appellant claims that its use of its capital loss carryover is an "offset" under the criteria of the Bray decision, supra, it is evident from the above discussion that such use actually constituted a prohibited double deduction of its capital loss. Accordingly, we must conclude that respondent's action in this matter was correct.

