

OFFICIAL TRANSCRIPT PROCEEDINGS BEFORE

THE SUPREME COURT OF THE UNITED STATES

DKT/CASE NO. 85-1226

TITLE COMMISSIONER OF INTERNAL REVENUE, Petitioner V.
ROBERT P. GROETZINGER

PLACE Washington, D. C.

DATE December 8, 1986

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1 IN THE SUPREME COURT OF THE UNITED STATES

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3 COMMISSIONER OF INTERNAL ;

4 REVENUE, ;

5 Petitioner, ;

6 V. ; No. 85-1226

7 ROBERT P. GROETZINGER ;

8 - - - - -x

9 Washington, D.C.

10 Monday, December 8, 1986

11 The above-entitled matter came on for oral
12 argument before the Supreme Court of the United States
13 at 10:02 o'clock a.m.

14 APPEARANCES:

15 ALBERT G. LAUBER, JR., ESQ., Deputy Solicitor General,
16 Department of Justice, Washington, D.C.; on behalf of
17 the petitioner.

18 CARROLL BAYMILLER, ESQ., Peoria, Illinois; on behalf of
19 the respondent.

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1 PROCEEDINGS

2 CHIEF JUSTICE REHNQUIST: We will hear
3 argument first this morning in No. 85-1226, Commissioner
4 of Internal Revenue versus Robert P. Groetzinger.

5 Mr. Lauber, you may proceed whenever you are
6 ready.

7 ORAL ARGUMENT OF ALBERT G. LAUBER, JR., ESQ.,
8 ON BEHALF OF THE PETITIONER

9 MR. LAUBER: Mr. Chief Justice and may it
10 please the Court, the question here is whether a person
11 who spends his full time gambling at racetracks for his
12 own account is engaged in a trade or business for
13 federal income tax purposes. This is a question on
14 which the Commissioner, the courts, and gamblers have
15 gone back and forth over the years, depending largely,
16 it seems, on whether it was good or bad taxwise for a
17 gambler to be in a trade or business at the particular
18 tax year involved under the relevant tax provisions.

19 The provision that gave rise to this case was
20 a minimum tax provision that was in effect from 1976
21 until 1982 under which gambling losses generally were
22 items of tax preference that could give rise to a
23 minimum tax liability. The way a gambler could avoid
24 minimum tax would be to argue that his trade or business
25 was gambling, so that his gambling losses were not

1 garden variety itemized deductions, but rather were
2 trade or business deductions that were exempt from
3 minimum tax.

4 The Court of Appeals below accepted this
5 argument, persuaded in large part by the seeming
6 inequity of imposing a minimum tax on somebody who had
7 net gambling losses for the taxable year, as Mr.
8 Groetzinger did.

9 Congress has eliminated that inequity for
10 years after 1982 because it amended the minimum tax law
11 in that year to remove gambling losses from the minimum
12 tax base. Now that Congress has fixed that, the IRS
13 cannot really tell whether it is better for us to win or
14 lose this case from a revenue point of view
15 prospectively because, as I said, it can be good or bad
16 for a gambler to be in or not to be in business.

17 QUESTION: Do you have any idea how much is at
18 stake?

19 MR. LAUBER: It is impossible to tell, Justice
20 Brennan, because there are so many different numbers on
21 the tax return that can go up or down depending on
22 whether you are in business. It affects the adjusted
23 gross income which is a floor beneath your casualty loss
24 deduction and your medical deduction, the ceiling on
25 your charitable contribution deduction. It can enable

1 you to take home office expenses deductions. It can
2 also make you liable for self-employment tax if you are
3 in a trade or business. It is like the FICA tax
4 employees pay.

5 So, depending on whether the gambler has gains
6 or losses for the year and whether he has medical
7 expenses and so forth it can be good or bad and you
8 simply can't program a computer to figure out what the
9 net will be, so the reason we sought certiorari here was
10 to get a clear answer to the question to resolve the
11 conflict in the circuits and get an answer we hope will
12 be consistent with the overall structure of the --

13 QUESTION: Mr. Lauber, will the decision we
14 make have any consequences under the new tax code to
15 take effect next year or are the definitions changed
16 enough for that that it doesn't have an impact?

17 MR. LAUBER: The new tax code preserves the
18 post-'82 treatment for gambling losses. They are still
19 carved out from minimum tax and so forth. I would think
20 the one possible effect the decision could have -- I
21 haven't read the new tax law from cover to cover but the
22 new tax law does put a 2 percent floor underneath
23 investment type expenses.

24 You can't deduct expenses of investing, of
25 getting advice from brokers, investment, valueline, that

1 kind of stuff except to the extent it exceeds 2 percent
2 of your adjusted gross income, and that basically puts a
3 floor under the Section 212 deduction now in the Code,
4 and there may be some greater incentive for investors to
5 try and say they are in a trade or business under the
6 new tax law to avoid that 2 percent floor.

7 QUESTION: By virtue of Section 212 are there
8 any consequences if this case were affirmed outside the
9 context of full-time gambling? What are the real risks
10 of an affirmance in other areas in your view?

11 MR. LAUBER: The greatest risk to affirmance
12 would be if the Court did anything to impugn the rule of
13 Higgins versus Commissioner, which held that investors
14 are not in a trade or business.

15 QUESTION: Well, it could be affirmed, I
16 suppose, without doing that, depending upon what the
17 elements were of the test to be employed.

18 MR. LAUBER: That's right.

19 QUESTION: Of course, to speak of the rule of
20 Higgins against Commissioner is to give that case the
21 benefit of a good deal of doubt since you tell me what
22 rule it is other than that the government won it.

23 MR. LAUBER: Well, one might say that very
24 well.

25 QUESTION: Mr. Lauber, you argued the slot

1 machine case last year, didn't you.

2 MR. LAUBER: Unfortunately, I did, yes.

3 QUESTION: You are getting to be an expert on
4 gambling devices.

5 MR. LAUBER: I have quite a bit of knowledge
6 about the different subjects now. That is true.

7 QUESTION: Does this definition, what amounts
8 to a trade or business, it will have some general
9 applicability, won't it?

10 MR. LAUBER: It will because the term is used
11 in 50 different sections of the code.

12 QUESTION: And do you think that -- I guess
13 you don't need to know, but is it supposed to mean the
14 same thing in all these sections?

15 MR. LAUBER: Well, it has a number of special
16 purpose definitions and special sections that define
17 it --

18 QUESTION: I see.

19 MR. LAUBER: -- like the unrelated business
20 income tax defines it for purposes of one section. That
21 is true --

22 QUESTION: But at least for some other
23 sections the way this is defined it will be --

24 MR. LAUBER: The majority of them it is the
25 same definition. Section 162, Section 62.1, all of

1 those we generally think have the same meaning of trade
2 or business. The Court of Appeals below held that a
3 trade or business should be defined as any activity that
4 can fairly be characterized as a person's livelihood,
5 occupation, or means of earning a living, so that the
6 only requisites of a trade or business from that point
7 of view are that you carry on an activity on a regular
8 and extensive basis with the intent to earn a profit or
9 livelihood from it. We think this definition has some
10 obvious intuitive appeal but we think it incorrect under
11 the code as we actually know it.

12 QUESTION: Has that been the consistent
13 position of the Tax Court over the years?

14 MR. LAUBER: The Tax Court is one of the
15 courts that has flip-flopped on this question. When it
16 first came to the Tax Court in 1976, Judge Tannenwald
17 defined the term much more narrowly and adopted what we
18 call the goods and services test of Justice
19 Frankfurter's concurring opinion in Deputy v. DuPont to
20 hold that a gambler was not in a trade or business, and
21 the gambler there did not want to be in a trade or
22 business because he was trying to be hit with
23 self-employment tax.

24 And then after Congress put in the minimum tax
25 provision that was bad for gamblers, the Tax Court

1 reversed itself, overruled Judge Tannenwald's opinion,
2 so they have not been consistent. They have kind of
3 sided with the gambler, depending on the equities of the
4 particular tax provision involved for the relevant tax
5 year.

6 QUESTION: You mean they have been on the side
7 of equity?

8 MR. LAUBER: Right. We are not contending
9 that there are any equities on our side in this
10 particular case. We are simply out to get a definition
11 of trade or business that does not damage the entire
12 structure of the revenue code.

13 The code itself regularly distinguishes
14 between trade or business activities and other
15 activities carried on on a regular basis with the intent
16 to earn a profit. Particularly in the landmark case of
17 Higgins, that I mentioned before, this Court held that a
18 full-time investor is not in a trade or business even
19 though he devotes the bulk of his time to managing his
20 securities portfolio and even though he was engaged in a
21 regular course of activity with the intent to earn a
22 profit or livelihood from this portfolio.

23 QUESTION: He was trying to deduct the
24 salaries of his employees, wasn't he, in that case?

25 MR. LAUBER: Mr. Higgins had a very, very

1 large investment portfolio as well as a very large real
2 estate activity apparently, and he did hire people to
3 work for him, bookkeepers. He made all the investment
4 decisions himself, I think. He gave the --

5 QUESTION: Didn't Congress later decide that
6 he should have been able to deduct these expenses?

7 MR. LAUBER: It did, and then it enacted
8 Section 212, but it is important to note that Congress
9 thought that the problem with Higgins was the Court had
10 defined trade or business too narrowly to exclude his
11 kind of expenses. They respond to that not by expanding
12 the definition of trade or business but by enacting a
13 new section, 212, to allow deduction of non-business
14 expenses incurred to produce income on management
15 investment property.

16 QUESTION: Mr. Lauber, does a casino offer
17 goods or services within the meaning of the term as you
18 understand it?

19 MR. LAUBER: The casino itself does, and a
20 bookie would.

21 QUESTION: And what are the services?

22 MR. LAUBER: Well, a casino is running a --

23 QUESTION: Say a casino where you have, say,
24 just a dice table.

25 MR. LAUBER: They are offering roulette, the

1 services of a roulette wheel or a blackjack dealer that
2 gamblers can avail themselves of to gamble. I guess
3 they are not really offering goods but they are offering
4 services. They serve drinks while you are at the gaming
5 table, and a bookmaker --

6 QUESTION: At the slot machines, too?

7 MR. LAUBER: Pardon me?

8 QUESTION: At the slot machines, too?

9 MR. LAUBER: I think that is providing a
10 service in that they are making available to gamblers a
11 facility to -- it is like an amusement park type of
12 service.

13 QUESTION: It is certainly not gambling
14 because gambling is a game of chance, and the casinos
15 don't take chances.

16 (General laughter.)

17 MR. LAUBER: But if you think of this being
18 like an amusement park and they take their cut and they
19 provide fun for people --

20 QUESTION: What if this man provided his own
21 dice and he went to a dice game every day and he brought
22 the dice, played with a bunch of friends and they
23 gambled every day full-time but he is the one who
24 supplied the dice? Would that be enough?

25 MR. LAUBER: I don't think that would be

1 enough to make him --

2 QUESTION: Why isn't that the same as a casino
3 supplying the dice?

4 QUESTION: And it is always at his house.

5 MR. LAUBER: Well, I think -- well, if he did
6 it on a regular, continuous basis and got paid, and got
7 money for it.

8 QUESTION: Well, he gets money when he wins,
9 of course; he doesn't when he loses, just like --

10 MR. LAUBER: But he is the one who is
11 providing the facilities.

12 QUESTION: And they use his kitchen.

13 MR. LAUBER: That is different from being a
14 gambler.

15 QUESTION: If he used his kitchen, he had a
16 permanent poker game or dice game, then he is like a
17 casino. Is that right?

18 QUESTION: You don't really want us to hold
19 that, do you?

20 MR. LAUBER: Well, we don't want you to tell
21 people to hold gambling games in the kitchen as a trade
22 or business. No, we don't want that.

23 QUESTION: I didn't think so.

24 MR. LAUBER: But I think it is different being
25 the vendor or the provider of the facility and the

1 consumer of the services like the respondent here. He
2 was just a gambler who was coming in to play, and we
3 think that Higgins really controls this case, because we
4 can see no real distinction between somebody who engages
5 in a regular course of profit-seeking investment
6 activity and somebody who engages in the regular course
7 of profit-seeking gambling activity.

8 QUESTION: What about real estate
9 development? That is like a person with an investment
10 portfolio?

11 MR. LAUBER: We have an amicus brief filed on
12 behalf of real estate developers, and we think that
13 question is not presented here. There is a particular
14 doctrine that has come up in the tax shelter area called
15 the doctrine of pre-opening expenses that kind of takes
16 care of when a real estate developer -- a real estate
17 investment partnership is in the business of renting
18 apartment units. A developer himself would be in a
19 business all the time because he is engaged in the
20 regular course of developing, improving property.

21 QUESTION: Mr. Lauber, the case of the
22 full-time stock trader seems to me rather analogous to
23 the full-time gambler --

24 MR. LAUBER: Well, I think the --

25 QUESTION: -- and the stock trader is treated

1 as having deductible.

2 MR. LAUBER: There is a line of cases in the
3 lower courts that have held that a stock trader as
4 opposed to an investor is engaged in a trade or business
5 but I think --

6 QUESTION: Do you think that is incorrect,
7 that that shouldn't be the rule?

8 MR. LAUBER: I think one can find analogies
9 both between the investor and the trader to the
10 gambler. Let me say a little bit more concretely about
11 how they are similar.

12 QUESTION: How would you treat, how would you
13 treat the full-time stock trader under the rule you
14 seek?

15 MR. LAUBER: The position of the IRS is that
16 the full-time stock traders who do rapid turnover of
17 investments are in a trade or business, and that goes
18 back to --

19 QUESTION: I think that is really close to
20 this case.

21 MR. LAUBER: I agree, it is very close to this
22 case, and I think that is what makes this case
23 difficult. If we didn't have that line of cases, I
24 think this case would be easy after Higgins.

25 QUESTION: Well, all right, if you were to

1 develop a rule that said if it is a profit-seeking
2 activity, if it is activity that is intensively engaged
3 in over a period of time with personal effort of the
4 taxpayer, and you are not structuring in the preliminary
5 costs of getting into business, I mean, would that take
6 care of your concerns with the investor?

7 MR. LAUBER: I don't think it would, because
8 then you have to ask why did Higgins come out the way it
9 did. If you are right, why wasn't Mr. Higgins, who
10 spent all of his time running around managing his
11 investments and giving buy and sell instruction,
12 picking stocks.

13 QUESTION: Well, it is hard to pay that much
14 reliance on Higgins, which was effectively overruled by
15 statute shortly thereafter.

16 MR. LAUBER: It was only overruled insofar as
17 the result, but Congress did not overrule the holding
18 that he was not in a trade or business. The Congress
19 preserved that holding and enacted a new provision to
20 allow non-business deductions to be taken.

21 QUESTION: What element is missing out of the
22 list I gave you?

23 MR. LAUBER: The element we would say is
24 missing is, he does not hold himself out as offering to
25 sell goods or services to others, and I think that a

1 gambler does not do that, and there are other -- there
2 are some illegal activities, for example, embezzlers.
3 You may have an embezzler who spends his days casing
4 houses and looking for -- trying to find new ways to get
5 money from his employer and tries to make a living doing
6 that, but the courts have held he is not in a trade or
7 business.

8 QUESTION: What about an embezzler that sells
9 shoddy goods and services, misrepresents them and gives
10 you not what he said he would?

11 MR. LAUBER: Well, an embezzler who just takes
12 money out of his --

13 QUESTION: Never mind embezzler. I mean, it
14 is not embezzlement, but a con man who --

15 MR. LAUBER: I think a con man or a drug
16 dealer is in a trade or business because they are
17 selling something. It may be illegal, but if they file
18 the tax return they could claim cost of goods sold.

19 QUESTION: Right, so that sort of takes some
20 of the force out of the fact that an embezzler would be
21 included because under any definition you are going to
22 get some strange people included. It seems to me no
23 more desirable to include con men than it does
24 embezzlers. So no matter what definition you get you
25 are going to get some strange people included as

1 conducting a trade or business.

2 MR. LAUBER: But I think the advantage of
3 Justice Frankfurter's test is, it explains why people
4 like embezzlers and investors and gamblers are not in a
5 trade or business.

6 QUESTION: But the only difference between
7 Higgins and the stock trader is that Higgins didn't move
8 his stuff as fast as a stock trader would?

9 MR. LAUBER: That is what the courts have
10 held, that he --

11 QUESTION: well, and the government agrees, I
12 take it.

13 MR. LAUBER: We agree. We feel we are stuck
14 with that line of cases and don't wish to abandon it.
15 And frankly, if the Court decides that it is impossible
16 to rule in our favor here without disapproving the stock
17 trader cases, my orders are to say that you should
18 affirm the decision below because the service believes
19 that the stock trader cases have become so firmly
20 entrenched in the law, going back to 1918 rulings of the
21 IRS, that they can't be -- they came before Higgins in a
22 way and they can't be abandoned, but we think that the
23 two lines can be reconciled.

24 QUESTION: Mr. Lauber, let me ask you another
25 case. Supposing a person were engaged for his own

1 account in buying and selling old coins or other old
2 artifacts of some kind but he never offered them to the
3 public, he always just kind of gambled on the market and
4 would buy from dealers and sell to dealers. Would he be
5 engaged in a trade or business?

6 MR. LAUBER: I would say he is not. He is a
7 coin collector who is trading --

8 QUESTION: The same sort of thing a stock
9 trader would be. That is even closer to a stock trader,
10 it seems to me, because he is buying and selling
11 something for which there is a market, but he is always
12 doing it just on his own account.

13 MR. LAUBER: The rationale of the stock trader
14 cases is that the trader is trying to take advantage of
15 the kind of short-term swings in the market, like to
16 get -- much as an arbitrageur would, to get a little
17 eighth here, an eighth there, because of market swings,
18 and that requires extremely heavy trading. I don't
19 think a coin investor --

20 QUESTION: How about gold bullion, large
21 quantities of gold bullion always trading on your own
22 account? And you know, there are changes in the market
23 every day on that.

24 MR. LAUBER: Well, I think that the service
25 would agree that a person who dealt in gold bullion in a

1 fashion similar to a stock trader who is held to be in a
2 business would also --

3 QUESTION: It would have to be a short swing
4 situation.

5 MR. LAUBER: It would have to be a very short
6 swing situation, I think, and very, very frequent
7 trades.

8 QUESTION: Am I correct that the Congressional
9 overturning of Higgins only overturns it as to whether a
10 deduction can be taken.

11 MR. LAUBER: That's correct.

12 QUESTION: And that there are other elements
13 in the Tax Code which continue to apply the Higgins rule
14 to someone who is managing his own investments,
15 detrimentally or, for that matter, favorably to that
16 individual as not considering that a trade or business
17 for purposes of other provisions of the code.

18 MR. LAUBER: That's right. Section 212 allows
19 someone to deduct expenses incurred in managing his
20 investments, but it would not allow him to deduct, say,
21 home office expenses, and that is why full-time
22 investors continue to try and seek trade or business
23 status to be able to take other deductions outside of
24 212 under Section 162, and the like.

25 But I think it may be helpful to consider in a

1 kind of concrete way what a full-time investor does,
2 resembles what a full-time gambler does. A full-time
3 investor presumably spends much of his time reading the
4 Wall Street Journal and becoming knowledgeable about
5 where to put his money. He reads Value Line, follows
6 the Dow-Jones ticker, reads corporate 10K statements,
7 consults with brokers and people in the industry trying
8 to figure out what the best companies or commodities
9 are, and once he has gotten educated he places a bet
10 essentially on a particular corporation or commodity by
11 buying a securities contract, and he thereby expresses
12 his hope that that company will do better than all the
13 other companies on the stock exchange. If he is right,
14 he will get a payoff many times his investment. If he
15 is wrong, he may become worthless.

16 Now, a gambler who gambles full-time is very
17 similar. He presumably spends his days becoming
18 knowledgeable about where to put his money. He reads
19 the newspapers, racing programs, racing forms.

20 QUESTION: He only reads the Morning
21 Telegraph.

22 MR. LAUBER: Excuse me?

23 QUESTION: (Inaudible) he only reads the
24 Morning Telegraph?

25 MR. LAUBER: Excuse me?

1 QUESTION: (Inaudible) maybe he reads.

2 MR. LAUBER: Well, he probably reads the
3 racing columns in all the newspapers. That may take a
4 couple of hours in the morning. And then he goes down
5 to the track and he talks to jockeys and other bettors
6 and tries to get a sense of what the best horses or dogs
7 are, and he then places his bet on the horse or dog he
8 thinks is going to do best by buying a betting slip, and
9 both the full-time gambler and the full-time investor
10 are taking some risks, but basically they hope they can
11 beat the market because of the superior information and
12 sophistication they have by doing what they do
13 full-time.

14 We think that neither of them, despite the
15 fact he uses some skill in what he is doing, is in a
16 trade or business, and the reason is, the reason Justice
17 Frankfurter gave in his concurring opinion in Deputy v.
18 DuPont, a case a year before Higgins which likewise
19 involved an investor, and he said that an investor is
20 not in a trade or business because he does not hold
21 himself out to others as engaged in the selling of goods
22 or services.

23 The same we think is true of a gambler who
24 does not act as a bookie or casino operator or sell tips
25 to other people, but rather gambles solely for his own

1 account. We think the goods or services test is a
2 useful tool for differentiating the world of trade or
3 business activities from a somewhat larger universe of
4 activities undertaken with the intent to make a profit.
5 It explains why investors are not in a trade or business
6 no matter how extensive and busy they are about their
7 investments.

8 It explains why gamblers of all types, whether
9 they play roulette, poker, bingo, keno, or horse races,
10 are not in a trade or business. It explains why
11 housewives or househusbands who sit home and cut the
12 tops of cereal boxes and enter contests all day are not
13 in a trade or business. And it explains why people like
14 embezzlers and burglars are not in a trade or business.

15 Each of these people may spend a lot of time
16 all day trying to --

17 QUESTION: But not why con men are not in a
18 trade.

19 MR. LAUBER: I think -- well, a con man, he
20 has to be offering goods or services, and if he is
21 selling deficient products I would say he is in a trade
22 or business. If he is simply trying to --

23 QUESTION: That really does not make the best
24 of all possible worlds, even this test, right? There
25 are still some strange things that are going to be --

1 MR. LAUBER: There always will be strange
2 cases, that's true, that are hard to categorize one way
3 or the other. We think the Frankfurter formula is also
4 useful as an administrative device because it allows
5 whole categories of taxpayers to be classified and
6 thereby avoiding the ad hoc and arbitrary line drawing
7 approach that the respondents' approach would require.

8 For example, under the approach that
9 respondent would urge the Court would have to figure out
10 how much time one needs to spend on gambling to make it
11 a trade or business, and there probably are millions of
12 people in the country who gamble, many of whom, one
13 suspects, are not in a trade or business, and the Courts
14 would have to draw really arbitrary lines between casual
15 and truly dedicated gamblers.

16 The courts might also have to draw arbitrary
17 lines between different types of gambling activities.
18 The respondent probably himself would agree that a
19 retired person who lives in Las Vegas and plays slot
20 machines eight hours a day is not in a trade or
21 business. I think that would have to be -- that would
22 be correct. And respondent might try and distinguish
23 between gambling like bingo and slot machines and
24 roulette from activities like poker, horseracing, and
25 dog racing on the theory the latter involved more skill

1 and are not purely, purely games of chance, and that
2 also, I think, could require difficult line drawing
3 problems depending on how much time the gambler spent on
4 each type of gambling.

5 QUESTION: Where would you put numbers?

6 MR. LAUBER: Where would I put?

7 QUESTION: Numbers? Oh, you don't know
8 anything about that?

9 MR. LAUBER: I don't think I know much about
10 that.

11 QUESTION: That's gambling. Lottery. Yes,
12 where would you put that, where somebody buys a lottery
13 ticket for ten cents every day?

14 MR. LAUBER: I think that would be like
15 bingo. Well, our position is, all gambling, all
16 gamblers don't qualify, and I think that clearly is on
17 the end of pure chance. There is not much skill
18 involved, I guess, in buying lottery tickets. It is
19 like, you know, again like the houseperson who just
20 enters contests and sends off jingles to cereal
21 companies.

22 And the problem is, because it can be good or
23 bad to be in a trade or business, depending on the
24 gambler's particular facts, whether he won or lost money
25 for the year, what he is trying to deduct. Gamblers can

1 pull all these factual levers and pulleys involving how
2 much time they spend and what kind of gambling they are
3 doing trying to get the best result for that.

4 QUESTION: What is the difference between
5 sending in a bunch of jingles in a contest and sending a
6 bunch of short stories to a magazine editor?

7 MR. LAUBER: Well, again, it would depend on
8 the amount of time and seriousness spent. If a person
9 seriously was writing advertising copy for corporations
10 I think that would be a trade or business, because you
11 are offering services. Someone who just sends off
12 jingles that get put in a bin and they spin around and
13 pick one out would not be. That would simply be
14 entering a contest. That would not be --

15 QUESTION: Yes, but don't they sometimes
16 publish the winners of those and use the jingle in their
17 advertising?

18 MR. LAUBER: Well, maybe if you then became
19 established as a good copywriter you could wind up later
20 on being --

21 QUESTION: Suppose he just wrote one story and
22 it is published. What about one jingle that is
23 published on some nationally advertised product and
24 millions of people see it on television?

25 MR. LAUBER: Probably in either event just

1 doing it once wouldn't be enough besides selling goods
2 you have to also do it on a regular basis.

3 QUESTION: An author who writes 100 stories
4 and only one gets published isn't engaged in a business,
5 and a guy who writes 100 jingles and one gets -- I don't
6 understand the difference.

7 MR. LAUBER: I think the difference is that
8 the jingles have an element of entering a contest in
9 them, and that --

10 QUESTION: They provide a service. I think --
11 maybe I am wrong, but it is my understanding they use
12 these things in their advertising if they hit one that
13 is particularly, you know, attractive to the audience.
14 I don't know why that is any different than writing a
15 short story.

16 MR. LAUBER: It might also be hard to show a
17 profit motive if you are writing jingles like thousands
18 of people.

19 QUESTION: If you did it full-time. we are
20 assuming this is full-time activity, and it is the only
21 way he gets any money, like this man.

22 QUESTION: This one only involved \$2,000 a
23 year.

24 MR. LAUBER: Well, it only involves \$2,000 a
25 year. That is absolutely right. And we had no desire

1 to subject Mr. Groetzinger to --

2 QUESTION: (Inaudible.)

3 MR. LAUBER: Well, the reason we had to seek
4 certiorari was because there was a circuit conflict on
5 the question and the Commissioner couldn't simply change
6 his position because either way he went it would be good
7 or bad for some gamblers. We had to have a clear answer
8 from this Court, and we tried to keep it out of the
9 Court for a long time, and finally we couldn't avoid it
10 any longer and here we are, and we need to have an
11 answer.

12 QUESTION: But the Higgins case was decided in
13 about 1940 or '41, and in all this time nobody has ever
14 asked Congress to help you out in this problem. Is that
15 right? I suppose they can decide some of these issues.

16 MR. LAUBER: Well, Congress did help gamblers
17 out in that it took care of the minimum tax problem that
18 created this litigation, but I think Congress has simply
19 decided to leave to the Courts defining this term,
20 because it has been a judicial term for a great many
21 years, and --

22 QUESTION: (Inaudible) any legislation
23 defining it?

24 MR. LAUBER: Not generally. There have been
25 proposals to find out particular purposes.

1 QUESTION: But has the Commissioner
2 consistently taken the position that trade or business
3 means what you now urge it means?

4 MR. LAUBER: well, except for the first
5 gambler case to come to the Tax Court when he argued
6 that the gambler was in business so he could be hit with
7 self-employment tax, that, I think, is the only
8 departure that I am aware of from the consistent
9 position that the Frankfurter formula is correctly part
10 of the test for trade or business. And we took that
11 position in the Snow case which involved the research,
12 R&D expenses in this Court, and the Department of
13 Justice determined not to appeal that first Tax Court
14 case where the Commissioner lost, and the Commissioner
15 agreed with the no appeal decision.

16 QUESTION: But he never wrote any regulations
17 on the point, either.

18 MR. LAUBER: There are no regulations that
19 define trade or business for all purposes. It may be
20 that the reason that -- the term does appear in so many
21 different parts of the code that it may be that there is
22 a reluctance to have a regulation define it for all
23 purposes for fear of having something being whipsawed in
24 some context, but it is a term the courts have tried to
25 define, and I think that both the Commissioner and

1 Congress have left it to the Courts to do that.

2 QUESTION: You don't mind us giving a general
3 definition like that that will whipsaw everything? It
4 is tough for the Tax Commissioner because he doesn't
5 know what he is doing, but we do, so we can just come up
6 with it.

7 (General laughter.)

8 QUESTION: And if you don't like what comes
9 out of here you will be --

10 MR. LAUBER: Then we can go to Congress.

11 QUESTION: -- you will be over across the
12 street right away.

13 MR. LAUBER: Yes, then we get two bites of the
14 apple that way.

15 CHIEF JUSTICE REHNQUIST: Thank you, Mr.
16 Lauber.

17 We will hear now from you, Mr. Baymiller.

18 ORAL ARGUMENT OF CARROLL BAYMILLER, ESQ.,

19 ON BEHALF OF THE RESPONDENT

20 MR. BAYMILLER: Mr. Chief Justice, and may it
21 please the Court, I am a little surprised at the
22 government when they likened the professional gambler to
23 the investor. Anybody that says placing bets at the
24 racetrack is an investment has another think coming
25 because he doesn't have a chance unless he knows what he

1 is doing, unless he studies, unless he works 60 to 80
2 hours a week as Bob Groetzinger does. Otherwise he has
3 no chance. It is not an investment.

4 Now, the difference between an investor and
5 the active trader according to the courts is that the
6 investor is letting his money earn a living for him. He
7 isn't doing the earning. His investment is doing the
8 earning. He buys stocks and bonds and he puts them in
9 his vault and every so often he gets a check for a
10 dividend or for interest, so he is not working.

11 The active trader is working practically every
12 day of his life. Now, a trader who goes to the
13 brokerage office maybe once a week or two or three times
14 a month and buys and sells a few stocks or commodities
15 certainly is not in business because it isn't a frequent
16 activity. That is one of the things that all of the
17 courts have said, that the activity must be frequent and
18 regular.

19 The government says that the active trader is
20 engaged in holding himself out to others as selling
21 goods or services, and they justify it by saying that he
22 is buying and selling stocks and commodities. Now, that
23 is a joke. We all know that the active trader is
24 gambling. He is betting that the price of a stock will
25 go up or go down. When he buys stock he doesn't take

1 delivery --

2 QUESTION: Counsel, that may well be, but it
3 doesn't matter. It seems to me that what the government
4 is saying is, it is all right to gamble, and you can
5 still qualify as being a trade or business, but you have
6 to gamble on the purchase and sale of goods and
7 services. So long as that is what you are gambling on,
8 you are still in the realm of goods and services. You
9 can gamble on the buying and selling of goods and
10 services. That is what the trader does. He gambles
11 that if he sells it a couple of years from now it is
12 going to be -- he is going to get more money than if he
13 sells it today.

14 It isn't the fact of gambling that makes the
15 difference. It is what you are gambling on. The
16 government says, so long as you are gambling on the
17 purchase and sale of something you are still in a trade
18 or business, whereas the person who places a bet on a
19 dog race is not gambling on the purchase and sale of
20 goods.

21 MR. BAYMILLER: But, Your Honor, he is betting
22 with every other patron at the track, the same as the
23 active trader is buying and selling with every other
24 active trader all over the country.

25 QUESTION: That's right, and he is pitting his

1 wits, or if you like his luck perhaps against theirs,
2 but what determines who wins or who loses is ultimately
3 the purchase and sale of goods.

4 MR. BAYMILLER: I say the active trader is not
5 buying and selling goods at all. The active trader
6 today is betting on the rise or fall of the Dow-Jones
7 averages. That is what the active trader does today.
8 He buys futures. He is not buying goods at all. He
9 goes in and he says, I will bet that the Dow-Jones
10 average will go up two points today. If it goes up he
11 wins. If it goes down he loses.

12 QUESTION: That may well be. I mean,
13 ultimately when he buys a stock he is buying a share in
14 a company, but even if you don't look on it that way,
15 and you simply say he is buying a piece of paper, which
16 some people will pay more for today than they may pay
17 for tomorrow. He is still buying or selling something.
18 What is the better in a dog race buying or selling?

19 MR. BAYMILLER: He is buying part of a dog to
20 win.

21 QUESTION: I don't see that. You can say
22 that, but is it true?

23 MR. BAYMILLER: He is making a bet. They say
24 that the casino operator is in business because he is
25 offering bets to the customer. It takes two to gamble,

1 and the man that goes into the bookmaker's office is
2 offering to make a bet with the bookmaker. Now, it is
3 different with the track.

4 The government says in the reply brief that
5 the gambler is making a contract with the track. Now,
6 that just is not true. The track is not making bets.
7 The track is a bookie, is a broker the same as a
8 stockbroker. The track is merely handling the bets of
9 everybody that goes to the window and determining how
10 what is left is to be divided, because the track and the
11 state take about 20 percent first.

12 The Frankfurter test has been used to deny
13 business status only in the gambling cases. They did
14 not use that test to deny business status in Higgins.
15 Justice Frankfurter was on the Higgins Court. Justice
16 Reed concurred with Justice Frankfurter in the DuPont
17 case and wrote the decision in Higgins and never
18 mentioned the Frankfurter test.

19 That test has never been mentioned by this
20 Court since.

21 QUESTION: How about the Courts of Appeals?

22 MR. BAYMILLER: The Courts of Appeals, three
23 circuits, three circuits have used the Frankfurter test
24 which --

25 QUESTION: And the Commissioner has.

1 MR. BAYMILLER: The Commissioner has. Counsel
2 says that the Tax Court has flip-flopped. That is not
3 true. In one case, Gentile, they decided that the
4 full-time gambler was not in business, and every case
5 since that time, even in view of being reversed by the
6 Second and Sixth Circuits, they adhered to the
7 proposition that the full-time gambler is in business
8 and that the Frankfurter test should not be used and
9 should not be adopted by the courts in determining
10 whether a full-time gambler is in business.

11 QUESTION: Well, is that the definition of
12 trade or business that the Tax Court regularly uses in
13 other contexts?

14 MR. BAYMILLER: I don't know that they have.

15 QUESTION: What about -- how about the
16 Investor?

17 MR. BAYMILLER: The investor --

18 QUESTION: What do they say about that?

19 MR. BAYMILLER: They don't say that the
20 Investor -- well, they follow this Court's decision
21 about the Investor.

22 QUESTION: Higgins.

23 MR. BAYMILLER: Higgins. But they do not say
24 that Higgins was not in business because he did not
25 offer to sell goods or services. They did not use that

1 as the test. They said he wasn't in business because he
2 was making investments, which is the same as all of us
3 do, at least to some extent. We all are investors, even
4 if we do nothing more than put a \$5 bill in a savings
5 account every week. That is what this Court held, but
6 they didn't do so because in Higgins the man did not
7 offer to sell goods and services.

8 Now, there are many, many other situations
9 that we have cited in our brief where the courts have
10 held a person to be in business where he didn't offer to
11 sell anything. Take for instance the tennis pro and the
12 golf pro. The government says that he is offering -- he
13 is selling entertainment. That may be true for the
14 McEnroes and the Lendls and the Nicklauses and those
15 people, but I am talking about what may be termed the
16 cannon fodder that go to these tournaments week after
17 week, pay their own expenses, pay an entry fee to get
18 in. They aren't paid anything to come there. Pay an
19 entry fee to get in. And if they win a match they win
20 some money. Now, what have they sold or what are they
21 offering to sell? There can't be any question but what
22 they are in business.

23 We have cases, there are cases in the Circuit
24 Courts, some of them even in the Second and Sixth. Here
25 is a man who decides to be an inventor, and he works on

1 It day in and day out, never gets anything invented,
2 never sells a thing, but the Court said that he was in
3 business. Here is a lawyer who spent --

4 QUESTION: Of course, he has to get income,
5 doesn't he, before he can deduct any of it, so an
6 inventor who never sells a thing isn't going to have any
7 income tax problems.

8 MR. BAYMILLER: He could still be subject to
9 minimum tax.

10 QUESTION: I guess in this case, Mr.
11 Baymiller, the tax is imposed on a gross loss, not
12 income at all.

13 MR. BAYMILLER: That is absolutely true.
14 Absolutely true. Here is a case that the Tax Court
15 recently decided. I don't know whether it is on appeal
16 or not, it hasn't reached the appellate division yet, a
17 fellow by the name of Meridith, he bet \$294,000 in one
18 year and lost \$310,000 That is a \$16,000 loss for the
19 year. And the government assessed him a minimum tax of
20 over \$16,000.

21 So that he had an economic loss for the year
22 of \$32,000 and paid a tremendous amount of tax to the
23 State of Colorado and commissions to the track so that
24 we say that the active gambler, the professional gambler
25 does not get for himself equal protection of the law.

1 The law says that the casino operator can -- is in
2 business. Why isn't the man on the other side of the
3 fence in business?

4 Now, a district judge out in Reno --

5 QUESTION: Mr. Baymiller, how can you -- can
6 we agree with you and stand by Higgins? Let's talk
7 about the investor as opposed to the trader, a person
8 who has extensive investments and really spends his
9 whole day managing those investments full-time. He does
10 nothing but look over this investment and see if this
11 company is indeed still worth investing in, what are its
12 prospects over the next five years, and so forth and so
13 on, full-time occupation.

14 Why isn't that as much a trade or business as
15 gambling if we agree with you that you don't have to be
16 engaged in the business of buying or selling goods or
17 services?

18 MR. BAYMILLER: I think it is. I personally
19 think that the full-time investor is in business, and
20 Congress apparently has thought so, too, because --

21 QUESTION: Well, I agree with you. It seems
22 to me that to agree with you we have to disagree with
23 Higgins.

24 MR. BAYMILLER: Higgins -- but Higgins did lay
25 down the rule that you examine all of the facts and

1 circumstances surrounding a person's activity to decide
2 whether he is in business.

3 QUESTION: If you call that a rule.

4 MR. BAYMILLER: Well, it is the best we have.
5 It is what this Court has said in the past.

6 QUESTION: It is not a rule. It is a throwing
7 up of the hands, isn't it, essentially?

8 MR. BAYMILLER: That probably is true. That
9 probably is true but it is like courts have said many
10 times. We can't define obscenity or pornography but we
11 know it when we see it. And I think that is exactly
12 what the courts should say. We know when a man is in
13 business and when he isn't in business.

14 Now, the full-time gambler is in business --

15 QUESTION: The problem with that is that there
16 are 600 district judges in the country and they may not
17 know when we know when he is in business.

18 (General laughter.)

19 MR. BAYMILLER: I agree with that, but you
20 just can't -- I don't think you can have a very specific
21 limiting definition of when a person is in business.
22 Justice Frankfurter, if he were here today, I am sure
23 that he wouldn't say that a full-time gambler is not in
24 business. At the time he laid down this rule we knew
25 nothing about parimutuel gambling.

1 QUESTION: How long have gambling losses been
2 deductible, or are they, for the purposes of the federal
3 income tax?

4 MR. BAYMILLER: They are deductible only to
5 the extent of winnings, specifically.

6 QUESTION: Well, historically, for a long time
7 they weren't deductible at all, were they?

8 MR. BAYMILLER: I think they have been.

9 QUESTION: Always?

10 MR. BAYMILLER: I think so.

11 QUESTION: But just not against -- just not
12 against other income?

13 MR. BAYMILLER: That's right. That's right.

14 QUESTION: But if a gambler loses every bet he
15 ever places he is not going to have a minimum tax.

16 MR. BAYMILLER: That is true. That is true,
17 because -- well, he --

18 QUESTION: You have got to --

19 MR. BAYMILLER: He will soon be out of
20 business.

21 QUESTION: Yes.

22 QUESTION: Well, so will the inventor who
23 never sells an invention.

24 MR. BAYMILLER: And about -- we had the
25 author. Here is the author, who spends hours and hours

1 gathering material and writing a book. Never gets it
2 published, never sells a thing, never offers to sell a
3 thing, but the courts have held he is in business.

4 QUESTION: But it doesn't do -- I don't see
5 how it does him any good to be in business if he never
6 gets any income.

7 MR. BAYMILLER: He deducted -- he is not the
8 same as gambler where his deductions are limited to his
9 winnings.

10 QUESTION: But what does he deduct it from?

11 MR. BAYMILLER: Well, in the particular case
12 that I refer to the man was a lawyer. And he spent 30
13 hours a week working on a book, taking pictures and
14 gathering materials to publish a book.

15 QUESTION: So he claimed he was in business
16 for writing a book at the same time he was a lawyer?

17 MR. BAYMILLER: Yes, and the Court held he
18 was.

19 QUESTION: Oh, is that right?

20 MR. BAYMILLER: The Court absolutely held he
21 was, even though -- and what did they say? How did they
22 justify it? They said --

23 QUESTION: Which court was this?

24 MR. BAYMILLER: Pardon me?

25 QUESTION: Which court was this, one of the

1 600 Judges?

2 (General laughter.)

3 MR. BAYMILLER: I think I can find it, Your
4 Honor.

5 QUESTION: Well, that is all right. Was it a
6 Court of Appeals?

7 MR. BAYMILLER: Yes, it was a Court of
8 Appeals. I think it was either the Second or Sixth,
9 which didn't follow that same reasoning when they got to
10 the gambling cases.

11 QUESTION: I don't know how they could have
12 done that if they simply took account of the simple rule
13 to take all the facts and circumstances into account.

14 (General laughter.)

15 MR. BAYMILLER: They said that he worked at
16 it, that he hoped to make a profit some day, but not
17 during the tax year in question, but they said he worked
18 30 hours a week gathering materials for a book that he
19 hoped to write. And the Court said, well, he is in
20 business. He went to see some publishers to try to get
21 it published but he never offered, he never had anything
22 to offer for sale.

23 That is the reason I say that Justice
24 Frankfurter's test does just not stand up, and if he
25 were here today I am sure he would not say that the

1 full-time gambler was not in business.

2 QUESTION: (Inaudible.)

3 QUESTION: You have mentioned it ten times.
4 Why waste my listening to hear that over and over
5 again?

6 MR. BAYMILLER: I am sorry, Your Honor.

7 QUESTION: That if he were here he would do
8 this?

9 QUESTION: Mr. Baymiller, this certainly has
10 no bearing on the case, but out of curiosity is Mr.
11 Groetzinger still in full-time gambling?

12 MR. BAYMILLER: Yes, he is. In fact, he is
13 missing the day at what he calls his office this day.

14 If there are no other questions, thank you.

15 CHIEF JUSTICE REHNQUIST: Thank you, Mr.
16 Baymiller.

17 Mr. Lauber, do you have anything more?

18 ORAL ARGUMENT BY ALBERT G. LAUBER, JR., ESQ.,

19 ON BEHALF OF THE PETITIONER - REBUTTAL

20 MR. LAUBER: I might make one point in
21 response to your questions, Mr. Chief Justice.

22 It is possible, the courts have held, for a
23 person to be in more than one trade or business at a
24 time, and what often has happened is, people have tried
25 to use a hobby loss like raising horses or operating a

1 winery on the side as in effect a tax shelter to shelter
2 their professional salary income by using the losses
3 from the second supposed business to deduct against
4 income from the first.

5 QUESTION: Mr. Lauber, it is clear from the
6 code that something can be a profit-making activity but
7 not be a trade or business.

8 MR. LAUBER: Absolutely.

9 QUESTION: It is very clear that you have to
10 draw some distinction between those two.

11 MR. LAUBER: The depreciation --

12 QUESTION: But is it necessary to draw a --
13 wouldn't it be enough to support that distinction simply
14 to say that it has to be a profit-making activity that
15 you engage in regularly as opposed to an isolated piece
16 of profit? Would that suffice to make the code
17 distinctions make sense?

18 MR. LAUBER: It still would not explain
19 Higgins though.

20 QUESTION: No, it wouldn't explain -- well,
21 that's true.

22 MR. LAUBER: He was doing it very regularly.

23 CHIEF JUSTICE REHNQUIST: Thank you, Mr.
24 Lauber.

25 The case is submitted.

1 (Whereupon, at 10:51 o'clock a.m., the case in
2 the above-entitled matter was submitted.)
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#85-1226 - COMMISSIONER OF INTERNAL REVENUE, Petitioner V. ROBERT P. GROETZINGER

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BY Paul A. Richardson

(REPORTER)