BEFORE THE STATE BOARD OF EQIJALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
CHESTER A. ROWLAND)

For Appellant: Chester A. Rowland, in pro. per.

For Respondent: Bruce W. Walker
Chief Counsel

Timothy W. Boyer
Counsel

OPINION

This appeal is made pursuant to section 19059 of the Revenue and Taxation Code from the action of the Franchise Tax Board in denying the claim of Chester A. Rowland for refund of personal income tax in the amount of $321.00 for the year 1972.

The question presented is the constitutionality of legislation limiting the offset against current capital gains of certain pre-1972 capital losses when carried over from previous years.

Appellant is a California resident. On Schedule D accompanying his 1972 state income tax return he reported a $4, 422 ne.t gain from the 1972 sales of capital assets held for not more than one year. All but $118 thereof reflected proceeds from the sales of property held more than six months. Appellant included the entire $4,422 in computing taxable income. He disclosed a $12, 173 net gain from the 1972 sales of capital assets held more than one year but not exceeding five years, and took 65 percent of that amount into account in computing taxable income. Appellant also reported a net loss of $2,753 from the 1972 sales of capital assets held over five years, and reduced his capital gains by.50 percent of this amount. Appellant used these percentages, based on holding period length, pursuant to section 18162.5 of the Revenue and Taxation Code, enacted December 8, 1971, and by its terms applicable to years beginning after December 31, 1971.1/

Appellant incurred capital losses from 1969 through 197 1, totaling $16,911 in excess of the amount that he could apply against capital gains or ordinary income for those years. Under prior law, all those excess capital losses could be carried forward indefinitely and applied at 100 percent against current capital gains until exhausted. However, pursuant to an amendment enacted

1/ Section 18162. 5, subd. (a), provides:

> In the case of any taxpayer, only the following percentages of the gain or loss recognized upon the sale or exchange of a capital asset shall be taken into account in computing taxable income:
>
> (1) One hundred percent if the capital asset has been held not more than one year;
>
> (2) Sixty-five percent if the capital asset has been held for more than one year but not more than five years:
>
> (3) Fifty percent if the capital asset has been held more than five years.

November 27, 1972, to section 18152 of the Revenue and Taxation Code, and applicable to years beginning after December 31, 1971, only SO percent of established pre-1972 "long-term" capital loss carryovers could be carried over and offset against capital gains. Only pre-1972 "short-term" capital loss carryovers could be fully offset against such gains.2/ The terms "long-term" and "short-term" were defined under prior law. Capital gains and losses were considered "long-term" where the asset was held for more than six months before sale, and "short-term" where the holding period did not exceed six months. (See Rev. & Tax. Code, § 18162 as it read prior to its repeal on November 27, 1972.)

Complying with the amendment, appellant applied 100 percent of the $577 capital loss carryover resulting from the sales of capital assets held- six months or less, and applied 50 percent of the $16,334 capital loss carryover resulting from sales of capital assets held longer than six months. Of the $16,334, $10,411 reflected losses from the sales of capital assets where the holding period did not exceed one year, and the balance represented losses from the sales of capital assets where the holding period exceeded one year but did not exceed five years. By conforming with these statutory changes, appellant reported a net taxable capital gain of. $2,214 for 1972 and paid tax thereon of $221.

2/ Specifically, Revenue and Taxation Code, § 18152, subd. (e), provides:

> In the case of a net capital loss which a taxpayer is entitled to carry over from any taxable year beginning before January 1, 1972--
>
> (1) If the net short-term capital loss (as defined prior to the repeal of Section 18162 by the 1972 session of the Legislature) exceeded the net long-term capital gain (as defined prior to the repeal of Section 18162 by the 1972 session of the Legislature), the excess shall be carried over a.t 100 percent.
>
> (2) If the net long-term capital loss (as.defined prior to the repeal of Section 18162 by the 1972 session of the Legislature) exceeded the net short-term capital gain (as defined prior to the repeal of Section 18162 by the 1,972 session of the Legislature), the excess shall be carried over at 50 percent.

Thereafter, appellant filed a second return for 1972 in which, contrary to the amendment of section 18152, he applied 100 percent of his pre-1972 capital loss carryover against his capital gains. As a result of this computation there was no net taxable capital gain shown; rather, an overall capital loss in excess of $1,000 resulted. Appellant's computation indicated that he overpaid his 1972 tax liability by $321, and was entitled to a capital loss carryover for subsequent years. Respondent treated the second return as a claim for refund of $321, and denied the claim. This appeal followed.

Appellant contends that the amendment limiting the offset of pre-1972 "long-term" capital loss carryovers is unconstitutional, inequitable, and inconsistent.

In support of his argument that the legislation is unconstitutional, appellant asserts that this amendment imposes an arbitrary tax burden upon him and others who are deprived of established "long-term" capital loss carryovers under similar circumstances. Appellant views this legislation as arbitrarily placing "over six month" holding periods in the category of "over 60 month!' holding periods. Therefore, one of his constitutional challenges is that the classification is. arbitrary and thus amounts to a denial of equal protection. He also urges that prior law implied a promise that all pre-1972 "long-term" capital loss carryovers could be fully applied against all current "long-term" capital gains, or at least could be applied in the same percentage that current capital gains, with similar holding periods, are taken into account. Therefore, appellant claims that a prior right has been wrongfully "dissolved". Accordingly, the second constitutional challenge is that there has been confiscation, i. e. , a denial of due process by legislation operating retroactively to deprive him of a vested property right. These two constitutional challeges (arbitrary classification and confiscation) are repeated by an assertion that appellant is paying a tax on losses rather than on income,

In making these constitutional challenges, appellant stresses that tax is imposed notwithstanding the following facts: (1) Virtually all loss carryover is only brought forward at 50 percent (and the balance "lost") but current net capital gains

are taken into account at 65 and 100 percent even though the same predominant holding period (more than 6 months but not over 60 months) preceded both: and (2) Established pre-1972 capital loss carryover ($16,911) exceeded 1972 net capital gains ($13,842) by $3,069. 3/

However, for the reasons explained in the Appeal of Homer B. and Lennie Mae Davis, decided this same date, we cannot conclude that any of appellant's constitutional rights were violated. We recognize that appellant, in claiming he is paying a tax on losses, has emphasized that his capital loss carryover exceeded the net capital gain from 1972 sales. This fact does distinguish this appeal from Davis to the extent that in Davis the current net capital gain from 1972 sales was in excess of the established capital loss carryover. Nevertheless, as in Davis, appellant is not paying a tax on losses. Just as in that appeal, a current deduction for losses of prior years is merely being limited.

Appellant also claims that inconsistency in the law's method of treating pre-1972 capital loss carryovers is apparent when that method is compared with the method of handling such carryovers under prior law and the method of handling post - 1971 capital loss carryovers under present law. As already explained, under prior law all capital loss carryovers were applied at 100 percent against current capital gains. Under present law, post- 1971 capital loss carryovers are applied at the same percentages that current capital gains and losses are taken into account. (Rev. & Tax. Code, §§ 18152, 18162.5) Appellant views the prior law and the present method of handling post - 197 1 carryovers as reasonable, but considers the transitional method of treating pre-1972 capital loss carryovers as inconsistent and unreasonable.

3/ These are also the principal reasons why appellant urges that the statute operated inequitably. By viewing 1969-1972 as one taxable period, appellant also maintains that the tax burden on capital gain transactions was greater than on ordinary income (and thereby inequitable) because tax was paid even though capital losses exceeded capital gains over the four year period. However, the law does not provide for determining taxable income on the basis of periods in excess of one year. (See Rev. & Tax. Code, §§ 17551, 17553.)

In support of his overall position, appellant has offered a number of calculations illustrating alternatives to section 18152, subdivision (e)(2) of the Revenue and Taxation Code, which, he maintains, are more equitable. Under all these calculations, appellant would be entitled to a $321 refund for 1972 and a capital loss carryover for subsequent years. We have thoroughly analyzed all these alternatives and they are clearly at variance with the plain language of the statute. This board is charged, with interpreting the law as enacted by the Legislature, and lacks authority to change that law. Thus, while we understand why appellant regards the amendment as inequitable and inconsistent and has offered alternatives, his disagreement with the amendment on otherthan constitutional grounds should be directed to the Legislature which is charged with formulating the law, and not to those charged with its enforcement. (Appeal of Samuel R. and Eleanor H. Walker, Cal. St. Rd. of Equal., March 27, 1973.)

Inasmuch as we have concluded that the legislation did not deny appellant any of his constitutional rights, we must 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 Chester A. Rowland

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 1.9060 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the claim of Chester A. Rowland for refund of personal income tax in the amount of $321.00 for the year 1972, be and the same is hereby sustained.

Done at Sacramento, California, this 21st day of October, 1975, by the State Board of Equalization.

John W. Lynch, Chairman

Member

George R. Reilly, Member

Member

Member

ATTEST: Cecil Dunlop, Executive Secretary