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BOARD OF EQUALIZATION

STATE OF CALIFORNIA

In the Matter of the Appeal of:	**HEARING SUMMARY**[2]
GILBERT P. HYATT	**FRANCHISE AND INCOME TAX APPEAL**
	Case No. 446509 (1992)

Year	Proposed Assessment Tax	Fraud Penalty
1992	$5,669,021.00	$4,251,765.75

Representing the Parties:

For Appellant: Edwin P. Antolin, Antolin Law Group
Michael W. Kern, Piercy Bowler Taylor & Kern
Bill Leonard

For Franchise Tax Board: William C. Hilson, Jr., Deputy Chief Counsel
Scott DePeel, Tax Counsel IV
Ann Hodges, Tax Counsel IV

ISSUES: (1) Whether appellant is taxable as a resident of California on all of his income from January 1, 1992 up to and including April 2, 1992.

[1] Appeals Bureau attorneys Grant S. Thompson and Josh Lambert prepared this Hearing Summary.

[2] Appellant also has an appeal pending for the 1991 tax year (Case No. 435770). This appeal (Case No. 446509) and the appeal for 1991 (Case No. 435770) were previously scheduled to be heard on May 23, 2017. The Franchise Tax Board (FTB or respondent) requested a two-month continuance due to a family medical emergency. Appellant did not object but requested that the hearings be held on the calendar commencing on August 29, 2017. In light of the foregoing, the appeals were rescheduled for the August 29, 2017 calendar.

(2) Whether a portion of appellant's income in the year at issue is taxable as California source income.

(3) Whether the FTB has shown that it properly imposed a penalty for fraudulently failing to file a tax return.

(4) Whether appellant has shown a legal basis for the abatement of interest under Revenue and Taxation Code (R&TC) section 19104.[3]

HEARING SUMMARY

Section 40 Appeal

This appeal involves an amount in controversy that is $500,000 or more and thus is covered by R&TC section 40, as explained below in Staff Comments under Issue 4.

ISSUE (1): Whether appellant is taxable as a resident of California on all of his income up to and including April 2, 1992.

Background

Prior to September 26, 1991, appellant was a California resident and domiciliary living on Jennifer Circle in La Palma, California. During 1991 and 1992, appellant earned a substantial amount of income from the licensing of patents.[4]

Appellant asserts that he relocated from Jennifer Circle, in La Palma, California, to Las Vegas, Nevada, on September 26, 1991, and sold his La Palma home to Grace Jeng on October 1, 1991.[5] According to appellant, he continued to reside and work in Las Vegas during the remainder of 1991 and all of 1992, and continues to reside and work in Las Vegas. Appellant contends that he

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[3] Appellant also asserts that the amnesty penalty should not be imposed, but acknowledges that the Board has repeatedly held that it does not have the jurisdiction to review the penalty. (See App. 1992 Concluding Summary (CS), p. 26; App. 1991 Opening Brief (Op. Br.), pp. 86-87.) Pursuant to R&TC section 19777.5, there is no legal basis for the Board to review the post-amnesty penalty at this time, because the penalty has not been assessed and paid and the taxpayer is not appealing from a timely refund claim that raises a computational error. Accordingly, it is not discussed further.

[4] Appellant's 1992 federal Form 1040, Schedule C, listed a business of "INVENTOR/LCD – COMPUTERS AND R&D," with gross income of $84,770,124 and net profit of $84,123,914. Appellant's 1992 federal tax return can be found in appellant's Annex V, at H02603, and can also be accessed through a link in footnote 275 on page 54 of appellant's 1992 Opening Brief.

[5] For appellant's factual contentions regarding residency, see, among other briefing: App. 1991 CS, pp. 1-3, 9-21 (which is incorporated by reference in appellant's 1992 CS), and App. 1992 Reply to FTB CS, pp. 1-10.

initially resided in the Continental Hotel in Las Vegas before moving to the Wagon Trails Apartment building in Las Vegas on October 21, 1991. He contends that he resided in Wagon Trails until he moved into his newly purchased home on Tara Avenue in Las Vegas.

In contrast, the FTB asserts that appellant continued to live and work at his La Palma home through April 2, 1992.[6] The FTB further asserts that appellant operated a California business throughout all of 1992. The FTB argues that appellant continued to own his La Palma home throughout 1992 and that, on June 10, 1993, appellant caused a notary to backdate sale documents to indicate an October 1, 1991 sale of the La Palma home.

As discussed further under Issue (2), regarding sourcing, the FTB asserts that, even if appellant ceased to be a California resident prior to April 2, 1992, some of his 1992 income remains taxable by California on the basis that his income arose from a California source. The FTB further contends that appellant is also taxable on some of his income received after April 2, 1992, on the basis that, in the FTB's view, the income arose from a California source.[7] Appellant disputes both of these contentions.

Appellant did not file a California tax return for the 1992 tax year. On or about June 2, 1993, the FTB initiated an examination of appellant's residency status with regard to appellant's 1991 tax return.[8] On November 2, 1995, the FTB sent an initial audit letter for the 1992 tax year requesting documentation regarding income received during 1992.[9] The parties dispute whether appellant cooperated during the audit and the relevance of internal FTB documents showing the FTB's

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[6] For the FTB's factual contentions, see, among other briefing: FTB 1992 CS, pp. 2-11; FTB July 16, 2014 Br., pp. 2-13.

[7] As noted above, appellant's 1992 federal Form 1040, Schedule C, reported over $84 million of income. It appears to staff that less than $27 million of this income was received prior to April 3, 1992. The FTB's 1992 Notice of Action sustained its Notice of Proposed Assessment, which determined that appellant had California adjusted gross income of $51,595,186.

[8] FTB 1992 Op. Br., fn. 1. Further information about the audit and protest proceedings is provided in the sections entitled "Background" for Issue (2), regarding sourcing, and Issue (4), regarding interest abatement.

[9] App. 1991 Op. Br., p. 73, fn. 377 [progress report noting letter]; FTB Feb. 19, 2013 Br., p. 3-5, Ex. EE, Tab 2 [letter].

consideration of various issues during the audit.[10]

On August 14, 1997, the FTB issued a Notice of Proposed Assessment (NPA) to appellant for the 1992 tax year, assessing additional tax of $5,669,021.00 and a fraudulent failure to file penalty of $4,251,765.75. In the NPA, respondent determined that appellant was a California resident through April 2, 1992, and was therefore taxable on income from all sources through that date. On October 10, 1997, appellant protested the 1992 NPA. (FTB 1991 Op. Br., p. 1, Ex. A, Tab 2 [NPA]; FTB 1992 Op. Br., Ex. H, Tab 25 [protest].)

On October 10, 1997, appellant protested the NPA. (FTB 1992 Op. Br., Ex. H, Tab 25 [protest].) Appellant's protest describes the issue as being whether appellant was a resident through April 2, 1992.

On January 6, 1998, appellant sued the FTB in Nevada claiming the FTB committed tortious acts during the audit, including fraud and the intentional infliction of emotional distress. During the protest period with regard to the FTB's proposed assessment of additional income tax, the FTB and appellant were engaged in this litigation. A trial was not held until 2008. Following the trial, the jury awarded appellant over $388 million in compensatory and punitive damages, plus costs and interest. However, this award amount was substantially reduced by the Nevada Supreme Court, and the United States Supreme Court subsequently capped the FTB's liability.[11] The parties dispute the relevance of that litigation to the issues on appeal.

On December 27, 1999, appellant obtained a protective order from the Nevada court allowing appellant to designate information as confidential information which could not be shared

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[10] See, *e.g.*, App. 1992 Op. Br., p. 6; App. 1991 Op. Br., pp. 84-85; App. 1991 Reply Br., pp. 74 (fn. 454), 87-89; FTB 1991 Reply Br., p. 56; FTB 1992 Reply Br., pp. 28-29.

[11] The jury ruled for appellant for causes of action including fraud. In 2003, the United States Supreme Court held that the FTB could be sued in Nevada courts. (*FTB v. Hyatt* (2003) 538 U.S. 488.) In 2014, the Nevada Supreme Court partially reversed the trial court, sustaining only a $1 million award for fraud and an award for the intentional infliction of emotional distress that it remanded for a new trial. (*FTB v. Hyatt* (Nev. 2014) 335 P.3d 125.) In 2016, the United States Supreme Court found, in its second opinion in the litigation, that damages must be limited to the statutory liability limit for Nevada agencies ($50,000), and remanded the case back to the Nevada Supreme Court. (*FTB v. Hyatt* (2016) 136 S.Ct. 1277.) The parties are currently disputing in the Nevada Supreme Court how the United States Supreme Court's 2016 ruling should be applied.

outside the FTB's litigation team except in certain circumstances.[12]

Protest hearings were held on September 27, 2000 and October 4, 2000.[13] Between September 2000 and November 2007, the parties were involved in a number of disputes regarding the scope and application of the Nevada protective order and various subpoenas issued by the FTB. It appears that, during some portion of this time, the FTB had difficulty organizing its audit and protest records, and, due to the Nevada litigation, deferred action on the processing of the protest for a period. As discussed under Issue (4), regarding interest abatement, the parties dispute which factors contributed to the length of the protest period.[14]

On November 1, 2007, respondent issued a Determination Letter for both the 1991 and 1992 tax years in which respondent stated it would affirm the NPA for 1992 as well as the NPA for 1991. The Determination Letter also advanced "an additional and alternative basis for the assessments that the patent licensing income received by the taxpayer is, in whole or in large part, California source income taxable by California."[15]

On December 26, 2007, the FTB issued a Notice of Action (NOA) for the 1992 tax year, affirming the NPA. The NOA references the November 1, 2007 Determination Letter. The NOA finds appellant to be a resident of California through April 2, 1992 and, as such, taxable on his income from all sources through that date. In addition, the NOA states that, as a result of facts developed at protest, the assessment was "further and alternatively sustained" on the basis that appellant's income was generated from intellectual property that had a business situs in California for the entire taxable year and

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[12] FTB 1992 Op. Br., p. 50 & Ex. H, Tab 27. The order had been prepared on December 3, 1999 by a "Discovery Commissioner."

[13] The FTB argues that both hearings covered both years while appellant contends that the 1991 protest hearing was held on October 4, 2000 and the 1992 protest hearing was held on September 27, 2000. (See FTB 1992 Reply Br., p. 81; App. 1991 Op. Br., p. 88; App. 1992 Op. Br., p. 68; FTB Feb. 19, 2013 Br., p. 15, Ex. DD, Tab 11 [October 4, 2000 letter from the FTB noting that protest hearings were held on September 27, 2000, and October 4, 2000, and setting forth issues].)

[14] Additional information regarding actions during the protest is provided under the section entitled "Background" for Issue (4).

[15] FTB 1991 Op. Br., p. 1, Ex. A, Tab 4, FTB 28751 [Determination Letter; see sourcing arguments on pages 30 to 48 of the letter and beginning on page 123 of the PDF].

was derived from sources within California. Appellant then filed this timely appeal.[16] (FTB Op. Br., p. 1, Ex. A, Tab 4 (FTB 28811 [NOA]).)

Appellant's Contentions – Issue (1) - Residency

Appellant incorporates by reference his introduction to his 1991 Concluding Summary. There, appellant contends that he "moved to Las Vegas on September 26, 1991, and sold his only California house five days later on October 1, 1991." He further contends that, after staying "at a Las Vegas hotel for a short time," he moved to a Las Vegas apartment on October 21, 1991 and into his 5,400 square foot Las Vegas Tara home on April 3, 1992. He argues that, during the 190-day disputed period between September 26, 1991 and April 2, 1992, he "had 125 full days in Nevada as a resident, zero full days in California as a resident, and 37 days partly in Nevada as a resident and partly in California for temporary or transitory purposes." Appellant argues that he has produced "overwhelming ***eyewitness and documentary*** evidence" supporting his appeal including "more than 220 declarations and affidavits from more than 150 witnesses . . . . [appellant's emphasis]"[17] (App. 1991 CS, p. 1; App. 1992 CS, p. 1.)[18]

Appellant contends that the FTB failed to correct a $24 million error that was reflected in the 1992 NPA.[19] Appellant argues that the FTB cannot now change "the basis for the $24 million assessment because the FTB was required to set forth the reasons for any proposed deficiency assessment and the computation thereof in the NPA." Appellant further argues that the NPA must be based on a determination that is not "arbitrary or without foundation," and that the FTB has not carried

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[16] This appeal was deferred many times at the request of one or both parties and in order to allow evidence to be presented and to obtain additional briefing. During the appeal, appellant and the FTB were involved in litigation in New York courts in which appellant sought to prevent the FTB from introducing evidence in this appeal (sometimes referred to as "Philips documents"). Once the New York litigation resolved, additional briefing was obtained with regard to the Philips documents that had been the subject of the New York litigation as well as evidence provided by appellant with his final brief prior to additional briefing.

[17] Appellant provides a comprehensive list of affidavits and declarations in HYATT_LINKED_BRIEFS/08_Affidavits_re_Supp_Briefs/000_Updated_Index_of_Affidavits.pdf.

[18] As noted previously, "CS" refers to Concluding Summary. Each party's concluding summary contains citations to exhibits and portions of its other briefs supporting its arguments. For brevity, footnotes are generally omitted when quoting from a party's contentions.

[19] Appellant argues that the FTB overstated by approximately $24 million the amount of income he received between January 1, 1992 and April 3, 1992. This issue is discussed under Issue (2), regarding sourcing.

its "initial burden [] to show why its assessment[s] [are] reasonable and rational[,]" quoting the *Appeals of Wesley et al.*, 2005-SBE-02, decided November 15, 2005 (*Wesley*). (App. 1992 CS, pp. 1-4.)

In support, appellant argues that the assessments were imposed in bad faith (as allegedly evidenced by "FTB's $24 million error") and because of "FTB's gross misconduct and extreme bad faith treatment of Mr. Hyatt, FTB's calendar and attachment A-R [being] made in bad faith (more than 2,000 false statements) and [because] there was no 1992 audit." Appellant further contends that the assessments were imposed "in bad faith by a rogue auditor and supported by other FTB personnel who were intent on issuing assessments against Mr. Hyatt and imposing enormous fraud penalties to coerce an unjustified settlement." Appellant argues that "[i]t has been conclusively determined that FTB committed fraud, intentionally inflicted emotional distress, and acted in bad faith in its audits and protests of Mr. Hyatt[,]" citing the Nevada jury verdict and the September 18, 2014 opinion of the Supreme Court of Nevada.[20] (App. 1992 CS, pp. 2-5.)

In rebuttal to the FTB's argument, appellant argues that: "The U.S. Supreme Court did not overturn the decision of the Nevada courts that FTB had committed fraud against Mr. Hyatt. It only limited the award of damages." Appellant contends that the U.S. Supreme Court "left in place" the determination of the Nevada courts "that FTB conducted a fraudulent audit and intentionally inflicted emotional distress on Mr. Hyatt." Appellant further argues that "[t]he fraud committed by FTB renders the FTB's determinations of its 1991 and 1992 NPA's and NOA's unreliable; the conclusive findings of fraud and intentional infliction of emotional distress should be given great weight." (App. 1992 Reply to FTB CS Reply, p. 23.)

Appellant incorporates by reference his introduction for the 1991 appeal. There, appellant argues that he prepared for his move to Las Vegas for over nine months and that he permanently moved to Las Vegas on September 26, 1991. He contends that he initially "stayed in a Las Vegas hotel for several weeks," that he sold his California house on October 1, 1991, and that "he leased a Las Vegas Apartment for six months" before purchasing a Las Vegas house where he still resides. (App. 1992 CS, p. 1; 1991 CS, p. 1; see also App. 1992 Reply to FTB, pp. 1-2.)

[20] The referenced opinion of the Nevada Supreme Court is *FTB v. Hyatt* (Nev. 2014) 335 P.3d 125. This opinion was vacated and remanded by the United States Supreme Court in *FTB v. Hyatt* (2016) 136 S.Ct. 1277.

Appellant contends that, in December of 1990, "shortly after his decision to move, [he] engaged Mahr Leonard [Mahr Leonard Management Company or MLMC] to license his patents but Mahr Leonard failed to get any licenses." Appellant states that, in July of 1991, he gave U.S. Philips Corporation (Philips) a license that provided the exclusive authority to sublicense his patents and that, as Philips told him it could take years of litigation to get the patents licensed, Philips provided a "minimum annual license fee for up to 10 years . . . ." Appellant asserts that his "finances were very uncertain at the time he moved to Las Vegas and sold his California house." (App. 1991 CS, p. 1)

Appellant argues that "[w]ell into October 1991, the Mahr Leonard negotiations with Fujitsu [Fujitsu Ltd.] and Oki [Oki Electric Industry Co., Ltd.] were continuing and changes were being made to the patent agreements in mid-October 1991." Appellant contends that Philips then "unexpectedly started to license his patents[,]" which permitted him to focus more on "research and development and building his life in Las Vegas." (App. 1991 CS, p. 1.)

In support, appellant cites to his affidavits and the affidavits[21] of many others, and argues that "[t]here are many eyewitnesses to the above events . . . ." With regard to the number of eyewitnesses supporting his view of the chronology, appellant argues, among other things, that 26 witnesses testified about his "decision to move to Las Vegas," 32 witnesses testified about his "preparations to move," 72 witnesses testified about his move away "in 1991," and "22 Jennifer Circle neighbors testified about [him] moving away in 1991." (App. 1991 CS, p. 2, pp. 2.)

Appellant contends that, during the disputed period from September 26, 1991 to April 2, 1992, he "had 125 full days in Nevada as a resident, zero full days in California as a resident, and 37 days partly in Nevada as a resident and partly in California for temporary or transitory purposes." Appellant further argues that he "has produced overwhelming ***eyewitness and documentary*** evidence in support of his appeals," stating the he "filed more than 220 declarations and affidavits from 150 witnesses from many walks of life in support of his position . . . and he filed thousands of pages of very relevant contemporaneous documentary evidence "CDE"). [appellant's emphasis]" (App. 1991 CS, pp. 2-3, 5-9.)

[21] Generally, unlike an affidavit, a declaration is not witnessed and sealed. Here, staff generally refers to affidavits and declarations interchangeably.

Appellant provides an overhead photograph of the Jennifer Circle cul de sac showing the location and names of residents at the time he moved, noting that there are only 16 houses on Jennifer Circle. Appellant argues that "***twenty-two* Jennifer Circle neighbors** testified about [him] moving away in 1991 and ***23-witnesses testified*** that they did not ever again see [him] at Jennifer Circle after he moved away in 1991. [appellant's emphasis]" Appellant argues that the testimony from his former neighbors "alone defeats the FTB's residency case and sourcing case." Appellant contends that both cases rest "upon the same premise - that [he] lived, worked and operated a California licensing business at the Jennifer Circle house." Appellant further contends that the "FTB's claim that it can infer from an address on a correspondence that [he] was physically present at the Jennifer Circle house must be rejected when eyewitnesses with personal knowledge establish that [he] moved away from the Jennifer Circle house and did not return." (App. 1991 CS, p. 5.)

Appellant argues that the testimony of his neighbors "is just one part of his overwhelming documentary and testimonial evidence," pointing to, among other things, 72 witnesses who testified about his "move away in 1991[,]" and 15 eyewitnesses who testified "that an Asian woman (or Ms. Jeng) moved into the Jennifer Circle after [he] moved away in 1991." Appellant further contends that "dozens" of witnesses testified regarding his "presence in Las Vegas, visiting him and telephoning him at his Las Vegas apartment, worshiping with him at their Las Vegas synagogue, house hunting with him in Las Vegas, and much more." Appellant argues, among other things, that 37 witnesses testified "about [his] stay at a Las Vegas hotel when he first moved to Las Vegas in 1991 . . . ." (App. 1991 CS, p. 6.)

Appellant contends that he sold his Jennifer Circle house on October 1, 1991, and that, "[a]fter signing and delivering a Grant Deed to the purchaser [Ms. Jeng] and after receiving a down payment from the purchaser, he moved his remaining belongings out of the Jennifer Circle house and returned to Las Vegas[,]" citing his affidavits. Appellant further contends that "[t]he lead FTB auditor determined "[he] sold [his] La Palma house on 10/1/91[,]" quoting from the FTB's 1991 narrative Report. Appellant argues that the FTB has never alleged or shown that he "had any abode outside of Las Vegas thereafter other than the Jennifer Circle house." Appellant states that 16 witnesses testified about the sale of his house in October 1991 and "two former Orange County Assessors testified that the

documentation for the sale of [his] California house satisfied the requirements of the Orange County Assessor's Office for [the] sale of a house in 1991." (App. 1991 CS, p. 6.)

Appellant argues that his closest connections were with Nevada after his move, arguing that, after initially staying at a hotel, he leased an apartment, purchased a home, opened Las Vegas financial accounts, joined a Las Vegas synagogue, obtained a Nevada driver's license and voter registration, used a Las Vegas insurance agent and other Nevada professionals, and "did hundreds of other things that established his permanent residence in Las Vegas." Appellant further argues that he sent "numerous written changes of address[,]" "informed more than 100 persons of his move[,]" and provided his Las Vegas contact information to friends, family, and associates. Appellant argues that "even FTB agrees" he became a resident and only disputes when he moved, as the FTB's 1992 Notice of Proposed Assessment finds he became a Nevada resident on April 3, 1992. (App. 1991 CS, p. 7.)

Appellant argues that the FTB has "no credible evidence" that he lived and worked at the Jennifer Circle house after September 26, 1991 and instead "resorts to fabricating fantastic stories, mischaracterizing . . . documents, relying on an address on correspondence as 'proof' of [his] location, calling [his] witnesses perjurers, drawing illogical inferences, and disregarding overwhelming evidence produced by [him]." Appellant states that a Nevada jury found that the FTB engaged in "gross misconduct and fraud" and that the "FTB's bad faith continues in these appeals." (App. 1991 CS, p. 7.)

As an example, appellant argues that the FTB's auditor made a $24 million income overstatement error. Appellant further argues that, although he produced significant evidence in 1997 that established the error, the FTB assessed tax on the basis of the error, assessed a fraud penalty, and "attempted to extort a settlement from [him] with it." Appellant contends that the FTB refused to correct the error or consider his evidence until "your Board required FTB to provide its evidence in an additional briefing." Appellant states that ". . . thanks to your Board, FTB finally admitted to its $24 million error." However, appellant argues that the FTB, acting in bad faith, refuses to reduce the assessment of tax, penalty and interest to correct the error. (App. 1991 CS, pp. 7, 9; App. 1992 CS, pp. 1-3.)

Appellant contends that the FTB "fails to carry its "initial burden" of establishing "reasonable and rational" assessments on the grounds that the assessments were imposed in bad faith,

the FTB made "more than 2,000 false statements" on appeal, and that "there was no 1992 audit." Appellant argues that he has carried his burden of proof but the FTB "has failed to carry any of its burdens of proof." Appellant contends that the assessments were imposed "by a rogue auditor and supported by other FTB personnel who were intent on issuing assessments . . . and imposing enormous fraud penalties to coerce an unjustified settlement." Appellant further argues that "[i]t has been conclusively determined that FTB committed fraud, intentionally inflicted emotional distress, and acted in bad faith . . . [,]" citing *FTB v. Hyatt* (Nev. 2014) 335 P.3d 125[22] and the Nevada jury's verdict. (App. 1992 CS, pp. 2-4.)

Appellant argues that the *Bragg* factors "overwhelmingly establish [his] Nevada residency during the disputed period and thereafter."[23] Appellant incorporates his arguments on pages 10 to 15 of his 1991 Concluding Summary with regard to this issue. (App. 1992 CS, p. 1.)

Appellant argues that, after he moved to Las Vegas on September 26, 1991, his closest connections and "all his personal and professional activities" were located in Las Vegas. Appellant contends that he intended to, and did, move to Las Vegas, as evidenced by, among other things, his sale of his California residence "five days after he moved," his purchase of a home in Las Vegas on April 3, 1992, his move of his telephone, his filing of his tax returns from Las Vegas, his financial accounts and transactions, his attendance at worship services in Las Vegas, registration of his 1997 Toyota car, obtaining a Nevada driver's license and registering to vote in Las Vegas. (App. 1991 CS, pp. 10, 13.)

With regard to his ownership of real property, appellant argues that he did not own "any residential real property in California after he sold his California house on October 1, 1991." He further argues that he shopped for a Las Vegas home in person, as evidenced by his affidavit and the affidavits of Mr. McGuire and Mr. Shoemaker, and observes that he closed on his Las Vegas Tara home on April 3, 1992. (App. 1991 CS, pp. 10, 11)

Appellant observes that the FTB's audit file indicates that he "sold his Jennifer Circle

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[22] This decision was vacated and remanded by the United States Supreme Court in *FTB v. Hyatt* (2016) 136 S. Ct. 1277. The United States Supreme Court found that Nevada must provide the FTB with the same damages cap available to Nevada agencies. Appellant and the FTB appear to disagree on the scope and impact of this United States Supreme Court decision and are currently engaged in litigation in Nevada with regard to the decision.

[23] The *Bragg* factors refers to the factors set forth in the *Appeal of Stephen D. Bragg*, 2003-SBE-002, May 28, 2003 (*Bragg*).

house on October 1, 1991." Appellant argues that, on October 1, 1991, he "signed and delivered" the grant deed, and that, on June 10, 1993, "he properly notarized the gran[t] deed with an acknowledgment of his prior signature." Appellant argues that he had "no California abode" after the sale and that two former Orange County assessors "confirmed the validity of the sale . . . ." Appellant further argues that he "took a note from the purchaser of his former La Palma house, he received a $15,000 down payment, monthly payments for six years, and a balloon payment to pay off the loan in full in six years." (App. 1991 CS, p. 11.)

Appellant contends that he "did not live with his family, his children were grown, he was divorced, he terminated his California homeowner's property tax exemption, he was not employed, he did not have business interests, he did not use professional licenses, and he had no investment real property." Appellant argues that his "only telephone was located in his Las Vegas apartment and his account was with the Centel telephone company in Las Vegas." He further argues that "all of [his] calls originated from Las Vegas[,]" and states that "many eyewitnesses testified about the telephone in [his] Las Vegas apartment and telephone calls with [him]." (App. 1991 CS, pp. 11-12.)

Appellant contends that he "spent all of his time during the disputed period in Nevada except for short temporary and transitory trips to other states." He argues that he was only in California for temporary and transitory purposes, such as a hospital stay for surgery, and that such visits "do not count as California residency days." He contends that, after October 1, 1991, he "stayed at motels, not at his former La Palma house, when he visited California." (App. 1991 CS, pp. 12-13.)

Appellant states that his calendar "is supported by eyewitness and documentary evidence[,]" and notes that the calendar states that he "had 166 full and part days in Las Vegas as a resident out of 190 days in the disputed period." Appellant asserts that he has shown that he was partly in Nevada and partly in California for a temporary purpose on 46 days. (App. 1991 CS, pp. 12-13.)

Appellant argues that he had only Nevada bank accounts and Nevada situs investment accounts during the disputed period. He states that he opened a Las Vegas checking account on October 25, 1991, "he opened several other Las Vegas bank accounts shortly thereafter, and he opened many investment accounts using his Nevada address shortly thereafter." He argues that the FTB "disregards or misrepresents" the documentary evidence of his financial accounts. Appellant contends

that his checking and credit card transactions originated in Las Vegas, that he provided changes of address to Las Vegas for his national credit account companies, that "[h]e signed more than 80 checks in Las Vegas with his Las Vegas address printed thereon and with his banks' Las Vegas address printed thereon during the disputed period[,]" and that "virtually all of these transactions took place in Las Vegas." (App 1991 CS, pp. 13-14.)

Appellant argues that his "social, religious, and professional memberships and activities during the disputed period and thereafter were and are in Las Vegas." He states that he joined and regularly attended services at a Las Vegas synagogue, that he joined the Las Vegas Personal Computer Users Group, and that he "was associated with the Office of the Nevada Governor, Nevada Development Authority and Clark County School District." He asserts that he used "more than 100 non-California professionals" and that the FTB disregards his documentary evidence that he used non-California professionals and "falsely alleges that Philips' California professionals are [his] professionals." (App. 1991 CS, pp. 14 - 15.)

Appellant argues that he registered his cars in Nevada, he had a Nevada driver's license, he registered to vote in Nevada, and he did vote in Nevada. Appellant further argues that he used a Las Vegas insurance agent to insure his cars and home. (App. 1991 CS, p. 14.)

Appellant contends that the FTB's findings at protest "do not detract from the conclusion that [he] became a Nevada resident in September 1991." In this connection, he refers back to arguments made in his opening brief for 1991 with regard to the sale of his La Palma house, the termination of his homeowners' exemption, his residence at the Continental Hotel, his residence at Wagon Trails Apartments through April 3, 1992, his registration to vote, and his "extensive house hunting in Las Vegas during the disputed period." (App. 1991 CS, p. 15)

Appellant asserts that the Philips documents "significantly support [his] residency and sourcing appeals." Appellant argues that he provided 15 tables of excerpts from more than 5,000 pages of Philips documents, which were disregarded by the FTB.[24] (App. 1992 CS, p. 12.)

Appellant argues that he has provided "more than 220" affidavits from "more than 150

[24] Appellant refers to section 1.7.1 of his 1991 second additional brief filed on September 28, 2016.

witnesses that all support [his] facts." He further argues that the FTB's attacks on the eyewitness testimony are made in bad faith. He contends that the FTB's "inferences and speculation" cannot discredit the testimony of more than 100 witnesses and that "[n]o inference about [his] location can be drawn from ***mis-addressed documents*** . . . . [appellant's emphasis]" He asserts that the FTB disregards documentary evidence supporting the testimony and that the witnesses are "reinforced by consistent testimony from dozens of other eyewitnesses: 72-witnesses testified about [him] moving away in 1991." Appellant further asserts that the FTB took "numerous depositions of the Hyatt witnesses and Philips witnesses but the FTB did not brief the deposition testimony because the testimony supported [appellant]." (App. 1992 CS, pp. 13–14.)

Appellant contends that the FTB's arguments regarding his witnesses are baseless and unsupported. Appellant further contends that who "penned" the sworn statements does not determine credibility and that the FTB's allegations that the affidavits are "scripted" is "meaningless." Appellant argues that refreshing the memory of a witness is "entirely proper." (App. 1992 CS, p. 14.)

Appellant further contends that neither "[e]xtra-statutory compensation" paid to witnesses nor his relationships with the witnesses undermine the credibility of the affidavits or declarations. Appellant argues that affidavits are an approved form of providing evidence. (App. 1992 CS, p. 14.)

Appellant contends that his witnesses testified that FTB private investigators provided false testimony. Appellant therefore contends that the declarations of the FTB's investigators should be afforded no weight. (App. 1992 CS, p. 15.)

Appellant argues that he has provided "overwhelming" testimony from "dozens of eyewitnesses" identifying false statement by the FTB. Appellant points to "Testimonial Responses" summarized in tables attached to appellant's briefs. (App. 1992 CS, p. 15.)

Appellant argues that the FTB's false statements are "further illustrated with its treatment of Thomas McGuire, [his] Las Vegas real estate agent and [his] house hunting activities with Mr. McGuire in Las Vegas." Appellant asserts that the FTB "fabricates a ridiculous story that handwritten notes that Mr. Hyatt made while walking through houses (relative to purchasing) . . .were made during a telephone conversation." Appellant contends that the FTB falsely argues that Grace Jeng

did the house-hunting and that appellant did not meet Mr. McGuire until before the April 1992 closing. Appellant argues that the FTB's statements are contradicted by appellant's notes and by statements provided by Mr. McGuire, appellant, and Mary Stratton, the owner of the Tara house which appellant purchased on April 3, 1992. Citing to the affidavit of Mr. McGuire, appellant argues that the FTB sent a proposed declaration to Mr. McGuire which had false statements and which Mr. McGuire refused to sign. (App. 1992 CS, pp. 15-16.)

Appellant contends that the FTB "continues it[s] bad faith attacks on Mr. Hyatt by questioning the true and correct statements in his affidavits[,]" with "inferences and speculation." Appellant argues that, contrary to the FTB's contentions, he "was not present at his former La Palma house between October 1, 1991, when he sold the house, and late 1992 . . . ." He contends that 72 witnesses testified that he moved away in 1991. (App. 1992 CS, p. 16.)

Appellant further contends that, contrary to the FTB's contentions, (1) he "did not send faxes from his former La Palma house after October 1, 1991[,]" (2) he did not attend the meetings at Mr. Roth's office on September 24, 1991, (3) he returned to Las Vegas from the East Coast on October 21, 1991, not October 23, 1991, (4) he "did not negotiate with Hitachi [Hitachi Ltd.] and did not negotiate any patent agreements during the disputed period . . ." and that doing so would have violated the July 1991 Philips Agreement, (5) he resided in the Continental Hotel from September 26, 1991, and then in the Wagon Trails Apartments from October 21, 1991, citing witness testimony, (6) he "did not have an expectation that potential licensees would sign license agreements[,]" (7) he had "no discretion" over the distribution of license payments, (8) he was in Las Vegas on November 7, 1991, "when he wrote the drafts to distribute the Fujitsu license payment to Philips and Mahr Leonard[,]" citing witness testimony, (8) he did not send a "markup" draft letter to Philips on November 22, 1991, (9) he was in Las Vegas on February 27, 1992, not California, and a "misaddressed FedEx delivery does not mean he was in California[,]" and he drove from Las Vegas to California on March 30, 1992, returning on March 31, 1992. (App. 1992 CS, pp. 17-18.)

Appellant further contends that the testimony of his "eyewitnesses" is true and correct. Among other things, appellant contends that Mr. Roth accurately testified that: (1) Mr. Hyatt did not meet with Mr. McHenry and others at Mr. Roth's office on September 24, 1991; (2) "that he met with

Mr. Hyatt on March 31, 1992, but Mr. Hyatt did not negotiate with Hitachi on March 31, 1992 or May 26, 1992[;]" (3) Mr. Hyatt "did not attend the dinner show with Hitachi on January 28, 1992; and (4) ". . . the licensing correspondence was primarily between Philips, Mahr Leonard, PSB&C and the licensees and Mr. Hyatt was outside the mainstream of the licensing correspondence, as evidenced by correspondence and affidavits. Appellant also contends that he did not negotiate with Hitachi "at any time." (App. 1992 CS, p. 18.)

Appellant argues that his family members "accurately testified that [he] was in Las Vegas on October 21, 1991." Appellant also argues that the FTB "seeks to deceive your Board by implying Mr. Rudestam testified about photographs from a non-existing portrait photoshoot on October 6, 1991, when he did not." Appellant contends that the FTB also "seeks to deceive your Board by implying Mr. McHenry testified about 'all' photographs when he only denied involvement with specific photographs." Appellant further contends that "XCS witnesses," Ms. Maldonado and Mr. Tran,[25] and Dr. Peloquin,[26] "testified accurately and no false testimony was solicited." (App. 1992 CS, pp. 18–19.)

Appellant argues that the FTB's physical presence arguments in its RRBs are "without merit." Appellant argues that, in his 1992 ASB (referring to his supplemental brief filed on July 25, 2012), he "responded to FTB's incorrect statements regarding (a) his relevancy argument and his knowledge of future income[,]" (b) "'direct evidence'," XCS copy invoices, his 1977 Toyota, (c) "credit card charges that are not made by him[,]" (d) medical visits, (e) credit card charges and his checking account, (f) "his statement that FTB provides no evidence to support its assertion[,]" and other topics. (App. 1992 CS, p. 19.)

FTB's Contentions – Issue (1) - Residency[27]

The FTB contends that appellant was a "long-time California domiciliary" and was a resident "for the entire disputed period of September 26, 1991 through April 2, 1992." The FTB further

[25] XCS, Inc. (XCS) was a company that serviced copiers. Ms. Maldonado and Mr. Tran were employees of XCS.

[26] Dr. Peloquin provided an affidavit denying that a document provided by the FTB was a "verified statement" of the dates appellant visited his office.

[27] Respondent states that its legal arguments are extensively discussed at pages 68 through 77 of its opening brief for the 1991 tax year and at pages 19 through 23 of its 2007 Determination Letter and states that it is incorporating such arguments.

contends that "[o]bjective, contemporaneous documents confirm Mr. Hyatt remained in California throughout the disputed period and that he did not move to Nevada, with an intent to remain in Nevada . . . until escrow closed on his Tara home on April 3, 1992." The FTB emphasizes that "contemporaneous documentation demonstrates that Mr. Hyatt exercised a continuous personal and business presence in California, including access to his Jennifer Circle residence, throughout the contested period." In support, the FTB cites Mr. Hyatt's "ongoing use of the Jennifer Circle street address, Cerritos Post Office Box, and Jennifer Circle fax machine . . ." and meetings with "his California patent attorney," prospective licensees in California, and other professionals. The FTB also points to "speeches and interviews[,]" use of California banking services, and "meals at several Orange County restaurants." (FTB 1992 CS, p. 2.)

The FTB argues that appellant's California presence is "underscored by Mr. Hyatt concealing his whereabouts from September 26, 1991 to October 14, 1991 for five years, revealing it only after documents which could have confirmed or contradicted his claim of a long-term stay at the Continental Hotel . . . had been destroyed; and obtaining a back-dated notary acknowledgment . . . to try to create the appearance of a sale of his Jennifer Circle home to a friend on October 1, 1991 . . . ." The FTB also argues that appellant leased a "one bedroom unit in a low-income Las Vegas apartment complex which prohibited conducting a trade or business . . . [,]" that appellant failed to file a required "change of ownership statement" for the sale of his home and that appellant used flights that originated and terminated in Los Angeles. (FTB 1992 CS, p. 3.)

The FTB argues that Mr. Hyatt's declarations are "an attempt to deflect attention from the absence of contemporaneous documentation" and that many of the declarations "are from people who could have, and should have, been disclosed many years earlier, who support to speak about events which occurred during 1991 and/or 1992, providing accounts which cannot be independently verified." The FTB contends that, while Mr. Hyatt filed approximately 10 declarations or affidavits during protest, he has submitted approximately 160 declarations following protest, many of which are more than 15 years old and are "contradicted by contemporaneous documentation." The FTB further contends that many declarants admit that the declarations were drafted by appellant's attorney and many refused, on the instruction of lawyers, to answer questions during depositions. (FTB 1992 CS, p. 3.)

The FTB argues that the lawyers issuing instructions include Gregory Roth, "Mr. Hyatt's long-term patent lawyer, and Roger McCaffrey, Mr. Hyatt's probate estate lawyer." The FTB contends that the declarations lack credibility because of "the belated nature of the disclosure of the identities of [the] declarants/affiants[,]" "the lack of contemporaneous, objective verification[,]" and "the coincidence of the declarants/affiants being represented by Mr. Hyatt's attorneys . . . ." (FTB 1992 CS, pp. 2-4.)

The FTB provides the following analysis of the *Bragg* factors for evaluating residency.

Residential Real Property. Referring to its 1991 Concluding Summary, the FTB disputes appellant's contention that he sold the La Palma California house in October 1991. The FTB contends that appellant provided a non-recorded copy of a grant deed for the alleged sale to his "friend and colleague" Grace Jeng on October 1, 1991. However, the FTB argues, the grant deed for the sale "contains a fraudulent notary acknowledgement which is back-dated by almost two years." The FTB further contends that the testimony and journal of the notary, Darlene Beer, show that Mr. Hyatt appeared before her on June 10, 1993, not October 1, 1991. The FTB further contends that on February 10, 1992, appellant was "provided an opportunity to disclose the alleged unrecorded sale . . . but did not do so." The FTB argues that appellant continued to claim record ownership of the home and that the alleged sale had other "abnormalities" such as the fact that it was not recorded in 1991 or 1992, the lack of a contract for sale, the lack of a "change of ownership statement" and the fact that a "Ticor 'Property Profile' report . . . indicates Grace Jeng acquired the La Palma house on August 12, 1993 . . . ." (FTB 1992 CS, p. 4; FTB CS 1991 CS, pp. 11-12.)

The FTB states that appellant's "lease and purported occupancy of a Wagon Trails Apartment unit allegedly commencing in late October 1991" has been discussed in its 1991 Concluding Summary. The FTB argues that Ms. Jeng handled the leasing arrangements and sent the rental agreement to appellant at Jennifer Circle for his signature. The FTB further argues that Clara Kopp, who lived and worked at the apartments, did not remember seeing appellant there, although she did recognize Ms. Jeng. The FTB asserts that a "purported 'move out' letter was not produced until seven years after respondent commenced Mr. Hyatt's audit . . . [,]" that Mr. Hyatt's rental file was "missing," and that the typical form used to terminate leases had not been produced. The FTB argues that

Mr. Hyatt's tax counsel requested a copy of "move-out documentation Ms. Jeng signed" but that, "[b]ecause Mr. Hyatt never gave permission . . . to release copies of his rental file, respondent had no copies to give him." (FTB 1992 CS, p. 5; FTB 1991 CS, p. 13.)

The FTB acknowledges that appellant purchased residential real property in Las Vegas on April 3, 1992. However, the FTB argues that "Mr. Hyatt engineered the purchase of that property from and while he was in California[,]" with offers and counter-offers faxed to appellant at Jennifer Circle. The FTB argues that Mr. Hyatt "ultimately" assigned his contract rights to purchase the property to "a trust standing in the name of his accountant," with instructions faxed to Nevada by Mr. Hyatt. The FTB further argues that appellant's absence from Nevada is evidenced by his realtor sending a fax to appellant at Jennifer Circle and inquiring where he should pick up his client, with Mr. Hyatt then renting a car in Las Vegas. The FTB asserts that ". . . it is not until shortly after April 2, 1992, that any evidence of Mr. Hyatt purchasing common household items in Las Vegas appears." (FTB 1992 CS, pp. 5–6.)

Physical Presence. The FTB states that "Mr. Hyatt's continued and pervasive physical presence in California . . . has been extensively discussed" in prior briefing, including its 1991 Concluding Summary and its Attachment A (Revised). The FTB argues that "[f]rom the beginning of January 1992 to April 2, 1992, Mr. Hyatt spent 79.5 days in California, 4.5 days in Nevada, and 9 days in other states."[28] (FTB 1992 CS, p. 6.)

Telephone Service. The FTB argues that appellant has failed to produce telephone records for 1991 or 1992. The FTB argues that, "[i]n light of the continued use of the Jennifer Circle telephone and telefax lines during 1992 . . . , the negative inference therefrom is well deserved . . . [,]" citing to the FTB's 1991 Concluding Summary at pages 15 – 16. The FTB contends that appellant continued to use phone and fax numbers associated with his Jennifer Circle home "long after his alleged departure from California." The FTB states that it requested telephone records but appellant asserted that he routinely destroyed them, did not have them and could not obtain them. However, the FTB contends, appellant selectively provided phone bills to obtain the reimbursement of estate expenses. Citing the *Appeals of Appeal of James C. Coleman Psychological Corporation, et al.*, 85-SBE-028,

[28] Respondent states that support for its day-to-day analysis can be found at pages 81-126 of its Attachment A (Revised), pages 9-12 of its 1991 additional brief dated July 16, 2014, and pages 8-12 of [its] Attachment F.

decided April 9, 1985, the FTB contends that the failure to provide the information gives rise to the presumption that the evidence would be unfavorable. The FTB further argues that appellant has not shown that he activated telephone service in his Wagon Trails apartment before November 1991. (FTB 1992 CS, pp. 6–7; FTB 1991 CS, pp. 14–15.)

Bank, Safety Deposit, and Savings Accounts.[29]

The FTB argues that appellant received "bank statements from California Federal Bank, Lakewood and Cerritos branches, at his Cerritos Post Office box for nearly all of the disputed period." The FTB contends that appellant appeared before a California notary on February 11, 1992 with regard to a "safe dep box," and that he obtained notary services in California on February 11, 1992 and used a California Bank in connection with his transfer of funds for the Tara house purchase on March 24, 1992. The FTB argues that appellant's responses to its inquiries regarding checking account information were "quite lacking." The FTB states that "as many as 340 checks" for 1991 and a similar number for 1992 were not provided, and further contends that appellant had an undisclosed checking account. (FTB 1992 CS, p. 7; FTB 1991 CS, pp. 16-18.)

Vehicle Registration. The FTB asserts that, while Nevada residents must obtain a Nevada license and register vehicles within 45 days, appellant's 1977 Toyota Celica was not registered until May 6, 1992. (FTB 1992 CS, p. 7.)

Voter Registration, Voting Participation History, and Driver's License. The FTB argues that, in July 1994, appellant falsely represented in his voter registration that he resided at Sandpiper Lane, Las Vegas when he had never resided at the address. The FTB states that this property had been owned by Mr. Kern, Hyatt's Nevada accountant, and that Mr. Kern acquired a new home in June 1994 and sold his Sandpiper Lane property in October 1994. The FTB argues that appellant was a registered voter in California from September 12, 1990 to September 18, 1992. The FTB states that, in Nevada, you may vote if you reside in the state and county for 30 days and in the precinct for 10 days. The FTB argues that, on November 27, 1991, the day after purchasing two airline tickets, appellant obtained a Nevada driver's license, but then returned to California by November 29, 1991. (FTB 1992 CS, pp. 7-8;

[29] Throughout its Concluding Summary, the FTB incorporates by reference its discussion in the prior briefing and in its 1991 Concluding Summary.

FTB 1991 CS, p. 18.)

Professional Services. The FTB states that appellant obtained medical services on February 3, 1992 from Dr. Melvin Shapiro in Encino, and had surgery in California in mid-February of 1992. The FTB argues that appellant "did not consult any medical or dental provider(s) in Nevada" during the 1992 disputed period. (FTB 1992 CS, p. 9.)

The FTB argues that appellant consulted Gerald Block, CPA, on February 3, 1992 and February 25, 1992. The FTB further argues that on Mr. Hyatt's first visit he asked how to establish Nevada residency and that on his second visit Mr. Block advised that Mr. Hyatt needed to dispose of his California residence and establish a Nevada address. (FTB 1992 CS, p. 9.)

The FTB contends that appellant "obtained professional and/or support services from numerous individuals in California with respect to the *Hyatt v. Boone* interference who 'were paid by Philips on behalf of Mr. Hyatt.'"[30] The FTB lists over 15 individuals who the FTB contends were professionals "utilized by Mr. Hyatt for these matters in 1991 and 1992 . . . [,]" including Barry Lee, Gregory L. Roth, Caroline Cosgrove, and Grace Jeng. (FTB 1991 CS, p. 19.)

Business Interests. The FTB argues that appellant did not have a license to work from his Wagon Trails apartment or his Tara home and that he did not apply for a business license in Las Vegas until December 10, 1992. The FTB further argues that appellant "did not meet or consult with his Nevada accountant until mid-March 1992 and did not lease or rent any commercial office space in Nevada during the disputed period." (FTB 1992 CS, pp. 9-10.)

Professional Licenses. The FTB states that Mr. Hyatt's address of record for his engineering license was a P.O. Box in Cerritos, California. (FTB 1992 CS, p. 10.)

Memberships in Social, Religious, and Professional Organizations. The FTB argues that appellant has failed "to prove any Nevada affiliations other than membership in Congregation Ner Tamid during the disputed period . . . ." In its 1991 Concluding Summary, the FTB argues that it received no response to letters it sent to a Las Vegas computer group and a temple that appellant stated he was associated with. The FTB asserts that Rabbi Akelsrad of Congregation Ner Tamid "later told an

[30] The FTB cites in support an excerpt from a 2001 letter from appellant's attorneys stating that "[s]ome of Mr. Hyatt's non-California professionals were paid by Philips on behalf of Mr. Hyatt."

investigator that he did not remember the name of Gilbert Peter Hyatt." The FTB further asserts that, contrary to appellant's assertions, the Nevada Development Authority had no record of appellant's membership, the Nevada Governor's office had no record of contact with appellant, and a Nevada school tutoring program could not confirm that appellant volunteered. (FTB 1992 CS, p. 10; FTB 1991 CS, p. 21.)

Homeowner's Exemption. The FTB contends that no "change of ownership statement" was filed from 1990 to 1996 or within 45 days of the purported sale to Ms. Jeng. The FTB argues that "[a]s late as April 8, 1993, Mr. Hyatt continued to claim record ownership of the Jennifer Circle home[,]" and further argues that the Jennifer Circle home was not reassessed in 1991 or 1992, but was reassessed "as of June 1993." (FTB 1992 CS, p. 11.)

Tax Returns. The FTB notes that appellant did not file a California personal income tax return for 1992. (FTB 1992 CS, p. 11.)

Miscellaneous. The FTB states that "Mr. Hyatt's continued receipt of important business correspondence and licensing documents at his Cerritos Post Office Box and Jennifer Circle home has been extensively discussed" in prior briefing and its 1991 Concluding Summary. In its 1991 Concluding Summary, the FTB argues that appellant maintained "at least two P.O. boxes in California" and that appellant's Jennifer Circle home "is only 1.3 miles from the Cerritos Post Office." (FTB 1992 CS, p. 11; FTB 1991 CS, p. 22.)

The FTB also disputes appellant's argument that the Nevada litigation is relevant to the appeals. The FTB notes that, on April 19, 2016, the United States Supreme Court issued its opinion in *FTB v. Hyatt* (2016) 136 S.Ct. 1277. The FTB argues that the U.S. Supreme Court "vacated the Nevada Supreme Court's judgment as unconstitutionally discriminatory against a sister state" and found that, quoting the U.S. Supreme Court opinion, the Nevada court "ignored" immunity rules and "applied a special rule of law that evinces a 'policy of hostility' toward California . . . ." The FTB argues that appellant is relying on the "now-vacated Nevada Supreme Court opinion" in *FTB v. Hyatt* (Nev. 2014) 335 P.3d 125 "for its putative confirmation of certain facts and asserting that the underlying 'verdict controls how (seemingly) conflicting evidence from trial must be interpreted.'" The FTB argues that, because the opinion has been vacated, appellant cannot rely upon it, and further argues that appellant's

"own counsel" stated that the Nevada litigation is not relevant to the California tax dispute. The FTB also states that "[e]ven the Nevada District Court repeatedly instructed the empaneled jury that it was not to decide the residency or tax issues pending in California." (FTB 1992 CS, pp. 24 -25.)

Applicable Law – Issue (1) – Residency

Burden of Proof

It is well established that a presumption of correctness attends respondent's determinations of fact, including determinations of residency, and that an appellant has the burden of proving such determinations erroneous.[31] This presumption is a rebuttable one and will support a finding only in the absence of sufficient evidence to the contrary. (*Appeal of George H. and Sky Williams, et al., supra*.) The failure of a party to introduce evidence which is within the party's control gives rises to the presumption that, if provided, it would be unfavorable. (*Appeal of Don A. Cookston*, 83-SBE-048, Jan. 3, 1983.)

In *Todd v. McColgan* (1949) 89 Cal.App.2d 509, 514, Todd challenged the determination of the Franchise Tax Commissioner (the predecessor of the FTB) of how to determine the rate of return attributable to separate property of a husband that was invested as capital. The court stated that when the FTB's allocation of income "is found to be reasonable and rational the burden of showing error in [the taxing agency's] computation or application is on the taxpayer."

In *Wesley*, *supra*, 2005-SBE-002, Wesley filed a return with zeros for income and all other financial information, and the FTB estimated his income based on reporting by third parties. Citing *Todd v. McColgan*, *supra*, 89 Cal.App.2d 509, and other cases, the Board stated that the FTB's initial burden was to show that its assessment was "reasonable and rational." However, the Board stated, once the FTB introduced some evidence linking the taxpayer with the unreported income, the FTB's assessment is presumed correct and appellants have the burden of proving it to be wrong.

Residency

R&TC section 17041, subdivision (a)(1), provides, in pertinent part, that a tax shall be

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[31] Cal. Code Regs., tit. 18, § 5541, subd. (a); *Bragg, supra,* 2003-SBE-002[citing the *Appeal of Joe and Gloria Morgan*, 85-SBE-078, July 30, 1985]; *Appeal of Raymond H. and Margaret R. Berner*, 2001-SBE-006-A, Aug. 1, 2002; *Appeal of George H. and Sky Williams, et al.*, 82-SBE-018, Jan. 5, 1982.

imposed for each taxable year upon the entire taxable income of every resident of California who is not a part-year resident. R&TC section 17014, subdivision (a), provides that the term "resident" includes: (1) every individual who is in California for other than a temporary or transitory purpose; and (2) every individual domiciled in California who is outside California for a temporary or transitory purpose. Thus, if an individual is domiciled in California, he or she remains a resident until he or she leaves for other than temporary or transitory purposes. (Cal. Code Regs., tit. 18, § 17014; see also Rev. & Tax. Code, § 17014.)

The term "domicile" refers to one's permanent home, the place to which he or she intends to return after an absence. (*Appeal of Anthony V. and Beverly Zupanovich*, 76-SBE-002, Jan. 6, 1976 (*Zupanovich*) (citing *Whittell v. Franchise Tax Board* (1964) 231 Cal.App.2d 278, 284).) An individual can have but one domicile at any one time. (Cal. Code Regs., tit. 18, section 17014, subd. (c).) To change a domicile, a taxpayer must move to a new residence and intend to remain there permanently or indefinitely. (*Bragg, supra*, 2003-SBE-002; Cal. Code Regs., tit. 18, § 17014, subd. (c).) The party asserting a change in domicile bears the burden of proving such change. (*Appeal of Terance and Brenda Harrison*, 85-SBE-059, June 25, 1985.) If there is doubt on the question of domicile after the presentation of the facts and circumstances, the domicile must be found to have not changed. (*Appeal of Stephen D. Bragg, supra*. 2003-SBE-002.)

Regulation 17014, subdivision (b), states that "[w]hether or not the purpose for which an individual is in this State will be considered temporary or transitory in character will depend to a large extent upon the facts and circumstances of each particular case." The regulation further states:

> It can be stated generally, however, that if an individual is simply passing through this State on his way to another state or country, or is here for a brief rest or vacation, or to complete a particular transaction, or perform a particular contract, or fulfill a particular engagement, which will require his presence in this State for but a short period, he is in this State for temporary or transitory purposes, and will not be a resident by virtue of his presence here.
>
> If, however, an individual is in this State . . . for business purposes which will require a long or indefinite period to accomplish, or is employed in a position that may last permanently or indefinitely, or has retired from business and moved to California with no definite intention of leaving shortly thereafter, he is in the State for other than temporary or transitory purposes, and accordingly, is a resident taxable upon his entire net income . .

Regulation 17014, subdivision (b), also states that the underlying theory of R&TC sections 17014 to 17016 is that the state with which a person has "the closest connection during the taxable year" is the state of his residency. The contacts a taxpayer maintains in California and other states are important factors to be considered in determining California residency. (*Appeal of Anthony V. and Beverly Zupanovich*, *supra*, 76-SBE-002.) Although the actual or potential duration of the taxpayer's presence in, or absence from, California is very significant in determining his residency, it is also important in each case to examine the connections with California and compare them with those the taxpayer maintains in other places. (Id.)

In *Bragg*, the Board listed nonexclusive factors to aid it in determining with which state an individual has the closest connection. The Board in *Bragg* cautioned that these nonexclusive factors ". . . serve merely as a guide in our determination of residency," and ". . . [t]he weight given to any particular factor depends upon the totality of the circumstances" unique to each taxpayer for each tax year. The *Bragg* factors can be organized into three categories, as provided below. As will be seen below, many factors overlap one another.

Registrations and Filings

This group of factors includes items which the taxpayer has filed with the state or other agency. The factors in this category include:

- The state wherein the taxpayer claims the homeowner's property tax exemption on a residence;
- The address the taxpayer uses on his tax returns, both federal and state, and the state of residence claimed by the taxpayer on such returns;
- The state wherein the taxpayer registers his automobiles;
- The state wherein the taxpayer maintains a driver's license; and
- The state wherein the taxpayer maintains voter registration and the taxpayer's voting participation history.

Personal and Professional Associations

The factors in this group help show where the taxpayer had his day-to-day contacts in both his occupational life as well as in his personal life. These factors include:

- The state wherein the taxpayer's children attend school;
- The location of the taxpayer's bank and savings accounts;
- The state wherein the taxpayer maintains memberships in social, religious, and professional organizations;

- The state wherein the taxpayer obtains professional services, such as doctors, dentists, accountants, and attorneys;
- The state wherein the taxpayer is employed;

- The state wherein the taxpayer maintains or owns business interests;
- The state wherein the taxpayer holds a professional license or licenses;
- The state wherein the taxpayer owns investment real property; and
- Affidavits from third parties attesting to the taxpayer's presence and community involvement.

Physical Presence and Property

This group includes the factors showing where the taxpayer was physically located during the time in question, and where his tangible and real property were located. These factors include:

- The location of all of the taxpayer's residential real property, and the approximate sizes and values of each of the residences (i.e., indicating the nature of the use of the property) including whether the taxpayer sold or rented any residential property around the time of the alleged residency change;
- The state wherein the taxpayer's spouse and children reside;
- The taxpayer's telephone records (i.e., the origination point of taxpayer's telephone calls);
- The number of days the taxpayer spends in California versus the number of days the taxpayer spends in other states, and the general purpose of such days (i.e., vacation, business, etc.); and
- The origination point of the taxpayer's checking account transactions and credit card transactions.

In the case of individuals who claim to be nonresidents by virtue of being outside of the state for other than temporary or transitory purposes, affidavits of friends and business associates as to the reasons for being outside of the state should be submitted. (Cal. Code Regs., tit. 18, § 17014, subd. (d)(1).) Residency determinations depend on the facts and circumstances of each case, however, affidavits and declarations from an individual's friends, family, and business associates stating that the individual was in California for temporary or transitory purposes ordinarily are sufficient to overcome a presumption of residency. (*Ibid.*) In the *Appeal of William G. and Susan G. Crozier*, 92-SBE-005, decided April 23, 1992, the Board found, on the record before it, that contemporaneous records from the years at issue held more weight than statements Mr. Crozier made several years after the tax year at issue. In the *Appeal of Raymond H. and Margaret R. Berner*, 2001-SBE-006-A, decided August 1,

2002, the Board found, on the record before it, that the Berners had established through affidavits and declarations from friends, family, and professionals that they were domiciled in and resided in Nevada.

STAFF COMMENTS – ISSUE (1) – RESIDENCY

Residency determinations require a weighing of the particular facts and circumstances of each case. (*Bragg, supra*, 2003-SBE-002 [citing additional authorities].) Here, the record includes an extraordinary amount of both testimonial and documentary evidence, and very little agreement between the parties about the relevant facts.

In order to assess the evidence, the Board may find it helpful to compare the FTB's Attachment A (Revised) (daily analysis) and Attachment F (business activity analysis) with appellant's rebuttal to these documents, which are available in appellant's folder "02_FTB_Briefs_and_Hyatt_Rebuttals" in PDF files beginning with "06B" and "06C." Staff also notes that appellant has provided chronological statements of appellant's view of the facts in the folder "04_Chronological_Stmts_of_Facts" and affidavits and tables with contemporaneous documentary evidence in "HYATT_LINKED_BRIEFS/10_Hyatt_Contemporaneous_Doc_Evid." The FTB has provided a PDF with respect to documents from each day in the disputed period in FTB_LINKED_BRIEFS/07_FTB Calendar Support Documents.

A key factual determination for the Board will be whether or to what extent the Board finds the affidavits submitted by appellant to be reliable.[32] In making this determination, the Board may wish to consider, among any other factors it deems relevant, the passage of time between events described in the affidavit and the making of the affidavit, any business or social relationships of the affiant with appellant, and whether or to that extent the affidavit is corroborated, or contradicted, by other evidence. "The weight of the evidence does not necessarily depend on the number of witnesses called by a party, and the credibility to be given a witness is a matter for the Tax Court [i.e., the finder of fact]." (*Merchants Nat. Bank of Topeka v. Comm'r* (9th Cir. 1977) 554 F.2d 412, 416.)

To illustrate the evidence and arguments presented, staff summarizes the evidence and

[32] Appellant provides a comprehensive list of affidavits and declarations which can be found, among other locations, in HYATT_LINKED_BRIEFS/08_Affidavits_re_Supp_Briefs/000_Updated_Index_of_Affidavits.pdf. In addition, appellant provides linked tables showing affidavits and declarations regarding various topics in "05_Testimonial_Topics." The FTB provides its analyses of affidavits in FTB_LINKED_BRIEFS/02_FTB_Attachments (attachments B, D & E).

arguments presented with regard to various dates at issue. It appears to staff that, for many dates, the FTB has provided some evidence which, on its face, appears to suggest a California presence at a particular time, such as an attorney billing record. However, appellant seeks to explain the evidence by arguing, among other things, that the evidence does not in fact demonstrate a California presence, that any California presence was temporary, that the evidence is contradicted by affidavits, that the evidence is unreliable, and/or that the evidence is contradicted by documents listing a California address. It will be up to the judgment of the Board, as the finder of fact, to weigh the totality of the evidence and assess the credibility of the arguments.

Saturday, January 25, 1992. Before the Philips documents were introduced into the appeal record, appellant argued that he was in Nevada on January 25, 1992, that "it is established that [he] was not present in California on this day[,]" and that he "was certainly physically present" in Las Vegas during this weekend. Citing Mr. Howard's testimony, he further stated that he and Mr. Howard met at an indoor swap meet, visited a property and took a drive. Citing the testimony of the Strattons, he stated he also visited them in their Las Vegas home. Citing the testimony of Mr. Shoemaker, appellant stated that he also met Mr. Shoemaker at appellant's apartment to review the seller's counter-offer on the Palm Canyon property.[33]

The FTB then obtained and provided a billing record from Philips which indicates that appellant met Mr. Roth, a Los Angeles attorney, for one hour.[34]

Appellant now contends that, on this day, he traveled to California where he had the one hour meeting with Mr. Roth, and then, on the same day, returned to Las Vegas,[35] where he engaged in multiple activities including visiting the Strattons at their Las Vegas Tara house and meeting with Mr. Shoemaker at his Las Vegas apartment, and then spent the night in his Las Vegas apartment.[36]

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[33] HYATT_LINKED_BRIEFS/02_FTB_Briefs_and_Hyatt_Rebuttals/06_Rebuttals_to_FTB_Attach_A_1992_Stmts, pp. 64-66.

[34] FTB_LINKED_BRIEFS/02_FTB_Attachments/04_Attachment A (Revised) (with Philips Documents).pdf, p. 91.

[35] Staff estimates it would take approximately 8 to 9 hours to drive from Las Vegas to the Los Angeles area and back, depending on traffic and whether any stops are made during the trip (e.g., for gas).

[36] HYATT_LINKED_BRIEFS/02_Briefs_and_Hyatt_Rebuttals/06B6_Jan_92_Rebutt_Att_A_F.pdf, pp. 306-310.

Tuesday, January 28, 1992. The FTB contends that appellant attended a hearing in California, had dinner at Medieval Times with Hitachi representatives in California, and then spent the night in California. However, appellant contends that on this day he traveled from Nevada to California, attended the hearing, and then traveled back to Nevada. Appellant argues that he did not attend the dinner at Medieval Times.

Appellant stated in an affidavit regarding a California estate hearing, which was scheduled for 10 a.m. on January 28, 1992, that he executed the affidavit in La Palma, California. On January 7, 1992, appellant, who was the personal representative of the estate, submitted a declaration for reimbursement of expenses, including anticipated expenses. Under "Anticipated Future Services," appellant listed, for January 28, 1992, meeting with his attorneys for an hour to prepare for a hearing in the estate matter, a two-hour court hearing, and .75 hours (i.e., 45 minutes) of travel time. The FTB contends that this would mean that, if appellant drove from Las Vegas that morning to attend the hearing, appellant would have needed to leave Las Vegas no later than 4:30 a.m. The FTB contends that appellant attended a dinner with Mr. Roth, Hitachi representatives, and George Mahr and David Leonard of MLMC at the Medieval Times in Buena Park, California. Roth records and bills indicate that four hours were spent by Roth at a "MEETING" "REGARDING HITACHI." The Philips documents include an expense claim for the dinner at Medieval Times for this date, reporting "[i]n attendance: Hitoshi (Jin) Akaki, Mr. Ogino, Gil Hyatt, and G. Roth."[37]

As noted above, appellant contends that he did not spend the night in California and that he made a round trip from Las Vegas to California and back to Las Vegas on this date. Appellant provides an affidavit from Mr. McCaffrey stating that appellant told him that day that appellant "had driven from his apartment in Las Vegas and that he would immediately return to Las Vegas after the hearing." Mr. McCaffrey also states in an affidavit that he billed only .75 hours of travel time in order to avoid a disagreement with appellant's siblings by seeking a larger amount. Appellant contends that he did not attend the dinner at Medieval Times and that he returned to Las Vegas and had dinner with

[37] FTB_LINKED_BRIEFS/02_FTB_Attachments/04_Attachment A (Revised) (with Philips Documents).pdf, p. 93 [providing links to Exhibit M, Tab 31, appellant's affidavit in the estate matter; Exhibit J, Tab 22, appellant's invoice for services to the estate; FTB_Philips 6596 (expense voucher for meal) and Exhibit M, Tab 32, a January 15, 1992 letter from Roth to Hitachi, copying appellant and others, and inviting "everyone" to dinner at Medieval Times].

Mr. Howard and provides an affidavit from Mr. Howard in support. With regard to the dinner expense claim listing appellant's name, Mr. Roth's 2016 affidavit states, at paragraph 15, that the charge was incurred because he purchased a ticket for Mr. Hyatt "in case he chose to attend," but that in fact Mr. Hyatt did not in fact attend the dinner.[38]

Monday, February 3, 1992. Appellant initially argued that he was in Nevada on February 3, 1992, and that "it is established that [he] was not present in California on this day."[39] Appellant stated that he made a counter offer on a house in Las Vegas on this day, pointing to an offer and acceptance agreement dated February 3, 1992, and further stated that he signed a W-9 form which identified his address as a P.O. Box in Las Vegas.[40] He also provided a March 21, 2012 affidavit of Mr. McGuire stating that he met with appellant in his Las Vegas office on February 3, 1992. The FTB pointed to a doctor's note which stated that appellant "was seen on 2/3/92" but appellant argued that the note "is not credible evidence." The FTB pointed to a declaration of Gerald S. Block, a CPA, who stated that appellant visited him this day and informed him that "he had come into some money like $10 million and was about to earn another $30 million. [Appellant] asked [him] how to establish residency in Nevada." Appellant stated that the statement was incorrect and that he had "no recollection of meeting with Mr. Block in his office on this specific date." An article from the Los Angeles Times dated February 4, 1992, states that appellant was interviewed on "Monday [February 3, 1992]" and refers to him as a "La Palma inventor." Appellant stated that it is not possible to determine his location based on the article.

The FTB then obtained and provided a billing record from Philips which indicates that Mr. Roth and appellant met for 15 minutes.[41]

Appellant now contends that he traveled to California to meet Mr. Roth and "apparently met with Mr. Block" in California. He states that, prior to traveling to California and while in Las Vegas

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[38] HYATT_LINKED_BRIEFS/02_Briefs_and_Hyatt_Rebuttals/06B6_Jan_92_Rebutt_Att_A_F.pdf, pp. 367–398.

[39] HYATT_LINKED_BRIEFS/02_Briefs_and_Hyatt_Rebuttals/06_Rebuttals_to_FTB_Attach_A_1992_Stmts, pp. 90– 03.

[40] HYATT_LINKED_BRIEFS/04_Chronological_Stmts_of_Facts/03_Superseded_1992_Chron_re_Opening_Brief. pdf, pp. 5–6; FTB_Philips_0006582-6585.

[41] FTB_LINKED_BRIEFS/02_FTB_Attachments/04_Attachment A (Revised) (with Philips Documents).pdf, pp. 96–97.

on February 3, 1992, he met with Mr. McGuire and made the counter-offer on the house, signed the W-9 form which showed his address as a P.O. Box in Las Vegas, and signed the investment advisory agreement. He states that he returned to Las Vegas on the next day.[42]

Friday, February 7 to Sunday, February 9, 1992. In summary, appellant contends that on Thursday, February 6, 1992, he traveled from Las Vegas to San Francisco, and then traveled back to Las Vegas to spend the night in Las Vegas.[43] Appellant argues that, on Friday, February 7, 1992, he traveled from Las Vegas to the La Palma area to visit a notary, and then traveled back to Las Vegas where he spent the weekend. The FTB argues that appellant was in San Francisco and then, rather than returning to Las Vegas, traveled from San Francisco to southern California where he was on February 7, and then remained in southern California until Sunday, February 9.

Appellant offers in support a 2012 affidavit of Mr. Hammer, who says he called appellant in Las Vegas on Thursday, February 6, and a 2010 affidavit from Mr. Lee, who states that appellant had no expenses for the San Francisco trip because Mr. Lee covered most of his expenses including air fare. Mr. Lee also states that he called appellant in Las Vegas on Wednesday, February 5 and Friday, February 7, 1992.

According to Darlene Beer's notary book, appellant appeared before her on Friday, February 7, 1992 at Capitol/Landmark Bank, La Palma, California.[44] As noted above, appellant states that, after returning to Las Vegas on the evening of Thursday, February 6, 1992, he traveled from Las Vegas to La Palma and visited the notary office, and then traveled back from La Palma to Las Vegas on the same day. Appellant contends that, after returning to Las Vegas, he received a call from Barry Lee and attended Temple Beth Am with Mr. Howard, and provides affidavits in support.[45]

On Saturday, February 8, 1992, at approximately 8:51 a.m., appellant faxed a letter and a February 8, 1992 article from the Orange County Register to Philips with the Cerritos P.O. Box number

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[42] HYATT_LINKED_BRIEFS/02_Briefs_and_Hyatt_Rebuttals/06B7_Feb_92_Rebutt_Att_A_F.pdf, pp. 36–64; Sept 6, 2016 Supp. Disputed Period CDE Aff. of Gilbert P. Hyatt, par. 207, p. 95.

[43] HYATT_LINKED_BRIEFS/02_Briefs_and_Hyatt_Rebuttals/06B7_Feb_92_Rebutt_Att_A_F.pdf, pp 94–126.

[44] FTB_LINKED_BRIEFS/02_FTB_Attachments/04_Attachment A (Revised) (with Philips Documents).pdf, p. 99.

[45] HYATT_LINKED_BRIEFS/02_Briefs_and_Hyatt_Rebuttals/06B7_Feb_92_Rebutt_Att_A_F.pdf, pp. 103–113.

and Jennifer Circle phone and fax number at the top of the letter.[46] The FTB contends that appellant sent this fax on the morning of Saturday, February 8, 1992, from California after spending Friday night in California on February 7, 1992. Appellant contends that he sent the fax to Philips from Las Vegas, and that Ms. Cosgrove, who "monitored certain newspapers for Mr. Hyatt[,] presumably sent him" the Orange County Register article. The FTB also contends that appellant received a fax at Jennifer Circle on this day from the real estate agent Tom McGuire. Appellant argues that he received the fax in Las Vegas.[47] Appellant also states that he signed a check while in Las Vegas and the check had his Las Vegas address on it and it was drawn from a Las Vegas checking account.

Tuesday, February 25, 1992. The FTB contends that appellant was in California on this date and met California CPA Gerald Block and also met with Mr. Roth. However, appellant contends that he spend the entire day in Nevada.

In a 2009 declaration, California CPA Gerald Block stated that appellant visited him on this date and he "advised [appellant] that to become a nonresident of California [appellant] needed to dispose of his residence in California and had to establish a Nevada address." (FTB Ex. M, Tab 39.) An invoice from Roth billed 1.25 hours for a "MEETING WITH GIL HYATT REGARDING LICENSING." (FTB_Philips_0002431-2432.) The Philips documents also include an undated fax cover sheet sent from appellant, listing the Cerritos P.O. Box and Jennifer Circle phone and fax, which the FTB states was the cover sheet for an amendment to a Fujitsu agreement that appellant sent on February 25. As support, the FTB points to a fax that Philips sent to appellant on the next day, which is addressed to appellant in La Palma, which states that appellant faxed the amendment on February 25, 1992.[48] The FTB states that the cover sheet and the Philips response were included in the same sequence of Philips documents.

Appellant states that he spent this full day in Las Vegas and did not travel to California. Appellant states that he received phone calls in his Las Vegas apartment from Will Connell, Caroline

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[46] FTB_LINKED_BRIEFS/02_FTB_Attachments/04_Attachment A (Revised) (with Philips Documents).pdf, p. 100.

[47] HYATT_LINKED_BRIEFS/02_Briefs_and_Hyatt_Rebuttals/06B7_Feb_92_Rebutt_Att_A_F.pdf, pp. 114–123.

[48] FTB_LINKED_BRIEFS/07_FTB_Calendar Support Documents/19920225_February 25, 1992.pdf, p. 7 [fax cover sheet from appellant], p. 1 [Philips February 26, 1992 fax letter].

Cosgrove, his son Daniel Hyatt, and Ms. Stratton and provides affidavits in support. Appellant contends that Mr. Block and the Roth invoice are both in error, and that the invoice should have indicated a telephone call. An affidavit from Mr. Roth states that he did not meet with appellant on this date and that the invoice should have indicated a phone call. Appellant contends that he did not meet with Mr. Block on this day and that he only met with Mr. Block once, on February 3, 1992. Appellant contends that he was already well established in his Nevada residence and did not need to know how to establish a residency in Nevada. Appellant contends that the fax sent to Philips was sent from Las Vegas and that, while he used the legacy Cerritos P.O. Box as a return address, this does not mean that he sent the fax from a Cerritos P.O. Box or any other place in California. Appellant asserts that overwhelming eyewitness testimony and documentary evidence establishes that his fax machine, computer, and active files were moved to Las Vegas.[49]

Tuesday, March 3, 1992. The FTB contends that appellant was in California on this day and met with Roth. An invoice from California attorney Gregory Roth indicates billing of "1.00" hour for a meeting with appellant regarding "status of documents."[50] However, appellant contends that he was in Las Vegas for this full day and that he did not travel to California. Appellant contends that he received a telephone call from Mr. Shoemaker, met with Ms. Frank at her Las Vegas Office, and signed two checks while in Las Vegas, and provides affidavits in support. Appellant contends that the Roth invoice should have indicated a teleconference, providing an affidavit from Mr. Roth in support, and argues that FedEx has his signature release on file.[51] Appellant has also stated that, on this date, he went to lunch at Sizzler with Mr. Howard and took a drive with Mr. Howard.[52]

Additionally, on this date, Algy Tamoshunas of Philips directed a FedEx package to appellant addressed to the Jennifer Circle property. The next day, March 4, 1992, the package was ///

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[49] HYATT_LINKED_BRIEFS/02_Briefs_and_Hyatt_Rebuttals/06B7_Feb_92_Rebutt_Att_A_F.pdf, pp. 263-278.

[50] FTB_LINKED_BRIEFS/02_FTB_Attachments/04_Attachment A (Revised) (with Philips Documents). pdf, p. 108.

[51] HYATT_LINKED_BRIEFS/02_Briefs_and_Hyatt_Rebuttals/06B8_Mar_92_Rebutt_Att_A_F.pdf, pp. 25-47.

[52] HYATT_LINKED_BRIEFS/02_Briefs_and_Hyatt_Rebuttals/06_Rebuttals_to_FTB_Attach_A_1992_Stmts, pp. 169-172.

delivered at 9:12 a.m. and a FedEx record states "SIGNED: G. HYATT."[53] Appellant contends that there was a clerical error by Philips in sending the package to that address and that he did not sign for it but rather that his signature release was on file with FedEx.[54]

ISSUE (2): Whether a portion of appellant's income is taxable as California source income.

Background

As discussed further below, appellant's 1992 federal tax return shows total adjusted gross income from all sources of $84,973,440. The FTB is not seeking to tax all this income. The FTB's 1992 NOA seeks to tax $51,595,186 of this income.[55] This $51,595,186 mount was based on the FTB's determination of how much income appellant recognized between January 1 and April 3, 1992.[56] It appears that the FTB made this determination based on a table provided by appellant's representative on February 7, 1996.[57] This table is set forth further below in this Background section. The FTB now agrees that appellant received less than $27 million between January 1 and April 3, 1992. In the FTB's February 19, 2013 brief (page 28, footnote 152), the FTB argues that $26,981,988 would be taxable on a residency basis if the Board sustains the FTB's determination that appellant remained a resident through April 2, 1992. However, the FTB asserts that the remaining amount, up to the full $51,595,186 amount reflected in its NPA, is taxable on the basis of source. Similarly, the FTB asserts that the full $51,595,186 amount reflected in its NPA is taxable on the basis of source, even if the Board determines appellant was not a California resident during 1992. The parties dispute both what income is taxable on a residency basis alone and whether any of appellant's income is taxable on the basis of its source.

It appears to staff that the licensing payments received by appellant in 1992 consist of the

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[53] FTB_LINKED_BRIEFS/02_FTB_Attachments/04_Attachment A (Revised) (with Philips Documents).pdf, p. 108.

[54] HYATT_LINKED_BRIEFS/02_Briefs_and_Hyatt_Rebuttals/06B8_Mar_92_Rebutt_Att_A_F.pdf, pp. 25–47.

[55] FTB 1991 Op. Br., Ex. A, Tab 2, p. 59 of PDF [FTB's calculation of tax attached to its NPA]. The NOA affirmed the NPA.

[56] The NPA found that appellant was a resident through April 2, 1992 and stated that "[a]s such, you are taxable on income from all sources through that date."

[57] FTB Feb. 19, 2013 Br., p. 5, Ex. EE, Tab 12 [February 7, 1996 letter]. Staff asked the FTB how it determined the amount of income received by appellant, and the FTB replied, at page 12, footnote 45, of its February 19, 2013 brief, that it relied on ". . . Mr. Hyatt's February 7, 1996 letter and FTB audit's responsive schedules[,]" citing its NPA and schedules attached to an April 1, 1996 letter from the FTB (which schedules are located at FTB Ex. EE, Tab 18.1, at p. 150 of the PDF).

payments listed below.[58] Staff lists below its understanding of the dates on which the payments are asserted to have been received and/or taxable.

January 14-15, 1992 - $23,866,465.55 of Income. This amount is related to payments by Sharp Corporation (Sharp), Sony, and NEC. Appellant refers to this income as being from Philips while the FTB refers to this income as being from Sharp, Sony, and NEC. (See App. First Add'l Br. April 10, 2013, pp. 3–4; FTB Feb. 19, 2013 Br., p. 29.) In a February 7, 1996 letter, appellant's representative provided the FTB with a table showing deposits received from Philips in January of 1992 that total this $23,866,465.55 amount.[59] (FTB Feb. 19, 2013 Br., Ex. EE, Tab 12 [February 7, 1996 letter, which is also set forth further below in this Background section].)

January 14, 1992 and January 24, 1992 - $50,000 of Income. This is the sum of two $25,000 payments related to foreign tax payments. As discussed further in Staff Comments, the FTB asserts that these amounts were paid on appellant's behalf in 1991 but should be recognized as income in January of 1992 under the duty of consistency doctrine. Appellant argues that these payments are not taxable income.

January 24, 1992 or February 12, 1992 - $52,861 of Income. This amount is related to payments by Sharp.[60] Appellant refers to this income as being from Philips.

January 31, 1992 or February 3, 1992; $1,699,213 of Income. This amount is related to a payment from Oki.[61]

(The FTB determined that appellant was a resident through April 2, 1992.)

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[58] In some cases, staff has provided alternative dates for the receipt of payment, as the parties disagree regarding the date of payment. Also, as discussed in Staff Comments, the FTB argues that some payments were received in 1991 but should be taxed in 1992. Staff further notes that the parties sometimes dispute whether a payment should be listed as from Philips (representing net proceeds from a company distributed by Philips) or a payment from the company directly. For arguments and payment information, see FTB Feb. 19, 2013 Br., pp. 28-29 and fns. 152-157, and App. First Add'l Br. Apr. 10, 2013, pp. 7-8.

[59] Specifically, the table shows January deposits from Philips of $10,000,000, $5,000,000, $4,000,000, and $4,866,465.55.

[60] The FTB argues that it is taxable on January 24, 1992, on the basis that it went into a trust account on that date, which the FTB contends that appellant controlled. Appellant argues that he did not receive his share of the proceeds from the trust account until February 12, 1992. It appears to staff that this timing difference is irrelevant unless the Board determines that appellant moved to Nevada on or between the two dates.

[61] The FTB argues that it was recognized as taxable income on the earlier date, when it was sent to the trust account, while appellant argues he did not receive his share of the proceeds until February 3, 1992.

July 8-9, 1992; $200,000 Annual Philips Payment. The FTB argues that this income "is California source income regardless of the date received" on the basis that appellant was a California resident when the licensing agreement was signed. (FTB Feb. 19, 2013 Br., p. 29, fn. 155. See also FTB 1991 Op. Br., pp. 24–26.)

July 30-31, 1992; $17,835,605. This reflects a payment from Sanyo.

September 4-8, 1992; Approximately $18.4 million; Hitachi. The FTB argues that appellant recognized $12,449,433 and $6,000,000 on September 4, 1992 (for a total of $18,449,433). Appellant argues that he received $16,549,433 (i.e., $4.1 million more than $12,449,433) on September 4, 2016 but only $2 million, rather than $6 million, on September 8, 1992 (for a total of $18,549,433). Thus, appellant appears to argue that, in total, he received approximately $100,000 more in this period than the FTB asserts.

October 1-5, 1992; $685,084. This reflects a payment from Omron.

November 13, 1992 (according to the FTB) or November 17, 1992 (according to appellant); $1,275,000. This reflects a second Oki payment. The FTB argues that it is also taxable on a residency basis on the ground that, according to the FTB, it was realized on January 31, 1992. (FTB Feb. 19, 2013 Br., p. 29, fn. 157.)

December 28-30, 1992; Approximately $14.4 million. This is related to payments from Hitachi. Appellant argues that $3 million of this amount was received on December 29, 1992 and $11,465,109 was received on December 30, 1992 (for a total of $14,465,109). The FTB argues that a total of $14,265,109 was received on December 28, 1992, consisting of a $10,265,109 payment and a $4.2 million payment.[62]

December 29, 1992; $6,140,935. This relates to payments from Nippon Columbia and Kenwood.[63]

Appellant's 1992 federal tax return, which showed income for all of 1992 from all

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[62] A February 5, 1996 letter from State Street Bank and Trust Company shows a $11,465,109 amount received on December 30, 1992, which corresponds to the amount listed by appellant. (App. 1992 Op. Br., Ex. 38, p. 6 of PDF, numbered H 02338.) Based on the letter, it appears possible that the FTB's $10,265,109 amount and its $14,265,109 total may represent a typographical error (i.e., that the FTB may have meant to refer to a $10,465,109 amount and a $14,465,109 total).

[63] The foregoing amounts total approximately $84.7 million.

sources, showed adjusted gross income $84,973,440, including gross receipts of $84,770,124 from Philips, Oki and Hitachi.[64] On August 21, 1995, FTB employee Monica Embry sent an internal FTB memorandum summarizing a June 6, 1995 discussion regarding audit issues and concluded that, as they had found few facts to support appellant's involvement in a patent business, there was "little evidence" to support a trade or business of developing patents or that the patents had a California business situs.[65] On November 2, 1995, the FTB sent appellant a letter with the subject heading "FTB audit of Gilbert P. Hyatt for 1992," noting its residency determination for 1991 and asking appellant for documentation concerning the Schedule C gross receipts shown on his 1992 federal tax return, "such as contracts, royalty reports, bank statements, and documentation of wire transfers to verify when the payments were received by Mr. Hyatt." On November 7, 1995, appellant objected (through his representative) that he was aware of a residency determination for 1991 but not for 1992, and indicated that he did not understand the relevance of the request. On January 19, 1996, the FTB sent a second request for the information. (FTB Feb. 19, 2013 Br., p. 3–5, Ex. EE, Tabs 2, 4, 11.)

On February 7, 1996, appellant's representative responded with a letter enclosing a table showing income from Philips, Oki, and Hitachi, and, according to appellant, the dates of receipt. The table is set forth on a following page, and for ease of reference includes staff notations "A" through "F" which are referenced in the explanation following the table.

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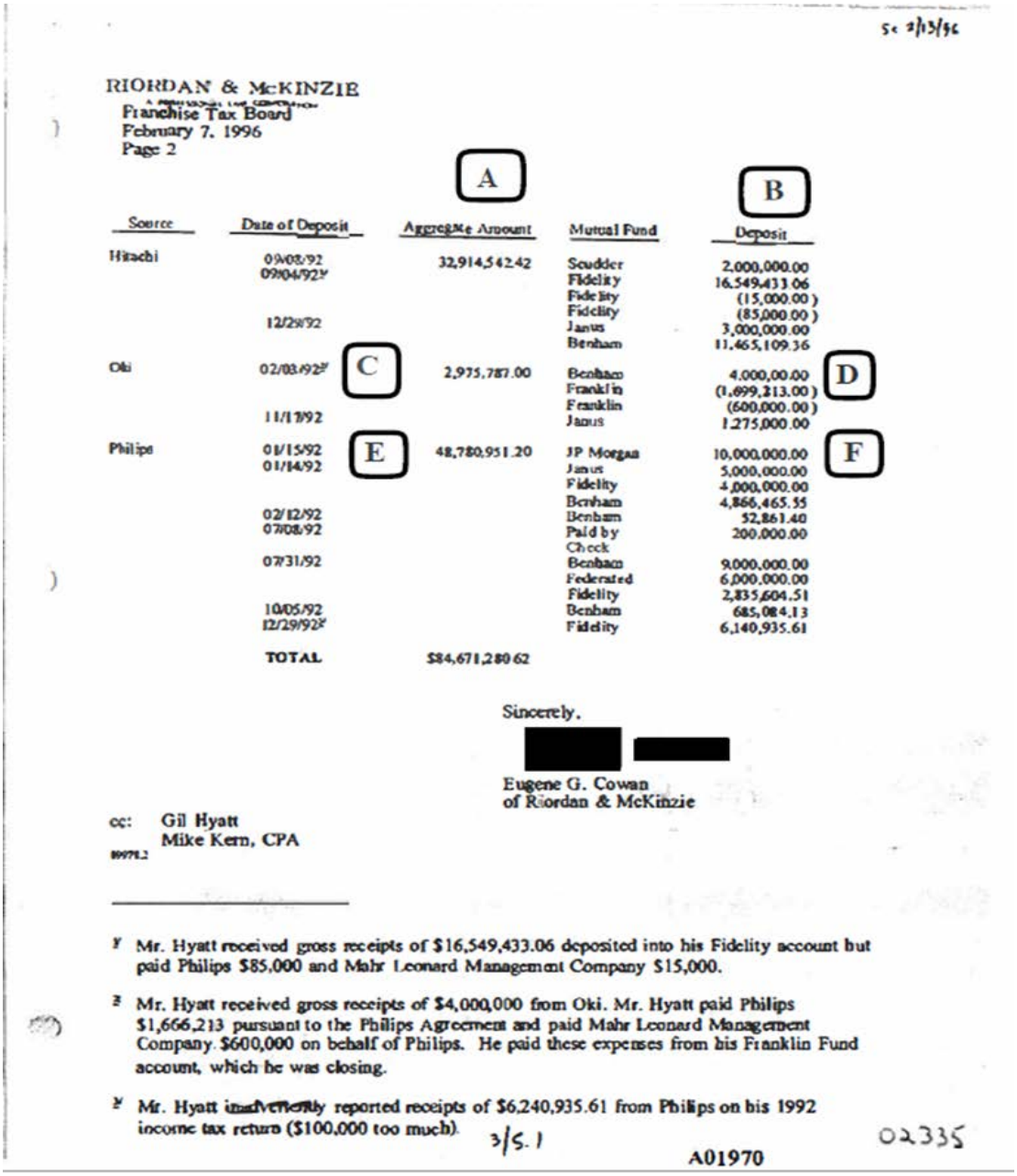
[64] Appellant's 1992 federal tax return can be found in appellant's Annex V, at H02603, and can also be accessed through a link in footnote 275 on page 54 of appellant's 1992 Opening Brief.

[65] See App. 1991 Op. Br., p. 83 & Ex. 69; App. 1991 September 28, 2016 Br., p. 15 & Ex. 69. The FTB argues that the Embry memorandum reflected an assumption that appellant was not engaged in a licensing activity which assumption, the FTB contends, was based on incomplete information proved incorrect by evidence largely acquired after the audit. (See FTB 1992 Op. Br., pp. 28-29.)



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Source	Date of Deposit	Aggregate Amount (A)	Mutual Fund	Deposit (B)
Hitachi	09/03/92	32,914,542.42	Scudder	2,000,000.00
	09/04/92[1]		Fidelity	16,549,433.06
			Fidelity	(15,000.00)
	12/28/92		Fidelity	(85,000.00)
			Janus	3,000,000.00
			Benham	11,465,109.36
Oki	02/03/92[2] (C)	2,975,787.00	Benham	4,000,000.00 (D)
			Franklin	(1,699,213.00)
	11/17/92		Franklin	(600,000.00)
			Janus	1,275,000.00
Philips	01/15/92 (E)	48,780,951.20	JP Morgan	10,000,000.00 (F)
	01/14/92		Janus	5,000,000.00
			Fidelity	4,000,000.00
	02/12/92		Benham	4,866,465.55
	07/08/92		Benham	52,861.40
			Paid by Check	200,000.00
	07/31/92		Benham	9,000,000.00
			Federated	6,000,000.00
			Fidelity	2,835,604.51
	10/05/92		Benham	685,084.13
	12/29/92[3]		Fidelity	6,140,935.61
	TOTAL	$84,671,280.62		

Sincerely,

[redacted]

Eugene G. Cowan
of Riordan & McKinzie

cc: Gil Hyatt
Mike Kern, CPA

[1] Mr. Hyatt received gross receipts of $16,549,433.06 deposited into his Fidelity account but paid Philips $85,000 and Mahr Leonard Management Company $15,000.

[2] Mr. Hyatt received gross receipts of $4,000,000 from Oki. Mr. Hyatt paid Philips $1,666,213 pursuant to the Philips Agreement and paid Mahr Leonard Management Company $600,000 on behalf of Philips. He paid these expenses from his Franklin Fund account, which he was closing.

[3] Mr. Hyatt inadvertently reported receipts of $6,240,935.61 from Philips on his 1992 income tax return ($100,000 too much).

3/5.1

A01970

02335

The table shows deposits and deposit dates in various mutual funds. It groups the deposits by source, meaning by reference to Hitachi, Oki, or Philips. For each of Hitachi, Oki, and Philips, the table shows, in the second column, the date of deposits, in a third column, the aggregate amount of payments for that source for the entire year (noted by staff with an "A"), and, in a fifth column, the amount of the deposits into appellant's investment accounts on specific dates, including

deposits made after April 2, 1992 (noted with a "B"). On the same line as the February 3, 1992 date, it shows an aggregate amount of $2,975,787 from Oki (noted with an "C" on the table) and a $4,000,000 deposit into an investment account (noted with a "D" on the table). For Philips, on the same line as the January 15, 1992 date, it shows, in the fourth column, an aggregate amount of $48,780,951.20 (noted with an "E") received from Philips, and in the fifth column, a $10,000,000 deposit into a mutual fund, which was the deposit for that date (noted with an "F"). The total amount shown from all sources is $84,671,280.62.[66] The letter attaches documentation, such as checks and statements and letters from financial institutions, showing purchases or deposits on the dates indicated. (FTB Feb. 19, 2013 Br., p. 5, Ex. EE, Tab 12; App. 1992 Op. Br., pp. 53-54, Ex. 38.)

On receiving this information, the FTB's auditor logged, on February 13, 1996: "Received letter from rep – Hyatt received $51m during beginning of 1992 (tax potential $4.8m)." (FTB Feb. 19, 2013 Br., p. 12, Ex. EE, Tab 3.) It appears to staff that the auditor added the aggregate amount received from Oki for the entire year, $2,975,787 (noted with a "C"), to the aggregate amount received from Philips for the entire year, $48,780,951.20 (noted with an "E"), which totals $51,756,738 (or approximately $51 million, rounded), and treated these amounts as if they were all received on February 3, 1992 (for Oki) and January 15, 1992 (for Philips). In fact, only a portion of the total payments for the year were received on February 3, 1992 and January 15, 1992.

On April 1, 1996, the auditor sent appellant a tentative Determination Letter that includes a schedule which carries over this apparent error and incorrectly shows the aggregate amounts having been received on February 3, 1992 and January 15, 1992. The letter states that appellant is taxable as a resident until April 3, 1992. Appellant indicated that he did not agree. (FTB Feb. 19, 2013 Br., p. 12, Ex. EE, Tab 18.)

On August 14, 1997, the FTB issued an NPA for 1992. In the NPA, the FTB determined that appellant was "a resident of this state through April 2, 1992 and, as such, [was] taxable on income from all sources through that date." The NPA attached calculations showing that, out of federal adjusted gross income of $84,973,440 for 1992, appellant's California income was $51,595,186. The

[66] In a footnote, appellant's letter indicates that he incorrectly over-reported receipts from Philips on his tax return by $100,000, pointing to an over-stated entry on December 29, 1992.

calculations thus continued to reflect the FTB's determination that appellant received a $48,780,951 payment from Philips on January 15, 1992. (FTB Feb. 19, 2013 Br., p. 14, Ex. A, Tab 2.)

On October 10, 1997, appellant protested the NPA. (FTB 1992 Op. Br., Ex. H, Tab 25 [protest].) Appellant's protest described the issue as being whether appellant was a resident through April 2, 1992, and again raised the issue of an error in the calculation of the amount of income received prior to April 3, 1992. On September 27, 2000, and October 4, 2000, protest hearings were held.[67] On October 4, 2000, the FTB sent a letter indicating that one of the four issues at protest was "[w]hether the patent license and royalty income received by Hyatt during 1991 and 1992 is California source income." (FTB Feb. 19, 2013 Br., p. 15, Ex. DD, Tab 11.) On February 2, 2001, appellant filed a 132-page protest supplement letter. (App. 1992 Op. Br., p. 63; App. Annex IV.)

On May 9, 2001, the FTB requested copies of contracts with Hitachi, documentation indicating when $9,000,000 was paid from Sharp, verification that the auditor did not include the $9,000,000 from Sharp in her adjustment, and, all contracts not yet provided "relating to the $48,780,951" received from Philips "during 1992." Appellant argued that information regarding payments made after the disputed period was irrelevant. (FTB Feb. 19, 2013 Br., Ex. EE, Tab 28.)

On November 1, 2007, the FTB sent a 50-page protest Determination Letter indicating that the hearing officer intended to affirm the NPA. The Determination Letter acknowledges that appellant had stated that only $23,919,327[68] was received during the disputed period. The letter states that the FTB repeatedly requested payment information from the taxpayer but that the FTB "never received adequate information to develop a reliable reconciliation of the payments by date and source." In a footnote, the letter notes a "possible reconciliation" in which appellant only receives $23,866,465 on January 14, 1992. On page 25, the letter further states that, due to a lack of information, the hearing officer had no choice but to affirm the assessment, and added: "To the extent that a quasi-judicial or

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[67] As noted previously, the FTB argues that both hearings covered both years while appellant contends that the 1991 protest hearing was held on October 4 and the 1992 protest hearing was held on September 27, 2000. (See FTB 1992 Reply Br., p . 81; App. 1991 Op. Br., p. 88; App. 1992 Op. Br., p. 68.)

[68] This amount corresponds to the (rounded) sum of $23,866,465.55 and $52,861.40, which amounts appellant describes as being received from Philips and the FTB describes as being received from Sharp, Sony and NEC. It does not include $161,552 of expenses and it does not include the following amounts that the FTB argues are taxable on a residency basis: the $1,699,213 Oki amount, the $200,000 annual payment, and the $50,000 in foreign tax payments.

judicial body determines based on credible evidence that there is an overassessment for taxable year 1992, the [FTB] will gladly make an adjustment." On page 41, the letter also states as follows: "If the income is California source income, all of the payments received by Hyatt from the licensing agreements during 1991 and 1992 are taxable by California. Accordingly, it is possible that for taxable year 1992, the department under assessed Hyatt on the licensing income." The letter argues that the patents have a business situs in California such that the income is California source income.[69]

On December 26, 2007, the FTB issued the NOA for 1992, which sustained the protest hearing officer's determination and refers to the November 1, 2007 Determination Letter. The NOA states:

> We consider you to be a resident of this state through April 2, 1992 and, as such, you are taxable on your income from all sources through that date. Consistent therewith and predicated upon all of the facts and evidence that we have developed as a result of your contest of the assessment, *the assessment is further and alternatively sustained on the basis that your intellectual property, from which your income was generated, had a business situs in California for the entire taxable year and was therefore derived from sources within California*. [emphasis added by Appeals Bureau staff]

(FTB Feb. 19, 2013 Br., Ex. A, Tab 4.)

In his 1992 Opening Brief, pages 52 to 56, appellant reiterated his contention that the FTB made a $24 million error, and provided in support the documents provided by his representative on February 7, 1996. In the FTB's 1992 Opening Brief, pages 46 to 47, the FTB stated generally that appellant's evidence was determined to be insufficient and that the issue continued to be in dispute. The FTB also argued "[u]sing their discretion, FTB audit staff rejected [the] deposit documentation [provided by appellant] as insufficient proof of earned income . . . ." On January 17, 2013, Appeals Division staff requested additional briefing with regard to the basis for the FTB's determination that appellant received a payment of $48,780,951 on January 15, 1992. The FTB responded with a brief dated February 19, 2013, and appellant responded with a brief dated April 10, 2013. The parties also addressed this issue in their Concluding Summaries and other briefing.

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[69] FTB 1991 Op. Br., p. 1, Ex. A, Tab 4 [The letter is located after the NOAs and begins with a page marked FTB 28751. Sourcing argument is on pages 30 to 48 of the letter, beginning on page 123 of the PDF, and the possible reconciliation is on page 25 of the letter, which is on page 118 of the PDF.].

Contentions – Issue (2) – Source of Income

Appellant's Contentions

Appellant incorporates various sections of his 1991 Concluding Summary. In his 1991 Concluding Summary, appellant argues that the FTB has the burden of proof on sourcing and cannot meet its burden. He further argues that the FTB's "Embry audit task force in 1995 determined that FTB did not have a sourcing case against Mr. Hyatt." He contends that the disputed income "came from the ordinary course of licensing Mr. Hyatt's ***Nevada situs patents*** and is therefore not taxable by California . . . [appellant's emphasis]" (App. 1992 CS, p. 24; App. 1991 CS, pp. 21-22.)

Appellant argues that he did not have California source income under Regulation 17951-4 "because he did not engage in a patent licensing business in California or anyplace else." He contends that he did not have California source income under R&TC section 17952 because his patents did not have a California business situs. He argues that "the substantial use and value" of the patents was transferred to Philips and that proceeds from the licensing agreements were transferred to Nevada financial accounts. He asserts that he had "very limited involvement in the Philips Licensing Program." He also argues that the FTB erroneously bases its arguments on mis-addressed documents. He argues that the use of California independent contractors "does not establish a California business[,]" and that the FTB's "so-called 'Commercial Exploitation' argument is without merit."[70] (App. 1991 CS, pp. 23-24.)

Appellant argues that the FTB has committed a "$24 million fraud on Mr. Hyatt." Appellant contends that the FTB failed to correct its error or respond to his evidence until requested to do so by the Board, [71] that "in bad faith" the FTB "still misrepresents the license payments" and "still persists in the tens of millions of dollars of taxes, interest, and penalties that it fraudulently assessed." Appellant argues that the "post-disputed period" in which appellant received the $24 million of income "has not been audited or protested by the FTB." Appellant further argues that the NPA is arbitrary such

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[70] Appellant appears to be referring here to the FTB's argument that the commercial exploitation of the patents produced California source income. (See, e.g., App. 1991 Op. Br., pp. 75 – 77 [referring to page 34 of FTB's November 1, 1997 Determination Letter]; FTB 1992 Reply Br., p. 14; FTB July 6, 2014 Br., pp. 22-24; App. 1992 Sep. 28, 2016 Br., p. 42.)

[71] Appellant refers here to the additional briefing letter sent by the Appeals Division on January 17, 2013.

that the FTB has the burden of proof, and that including the $24 million in income should be barred by the principles of equitable estoppel and the equitable doctrine of laches. (App. 1992 CS, pp. 1-2; see also App. 1991 CS, pp. 23 - 25.)

Appellant contends that: "Although FTB has now acknowledged that the $24 [million] in license payments were received after the 1992 disputed period when Mr. Hyatt is recognized by FTB to be a Nevada resident, FTB still holds to its NPA residency assessment of its $24 million error plus penalties and interest." Appellant further contends that the Board should "disregard" the FTB's sourcing arguments in the FTB's February 19, 2013 additional brief because the FTB was requested to provide briefing "narrowly focused on the factual issues" but instead used the briefing "to explain income related to its new sourcing argument after April 2, 1992." Appellant argues that the Board should correct the FTB's failure to withdraw the taxes, interest, and penalties "that were falsely assessed on its $24 million error" as the FTB now admits that the $24 million of income was received after the disputed period and not on January 15, 1992 as determined at audit and protest. (App. 1992 CS, pp. 2-3; see also App. 1991 CS, pp. 23-25.)

Appellant argues that the FTB's 1992 Concluding Summary denies that the FTB made a $24 million error even though the FTB previously acknowledged the error. Appellant states that the FTB previously "admitted that the license payments from Sanyo, Omron, Kenwood and Nippon Columbia were made in the second half of 1992 ***after the disputed period*** and not in January 1992 during the 1992 disputed period as previously falsely contended by FTB. [appellant's emphasis]" (App. 1992 CS Reply, pp. 19-20.)

Appellant notes that, in response to the FTB's request during audit, Mr. Cowan provided "a letter dated February 7, 1996 with a table detailing the dates of receipt of the payments from Philips, Oki, and Hitachi." Appellant argues that the FTB had stated that appellant could provide documentation such as bank statements and that, in response, appellant provided bank statements, "equivalent" documents, and copies of checks. Appellant contends that he provided the requested documentation and the auditor did not request any more information. (App. 1992 CS Reply, pp. 20-21.)

Appellant states that the FTB "incorrectly alleged that Mr. Hyatt received a $48.8 million payment from Philips on January 15, 1992[,]" despite the dates and documentation provided in

Mr. Cowan's letter. However, appellant explains, he only received $23.9 million from Philips in January of 1992 and did not receive $48.8 million on January 15, 1992 as "incorrectly contended" by the FTB. Appellant states that, as shown in Mr. Cowan's letter, he received "the rest of the license payments of $24 million from Philips much later in 1992, well after the disputed period." Appellant argues that the dates on Mr. Cowan's letter are clear, as are the attached documents, and that neither the FTB auditor nor the FTB in its 1992 Concluding Summary could possibly have interpreted the letter in good faith to state that $48.8 million was received on January 15, 1992. (App. 1992 CS Reply, pp. 20-21.)

Appellant argues that the FTB "falsely states that the financial institutions gave 'dates of Mr. Hyatt's own redeposits of his money during 1992.'" Appellant contends that these dates and amounts reflected the date of wire transfers and "one relatively small check from Philips." Appellant further contends that the FTB falsely states that the auditor requested "statements from Philips[,]" when the auditor requested "bank statements[,]" which is what appellant provided. Appellant argues that, contrary to the FTB's contention, appellant did not receive the disputed payments from the Japanese companies. Appellant further argues that Philips received payments from the companies "either directly or through a trust account held by Pretty, Schroeder, Brueggemann & Clark (PSB&C) for the benefit of Philips[,]" and that the payments at issue from Sanyo, Omron, Kenwood, and Nippon Columbia were wired directly to Philips in New York. Appellant contends that the "FTB does not identify any conflicts" in the information provided and that appellant "knows of none." Appellant further contends that, as he is a cash-basis taxpayer, the only relevant dates are the dates that appellant personally received the Philips payments, which are shown in Mr. Cowan's letter. Appellant states that he would not have received "wire transfer payment information" that the FTB discusses because the wire transfers "were sent to his investment account and not to him." (App. 1992 CS Reply, pp. 21-22.)

Appellant states that the FTB has confirmed in its additional briefing that the $24 million was not received on January 15, 1992. Appellant contends that it is indisputable "that Mr. Cowan produced correct information, that FTB made a $24 million error, that FTB delayed for about 15 years before finally admitting to the $24 million error as a result of the Additional Briefing ordered by your Board, and that FTB's statements attempting to excuse its bad faith and extortionate actions are false." (App. 1992 CS Reply, p. 22.)

Appellant reiterates that he did not receive payments directly from the Japanese companies but Philips received payments and then made much smaller payments to appellant. Appellant contends that he did not receive the $24 million from "his patents and patent licensing business[,]" as argued by the FTB, but instead received the amount from "his exclusive patent license with Philips under the terms of the July 1991 Philips Agreements." (App. 1992 CS Reply, p. 22.)

Appellant contends that, as sourcing only applies to nonresidents, the FTB "must concede Mr. Hyatt is a resident of Nevada for its sourcing argument." Appellant argues that he "did not have a California business." Appellant asserts that the FTB has "never argued" that his "patents were employed as capital within California[,]" and that the FTB "cannot establish that possession and control of the patents has been localized in connection with a business so that their 'substantial use and value' attach to and become an asset of the business in California." Appellant further asserts that, "[a]fter the July 1991 Philips Agreement granted Philips exclusive licensing rights [no] 'substantial use and value' remained to be transferred to a California business." (App. 1992 CS, pp. 19-21.)

Appellant argues that "[s]ourcing – at best – is only before your board for the period September 26, 1991 through April 2, 1992 because there has never been an assessment made against Mr. Hyatt regarding the post-disputed period." Appellant further argues that the evidence shows the FTB "cannot meet its burden of proof to show that Mr. Hyatt had California source income during the disputed period or thereafter." (App. 1992 CS, p. 21.)

In support, appellant argues that the Philips Licensing Program Agreements show that he did not have California source income. Pointing to the July 1991 Philips Agreement and an affidavit of Algy Tamoshunas, appellant argues that "Philips itself created and managed the Philips Licensing Program" and did not create any agency relationship between Philips and appellant. Appellant asserts that "[t]he fact that Philips Licensing Program correspondence was misdirected to Mr. Hyatt's former California addresses after he moved to Las Vegas does not establish he was in control of the Philips Licensing Program." Appellant also asserts that "neither the IRS audit nor the Philips/Hyatt termination agreement undermine the fact that Philips was in control of the Philips Licensing Program under the July 1991 Philips Agreement." (App. 1992 CS, pp. 20-21; see also 1991 App. CS, pp. 21-26.)

Appellant argues that the Philips documents do not support the existence of a "Jennifer

Circle, La Palma, home business[,]" and that the FTB incorrectly contends that Ms. Jeng worked from Jennifer Circle and was paid for services performed by Mr. Hyatt. Appellant further argues that the FTB incorrectly contends that appellant left and used office equipment at Jennifer Circle during the disputed period. (App. 1992 CS, p. 21.)

Appellant contends that, contrary to the FTB's argument, he "has never contended that DNC [Digital Nutronics Corp] participated in the Philips Licensing Program." Appellant contends that he signed patent agreements at Philips' request and pursuant to the three supplemental agreements and that "[n]othing in the September 1991 Mahr Leonard Agreement or Philips Supplemental Agreements undermine the fact that PSB&C and Mahr Leonard negotiated with Hitachi, not Mr. Hyatt." Appellant further contends that the testimony of witnesses regarding the Philips Licensing Program "cannot be discredited[,]" pointing to the testimony of Mr. Tamoshunas, Mr. Roth, Mr. Huntington, and his own testimony. In this connection, appellant contends that Mr. Roth "represented Philips, not Mr. Hyatt after July 1991 with respect to the *Hyatt v. Boone* interference and the Philips Licensing Program." (App. 1992 CS, p. 22.)

Disputing the FTB's contentions, appellant argues: that his business activities in California prior to moving to Las Vegas are not relevant; that any business expense deductions for his work "as an inventor and any related activities would have been performed at [his] home in Las Vegas[;]" that the FTB's arguments fail "as a matter of law" under R&TC section 17952 and Regulation 17952. Appellant further argues that "there were no '$33.5 million in guaranteed payments'" which amounts were a "condition precedent 'in order to retain the sublicensing rights'[,]" quoting the July 1991 Philips Agreement. Appellant also argues that there were no "$3 million in guaranteed payments[,]" also citing the July 1991 Philips Agreement. (App. 1992 CS, p. 23.)

Appellant asserts that the Philips documents "significantly support [his] residency and sourcing appeals." Appellant further argues that the Philips documents show that Philips managed the Philips licensing program and that appellant had "only limited involvement in the large worldwide Philips licensing program." Appellant contends that the documents refute the FTB's claim that he operated a licensing business at the Jennifer Circle house and show that he was "contractually prohibited from operating a licensing business." Appellant asserts that the FTB's "overbroad Philips subpoenas

forced Mr. Hyatt to obtain New York court orders and temporary restraining orders to protect his confidential information and to avoid an overbroad production . . . ." (App. 1992 CS, p. 12.)

Appellant asserts that the FTB "attempts to misrepresent . . . that Mr. Hyatt had a California licensing business by quoting statements Mr. Hyatt made in a radio interview with Mike Malone in May 1991." Appellant states that, during the interview, "Mr. Hyatt indicated that his people had been approached by a group of companies and were negotiating with them." Appellant states that, at the time of the interview, Mahr Leonard "had exclusive rights to negotiate with four companies pursuant to a First Amendment . . . to the December 18, 1990, Mahr Leonard Agreement." Appellant asserts that "Mahr Leonard was doing the negotiating." Appellant further asserts that: "Under the July 1991 Philips Agreement, Philips had the responsibility to sublicense Mr. Hyatt's patents." Appellant argues that he "did not personally negotiate sublicenses that were signed under the [Philips] Licensing Agreement." (App. 1992 CS, pp. 12-13.)

Appellant contends that the FTB falsely states that appellant works from his Jennifer Circle "home/business." Appellant further contends that he "did not have a 'home/business' at his former Jennifer Circle La Palma house, which he sold on October 1, 1991." (App. 1992 CS, p. 15.)

Appellant argues that he had "no discretion over distribution of the license payments from Fujitsu, Matsushita [Matsushita Electric Industrial Co., Ltd.] and OKI[,]" and that he "promptly distributed the license payments as required by the [First] Supplemental Agreement." Appellant argues that he did not negotiate with Hitachi at any time and that he did not attend a dinner show with Hitachi on January 28, 1992. Appellant contends that Mr. Roth "accurately testified that the licensing correspondence was primarily between Philips, Mahr Leonard, PSB&C and the licensees and Mr. Hyatt was outside the mainstream of the licensing correspondence . . . ." (App. 1992 CS, pp. 17-18.)

FTB's Contentions – Issue (2) – Source of Income

Citing R&TC section 17952, the FTB states that income from intangibles such as patents is California source income if the intangibles acquired a business situs in California. Quoting Regulation 17952, the FTB states that intangible property has a business situs in California if "[i]t is employed as capital in this State or the possession and control of the property has been localized in connection with a business, trade or profession in this state so that its substantial use and value attach to

and become an asset of the business, trade or profession in this state . . . ." (FTB 1992 CS, pp. 11-12.)

The FTB argues that appellant "devoted himself to the pursuit of patents," obtained his education in California, and that "the patents that generated the income at issue . . . were all researched, developed, applied for and issued while Mr. Hyatt admits he was a California resident."[72] The FTB contends that "[t]he patent which led to Mr. Hyatt finally realizing income" was the '516 patent for "Single Chip Integrated Circuit Computer Architecture" which was awarded to appellant on July 17, 1990.[73] The FTB states that, shortly after the award of the patent, Gary Boone contested the award of the patent with the United States Post Office (USPTO). (FTB 1992 CS, p. 12.)

The FTB contends that appellant "surrounded himself with retained California professionals to assist him with his patent and patent-related endeavors[,]" arguing that Mr. Hyatt had a professional relationship with Mr. Roth from 1970 "through at least July 1993." The FTB further contends that appellant "was also assisted in his patent licensing endeavors" by persons "who were located and performed their work in California and/or at Jennifer Circle[,]" listing Barry Lee, Grace Jeng, Caroline Cosgrove, and Leni Schlendwin. (FTB 1992 CS, pp. 12-13.)

The FTB argues that ". . . Mr. Hyatt retained expert assistance" to retain the '516 patent and to obtain licensing fees. The FTB further argues that "Mr. Hyatt entered into an agreement with Mahr Leonard Management Company (MLMC) for such services during November, 1990, which resulted in MLMC's immediate initiation of contacts with Japanese electronics companies." The FTB asserts that the purpose of the contracts "was to negotiate lump sum patent licensing payments to Mr. Hyatt in exchange for a waiver of formal claims, including potential litigation, of patent infringement." The FTB further asserts that various Japanese companies entered into licensing agreements with Mr. Hyatt and that MLMC "agreed to provide Mr. Hyatt with financing so as to enable him to defend Mr. Boone's challenge of . . . the '516 patent . . . ." (FTB 1992 CS, p. 13.)

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[72] It appears to staff that the relevant sourcing inquiry under R&TC section 17952 is whether the intangible property had a business situs in California during the periods at issue, not whether the intellectual property was developed in California in prior periods. If the FTB is arguing that the development of intangible property in California causes income from that intellectual property to be sourced to California in later years, it should be prepared to provide supporting authority.

[73] This is sometimes referred to as appellant's microprocessor patent. The FTB argues that "knowledgeable observers" would concur that this was appellant's "only valuable patent." (FTB 1991 Op. Br., p. 6, fn. 18.) Appellant argues in part that this was only one of 23 or 24 patents that were licensed. (App. 1991 Reply to FTB CS, p. 2.)

The FTB contends that ". . . Mr. Hyatt, with the assistance of Mr. Roth, sought, and, during July, 1991, obtained the professional assistance of [Philips] in his patent licensing endeavors." The FTB further contends that "[t]he patent marketing and licensing strategy that lead to the receipt of the licensing fees was designed and put into action by Mr. Hyatt and his team prior to September, 1991." The FTB asserts that, due to the potential that appellant could lose the microprocessor patent, ". . . the plan focused on obtaining agreements for 'paid-up royalties' in which the payment consideration was largely for past use (i.e. Hyatt's promise not [to] sue for past infringement) and was to be made either concurrently with, or shortly after, the effective/signatory dates of the agreements." The FTB further asserts that, in an August 15, 2005 deposition, Mr. Hyatt "states that no new information or technology was transferred pursuant to the licensing agreements and that in exchange for payment the companies were getting freedom from being sued for patent infringement." (FTB 1992 CS, pp. 13-14.)

The FTB argues that, by September 15, 1991, the day prior to "Mr. Hyatt's alleged termination of his California residency . . . MLMC, Mr. Hyatt and Philips knew that their marketing and licensing program was proving to be a huge success as they had 'current offers' from five Japanese companies totaling $80,500,000." The FTB further argues that if one compares the offers with the fees actually paid one can see "that virtually all of the negotiations were completed by September 25, 1991 as 96% of the aggregate value of those contracts had already been offered." The FTB contends that the "expectations soon became reality" with formal contracts being entered into as early as October 14, 1991, and with the "same strategy (and portfolio of patents)" used to execute agreements with six other Japanese licensees during 1991 and 1992. (FTB 1992 CS, p. 14.)

The FTB asserts that "[t]he center of activity undertaken to bring those contracts to fruition, and distribute the monies received, was California." The FTB further asserts that "Mr. Hyatt set up his Jennifer Circle home with the equipment necessary to conduct a patent acquisition, marketing and licensing business, which included: a commercial grade photocopy machine, fax machine, storage files, computer(s), commercial grade steel shelving, and an office or laboratory." The FTB argues that appellant signed invoices for copier repairs at Jennifer Circle "throughout 1991 and as late as May 7, 1992." (FTB 1992 CS, p. 14.)

The FTB argues that ". . . this activity is memorialized by numerous communications

being sent to or from Mr. Hyatt through his Jennifer Circle street address, the Cerritos, CA Post Office Box and/or the Jennifer Circle facsimile machine through the end of 1992, and as late as May, 1994." The FTB states that the first five licensing agreements, signed in 1991, state that appellant's mailing address is Cerritos, California. The FTB notes that the Sony Corporation (Sony) and NEC agreements, executed on December 10, 1991, state his mailing address is at what the FTB characterizes as appellant's "low-income apartment." However, the FTB argues, "business correspondence surrounding . . . those contracts reveals that Mr. Hyatt was in Orange County, CA." The FTB further argues that appellant "also attends meetings in California regarding licensing activity and negotiations throughout 1991 and 1992." (FTB 1992 CS, pp. 14-15.)

The FTB contends that ". . . the objective evidence . . . demonstrates that Mr. Hyatt's marketing and licensing business continued to be located in California through at least the end of 1992." The FTB further contends that "[t]he purchase of a fax machine for use in Nevada is not demonstrated until April 5, 1992 and it is not until this date that a telefax identification spray with a Nevada area-code telephone number starts to appear on documents." The FTB argues that, on July 30, 1992, Mr. Hyatt acquired a new commercial grade copier for his "Jennifer Circle home/business" which "coincides with the old one being moved to his property on Tara Avenue in Las Vegas." (FTB 1992 CS, p. 15.)

The FTB asserts that there is "no objective evidence" that appellant's patent files were moved to Nevada or that appellant had access to business facilities in Nevada that would be necessary "to conduct his patent marketing and licensing business for almost six months after his alleged departure from California." The FTB also contends that it was not until December 1992 that appellant signed an application for a Nevada business license. (FTB 1992 CS, p. 15.)

On these grounds, the FTB contends "the patents that generated the income at issue in this appeal acquired a business situs in California which did not change at any time during 1991 and 1992." The FTB incorporates its arguments from its 1991 Concluding Summary with regard to sourcing. There, the FTB focuses on payments received in 1991 and references to its prior briefing. (FTB 1992 CS, pp. 15; FTB 1991 CS, pp. 24-25.)

With regard to the alleged $24 million error, the FTB contends that "[t]he 1992 Notice of

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Action does not contain a $24 million error."[74] The FTB argues that appellant's "concealment of his 1991 income and failure to establish a purported $24 million error [have] been extensively discussed in [its] earlier briefing," citing pages 46 to 47 of its 1992 Opening Brief and pages 2 to 19 of its February 19, 2013 additional brief. The FTB asserts that "[t]he only real evidence about Mr. Hyatt's receipt of his 1992 income that respondent had before it issued the [1992 NPA] was Mr. Hyatt's federal income tax return showing total income for the entire year." As a result, the FTB argues, its auditor asked for, quoting the auditor's request, the following: "documentation supporting the above Schedule C receipts, such as contracts, royalty reports, bank statements, and documentation of wire transfers to verify when the payments were received by Mr. Hyatt." (FTB 1992 CS, pp. 22-24.)

The FTB asserts that appellant provided a "non-responsive answer" in the form of a "self-generated schedule listing purported sources payments, dates of deposit, aggregate amounts, mutual funds, and deposits." As support, the FTB states, Mr. Cowan "merely provided letters from Mr. Hyatt's various money fund accounts including Janus, Federated, State Street (for Benham), Fidelity Investments, Scudder, and Pierpont which gave the dates of Mr. Hyatt's own redeposits of his money during 1992." The FTB argues that Mr. Cowan "did not provide wire transfer documentation, royalty reports, contracts or statements from Philips showing when Mr. Hyatt received payments from the Japanese companies." The FTB contends that "[a] careful review of the dates of payment by the Japanese companies reveals conflicts between the date payment was actually made and the dates of payment listed on Mr. Cowan's self-generated schedules." The FTB further contends that appellant did not provide wire transfer payment information and failed to provide responsive documents during the audit. (FTB 1992 CS, p. 24.)

Applicable Law – Issue (2) - Sourcing

Adequacy of a NPA

R&TC section 19033 provides that "[i]f the [FTB] determines that the tax disclosed . . . on an original or amended return . . . is less than the tax disclosed by its examination, it shall mail notice to the taxpayer of the deficiency proposed to be assessed." R&TC section 19033 further

[74] This is the heading of Section V of the FTB's 1992 Concluding Summary.

provides that "[i]no no case shall the determination of the deficiency be arbitrary or without foundation." R&TC section 19034 requires that the FTB send a notice to taxpayers which "shall set forth the reasons for the proposed deficiency assessment and the computation thereof."[75] This notice is referred to as a NPA. The taxpayer then has an opportunity to protest the proposed deficiency assessment with the FTB, pursuant to R&TC sections 19041 and 19044. At the conclusion of the protest process, the FTB issues an action on the protest, known as a NOA, which the taxpayer may appeal to the Board.

In *Scar v. Commissioner* (9th Cir. 1987) 814 F.2d 1363 (*Scar*), the taxpayers successfully challenged a notice of deficiency sent by the IRS that stated on its face that the Scars' tax return had not been examined. The Ninth Circuit ruled that "[b]ecause the Commissioner's purported notice of deficiency revealed on its face that no determination of tax deficiency had been made in respect to the Scars for the 1978 tax year, it did not meet the requirements of [IRC] section 6212(a)." (*Scar*, *supra*, 814 F.2d 1363, 1370.)[76]

In *Clapp v. Comm'r of Internal Revenue* (9th Cir. 1989) 875 F.2d 1396, the Ninth Circuit stated that *Scar* does not require "any affirmative showing . . . that a determination . . . was made on the basis of the taxpayers' return." Instead, the Ninth Circuit stated, "[o]nly where the notice of deficiency reveals on its face that the Commissioner failed to make a determination is the Commissioner required to prove that he did in fact make a determination." Applying this standard, the Ninth Circuit found that the notices of deficiency at issue were valid as, on their face, the notices made clear that the IRS examined the returns, considered the deduction at issue and attributed income based on trusts related to the taxpayer rather than, as in *Scar*, on the basis of unrelated entities. Quoting *Scar*, the Ninth Circuit further stated that, in assessing the validity of the notice, it would not consider internal IRS memoranda and would not "depart from the rule that we should not 'look behind a deficiency notice to question the Commissioner's motives and procedures leading to a determination.'"

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[75] During 1991 and 1992, this language was set forth in R&TC section 18584.

[76] In *Wertin v. FTB* (1998) 68 Cal.App.4th 961, the appeals court applied *Scar* to a NPA issued by the FTB. The appeals court found that *Scar* was applicable as California tax law used language that was very similar to the language used in the Internal Revenue Code. Therefore, the court held that the FTB was required to review the Wertins' return prior to issuing its proposed assessment, and ruled in favor of the Wertins.

(*Clapp, supra*, 875 F.2d 1396, 1401 [quoting *Scar, supra*, 814 F.2d at 1368].)

In the *Appeal of Sierra Pacific Industries*, 94-SBE-002, decided January 5, 1994 (*Sierra Pacific*), the Board considered an appeal in which a subsidiary, Humboldt, transferred property to the taxpayer which the taxpayer then used in a sale-leaseback transaction.[77] The Board found that the FTB "may modify an NPA in order to reflect issues and conclusions developed during the protest." The Board stated that "[o]ne of the purposes of the NPA is to inform taxpayers so that they can intelligently lodge a protest." The Board found that the taxpayer was on notice that the FTB was reviewing the Humboldt transaction, which included the sale-leaseback.

Burden of Proof

In *Sierra Pacific, supra*, the Board also discussed whether the burden of proof should be shifted to the FTB. The Board stated as follows:

> If respondent's position on appeal results in a larger deficiency (had respondent adopted it initially), or requires the presentation of different evidence, then a new matter has been introduced and the burden of proving that new position shifts to respondent. However, if the assertion of a new theory merely clarifies or develops the original determination without being inconsistent with it or increasing the amount of the deficiency, it is not a new matter requiring the shifting of the burden of proof to respondent. (*Appeal of David G. and Helen Mendelsohn*, [85-SBE-141], Nov. 6, 1985; see also *Zarin v. Commissioner*, 92 T.C. 1084 (1989) and *Achiro v. Commissioner*, 77 T.C. 881 (1981) (interpreting Tax Court Rule 142(a)).)

Applying the above rules, the Board noted that the NOA decreased the amount of tax set forth in the NPA. The Board stated that ". . . it is logical for the respondent to modify its original determination so as to account for any new facts or information developed during the federal audit." The Board further stated that the property transaction, which it referred to as the Humboldt transaction, "was the subject of respondent's NPA, and continues to be so on this appeal." Accordingly, the Board found that the FTB had not raised a new matter that would shift the burden of proof.

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[77] The taxpayer argued that the transfer of property was a partial liquidation, but an IRS audit report found that the transfer was a dividend. The FTB then issued a NPA, dated July 19, 1976, which was apparently based on the IRS report. During protest, the taxpayer reached a settlement with the IRS. On June 8, 1987, following the protest, the FTB issued a NOA that accepted the IRS determination of a dividend, but changed the computation of the dividend and imposed additional tax on the sale-leaseback transaction. The taxpayer argued that the NOA was invalid because it raised new issues not covered by the NPA.

Source of Income

California residents are taxable on their income from all sources during periods in which they are a resident of California. For purposes of computing the taxable income of a nonresident or part-year resident, R&TC section 17951, subdivision (a), provides that "in the case of nonresident taxpayers the gross income includes only the gross income from sources within this state." R&TC section 17954 states that for purposes of computing taxable income of a nonresident or part-year resident, "gross income from sources within and without this state shall be allocated and apportioned under rules and regulations prescribed by the [FTB]."

Regulation 17951-4, subdivision (a), provides, in part, that if "the nonresident's business, trade or profession is conducted wholly within the state, the entire net income therefrom is derived from sources within this state." Regulation 17951-4, subdivision (b), provides that if a nonresident has a separate and distinct business in California that is unconnected with business outside the state then income from the California business is sourced to California. Regulation 17951-4, subdivision (c), provides rules for determining how to determine the income derived from California sources by a nonresident's sole proprietorship. It further provides that business income is apportioned pursuant to R&TC section 25120, *et seq*., while income that is not business income is determined by reference to R&TC sections 17951 through 17955.

R&TC section 17952 provides that "income of nonresidents from stocks, bonds, notes, or other intangible personal property is not income from sources within this state unless the property has acquired a business situs in this state . . . ." With respect to business situs, subdivision (c) of Regulation 17952 provides that:

> [i]ntangible personal property has a business situs in this State if it is employed as capital in this State or the possession and control of the property has been localized in connection with a business, trade or profession in this State so that its substantial use and value attach to and become an asset of the business, trade or profession in this State. For example, if a nonresident pledges stocks, bonds or other intangible personal property in California as security for the payment of indebtedness, taxes, etc., incurred in connection with a business in this State, the property has a business situs here.
>
> . . .
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> If intangible personal property of a nonresident has acquired a business situs here, the entire income from the property including gains from the sale thereof, regardless of where the sale is consummated, is income from sources within this State, taxable to the nonresident.

STAFF COMMENTS – ISSUE (2) – SOURCE OF INCOME

Issues to be Decided

It appears to staff that, once the Board decides when appellant moved to Las Vegas, it will need to decide two issues. The first issue is: what income, if any, is taxable on a residency basis?[78] As discussed further below, if the FTB's arguments are accepted, this amount would include a $200,000 payment from Philips and a $1,275,000 payment from Oki. Both of these payments were received after April 3, 1992, but the FTB argues these payments are taxable on a residency basis on the ground that appellant was a California resident when the license agreements were signed or became effective (in July of 1991 for Philips and January 31, 1992[79] for Oki). The FTB also argues that $50,000 in foreign tax payments (consisting of two $25,000 payments) that the FTB alleges were made on appellant's behalf in 1991 should be treated as taxable during the residency period in 1992.

The second issue is whether any of appellant's income is taxable on a source basis. California residents are taxable on income from all sources during the period in which they are resident in California. Sourcing is only relevant for periods in which appellant is not a California resident.

There are, of course, different tax results depending on how the Board determines these issues. For example, if the Board accepts the FTB's argument that appellant did not move until April 3, 1992, and rejects the FTB's sourcing arguments, but accepts the FTB's argument that the $200,000, $1,275,000 and $50,000 in payments are also taxable on a residency basis, then it appears to staff that the amount of taxable income would be $26,981,988 (i.e., the amount the FTB argues is taxable on a residency basis). On the other hand, if the Board accepts the FTB's argument that appellant did not move until April 3, 1992, but rejects both the FTB's sourcing arguments and the FTB's arguments regarding the $200,000, $1,275,000, and $50,000 payments, then it appears that the taxable income would be $25,456,988 (i.e., $26,981,988, less the sum of $200,000, $1,275,000 and $50,000). If the Board finds that appellant did not reside in California during 1992, *and* that the $200,000 Philips

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[78] This discussion is included here, rather than in Staff Comments for residency, because the timing issues appear to be intertwined with the sourcing arguments.

[79] If the Board determined that appellant moved to Las Vegas prior to January 31, 1992, then this Oki payment would not be taxable on a residency basis, even under the FTB's argument.

payment is not taxable on a residency basis,[80] then only income that is taxable on a source basis could be subject to tax. Although appellant received more than $80 million of income in 1992, the FTB's NPA and NOA only seek to impose tax on California income of $51,595,186, and staff's understanding is that the FTB is not seeking to tax income in excess of that amount.

The FTB's Calculation of Income Taxable on a Residency Basis

During additional briefing, the FTB conceded that appellant did not receive $51 million of income prior to April 3, 1992 and argued "that Mr. Hyatt's income earned before April 3, 1992, that would be used to for a computation of his 1992 tax only **if** the basis for taxation is California residency through April 2, 1992, would be $26,981,988. [FTB's emphasis]" (FTB Feb. 19, 2013 Add. Br., p. 28, fn. 152.) It appears that the $26,981,988 amount calculated by the FTB for this period includes (a) amounts totaling $23,866,465.55 received on or about January 14, 1992, (b) $50,000 related to foreign tax payments made during 1991, (c) $52,861.40 related to a Sharp payment, (d) a first payment by Oki of $1,699,213, (e) a $200,000 annual payment received on or about *July 9, 1992*, and (f) a $1,275,000 second Oki payment received on or about *November 13, 1992*. The total of these amounts, less $161,552 of expenses, equals the $26,981,988 amount that the FTB argues would be taxable if the Board sustains the FTB's residency determination but rejects the FTB's sourcing arguments. It appears that, aside from relatively minor timing differences, appellant agrees with these amounts, but disputes the FTB's argument that the $200,000 annual payment, the $50,000 in foreign tax payments, and the $1,275,000 Oki payment are taxable on a residency basis. (See App. First Add'l Br. Apr. 10, 2013, pp. 8-9.)

The $200,000 Philips Annual Payment & $1,275,000 Oki Payment

It is not clear to staff that the amount taxable on a residency-only basis should include the $200,000 Philips payment received on or about July 9, 1992 and the $1,275,000 Oki payment received on or about November 13, 1992. The FTB argues that the $200,000 amount would be taxable

[80] As noted above, the FTB argues that the $200,000 Philips payment is taxable on a residency basis on the ground that appellant was a California resident when the license agreement was signed in July of 1991. The FTB makes the same argument with respect to the Oki agreement, which is dated January 31, 1992, but, if the Board finds that appellant was not a California resident on January 31, 1992, the Oki payment would not be taxable on a residency basis even under the FTB's theory.

on the ground that California's jurisdiction to tax arose when the Philips agreement was signed on July 15, 1991, a time when appellant was a California resident. (FTB 1992 Op. Br., pp. 23–25.) With regard to the $1,275,000 Oki payment received on or about November 13, 1992, the FTB similarly argues that it was realized on January 31, 1991, which is the effective date of the agreement with Oki. (FTB Feb. 19, 2013 Br., p. 29, fn. 157 [citing pp. 24–26 of its 1992 Op. Br.]; FTB Ex. J, Tab 43 [Oki agreement].)

With regard to the Philips agreement, the FTB has argued that it provided guaranteed payments and therefore should be analogized to an installment sale of property. However, it is not clear to staff that the grant of the nonexclusive, nontransferable license of intellectual property is analogous to an installment sale of property.[81] With regard to whether the license was a sale of property, staff notes that, in the license at issue, not all rights were transferred (e.g., through Article 10, appellant retained the right to use the licensable patents, to license to affiliates, and to license to IBM). Even if the license could be viewed as a sale of property, it does not appear to staff that the payments in Section 4.6 of the licensing agreement were guaranteed because they were paid "in order [for Philips] to retain the sublicensing rights . . . [,]" and it appears they would not be owed if Philips decided to give up future sublicensing rights. Similarly, the $200,000 payment was made pursuant to section 3.1 of the agreement, and, even if the agreement could be viewed as a "sale" of property rather than an ongoing nonexclusive license, it is not clear to staff that this amount was guaranteed or analogous to a promised installment payment.[82]

With regard to the Oki agreement, the FTB argues that, because the Oki income "flows from" the agreement, it should be taxable by California based on appellant's residency as of the date of

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[81] The licensing agreement can be found, among other locations, at FTB's Exhibit G, Tab 10, and Exhibit 55 of appellant's 1991 Opening Brief.

[82] Under Section 7.4, if Philips did not make a payment under Section 3.1 *and* appellant elected to terminate the license (and thereby forfeited potential future sublicensing income under Section 4.6), appellant would not be entitled to the sublicensing payments listed in Section 4.6 and would only be entitled to smaller amounts due under Section 3.1, such as a $200,000 payment due for 1992. Thus, it appears that the payments in Section 3.1 would not be made if appellant declined to terminate the agreement in order to preserve the potential for future income under Section 4.6.

the agreement.[83] The FTB also references its arguments with regard to the Philips agreement, where the FTB argued that certain licensing payments were analogous to installment payments on a sale of property. In section 3.1 of the Oki agreement, appellant granted a "nonexclusive, worldwide (except Japan) license" to sell licensed products, and, in sections 2 and 3.3, released Oki from any infringement claims. (FTB Ex. J, Tab 43 [Oki agreement].) In Section 4.1, in return for the release and the "transfer and grant of the LICENSED PATENT right," Oki agreed to pay appellant "installment payments" including a $3 million payment on or before November 15, 1992. It appears that the $1,275,000 ultimately received is appellant's share of this payment after the deduction of Philips' share and expenses pursuant to appellant's agreement with Philips. At the hearing, the parties should be prepared to discuss further whether the $1,275,000 received by appellant in November 1992 should be treated as taxable by California on the basis that appellant was a California resident on the January 31, 1992 effective date of the agreement (if the Board find that appellant was a resident on that date).

The $50,000 in Foreign Tax Payments

The FTB argues that appellant had $25,000 of foreign taxes paid on his behalf by each of NEC and Sharp (for a total of $50,000). (FTB Feb. 19, 2013 Br., pp. 8, 22-23, 26, 29.) Appellant argues that these amounts are a foreign tax credit he received rather than taxable income. (App. First Add'l Br. April 10, 2013, p. 8.) The FTB argues that NEC paid $25,000 to Japan on December 27, 1991, and deducted this $25,000 from the amount to be paid to appellant, and notes that appellant reported this $25,000 as a foreign tax credit on his federal tax return. On this basis, the FTB argues that appellant received the income on December 27, 1991 but, "since Mr. Hyatt reported this income on his 1992 federal return, under the duty of consistency, FTB attributes this income to January 14, 1992." The FTB makes similar arguments with respect to Sharp's $25,000 payment.

The application of the duty of consistency requires (1) a representation by the taxpayer,

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[83] On page 24 of its February 19, 2013 brief, the FTB argues that "[a]s [the $1,275,000 payment] flows from the agreement executed on January 31, 1992 [referring to the effective date], it is realized on that January date, a finding only necessary if California residency as of April 2, 1992 is [not] used as a basis for taxation of Mr. Hyatt's income[,]" citing pages 24 to 26 of its 1992 Opening Brief. The FTB argues in fn. 157 of its Feb. 19, 2013 brief that the income was realized on January 31, 1991 (apparently meaning to refer to January 31, 1992), and again cites in support pages 24 to 26 of its 1992 Opening Brief. On pages 24 to 26 of its 1992 Opening Brief, the FTB discusses the Philips agreement but does not specifically reference the Oki agreement. (See FTB Feb. 19, 2013 Br., p. 29, fn. 157.)

(2) on which the FTB has relied, and (3) an attempt by the taxpayer after the statute of limitations has run to change the prior representation in a way that harms the FTB. If the duty of consistency applies, the FTB may act as if the representation is correct. (*Ashman v. Comm'r* (9th Cir. 2000) 231 F.3d 541, 545.) It appears to staff that, if the Board finds that these $25,000 payments were made on appellant's behalf in 1991, then they should have been included in appellant's 1991 income or in the FTB's assessment for 1991, unless, perhaps, the duty of consistency applies to estop appellant from arguing that the payments were not taxable income in 1992. At the hearing, the FTB should be prepared to explain how the elements of the duty of consistency are satisfied.[84]

Summary of Payments That Are Alleged to be Taxable on a Residency Basis[85]

Staff summarizes below its understanding of the payments received between January 1, 1992 and April 3, 1992, and the payments asserted by the FTB to be taxable on a residency basis if the Board sustains the FTB's determination that appellant remained a California resident through April 2, 1992.

January 14-15, 1992 - $23,866,465.55 of Income. Both parties agree that this $23,866,465.55 amount is included in appellant's taxable income if he is found to be a California resident on these dates. Appellant states he received this amount from Philips, out of proceeds that Philips received from Sharp, Sony, and NEC. The FTB argues that appellant received these amounts from Sharp, Sony, and NEC in December of 1991 when these companies made payments to a trust account which the FTB argues appellant controlled. However, the FTB argues that "since appellant reported this income on his 1992 federal tax return, under the duty of consistency, FTB attributes this income to January 14, 1992." (FTB Feb. 19, 2013 Br., pp. 20-22.) Appellant argues that he did not control the trust agreement and that he only received his share of the payments after Philip's share of the proceeds and expenses were taken out. (App. First Add'l Br. Apr. 10, 2013, p. 8.)

January 14, 1992 and January 24, 1992 - $50,000 of Income. This is the sum of the two

[84] If the Board finds the duty of consistency applies, the FTB should be prepared to discuss when in 1992 the two $25,000 payments should be treated as received. It is not clear to staff why the FTB treats these amounts as received on January 14, 1992 and January 24, 1992, as opposed to some other dates during 1992 or some pro rata apportionment methodology.

[85] Other payments received during 1992 are outlined above, under "Background" for this issue.

$25,000 payments discussed above.

January 24, 1992 or February 12, 1992 - $52,861 of Income. The parties agree that $52,861, which is related to Sharp, is taxable on one of these dates, but disagree which is the applicable date.[86]

January 31, 1992 or February 3, 1992; $1,699,213 of Income. The parties agree that this amount, which is a payment from Oki, is taxable on one of these dates.[87]

(The FTB's assessment determined that appellant was a resident through April 2, 1992.)

July 9, 1992; $200,000 of Income. This is an annual Philips payment. As noted above, the FTB argues that it is taxable on a residency basis even though it was received after April 2, 1992.

November 13, 1992 or November 17, 1992; Second Oki Payment; $1,275,000. Appellant argues that this amount was received on the latter date. As noted above, the FTB has included this payment as a payment that would be subject to tax on a residency basis if the Board sustains the FTB's residency determination.

Sourcing Law

In its Concluding Summaries, the FTB emphasizes that the licensing income at issue should be sourced to California on the ground that appellant's patents had a business situs in California under R&TC section 17952.[88] The general rule is that income from an intangible, such as a patent, follows the domicile of its owner.[89] Thus, in the absence of an exception to this general rule, if a nonresident receives income from stock, or from intellectual property licensed under a licensing

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[86] The FTB argues that it is taxable on January 24, 1992, on the basis that it went into a trust account on that date, which the FTB contends that appellant controlled. Appellant argues that he did not receive his share of the proceeds from the trust account until February 12, 1992. It appears to staff that this timing difference is irrelevant unless the Board determines that appellant moved to Nevada on or between the two dates.

[87] The FTB argues that it was recognized as taxable income on the earlier date, when it was sent to the trust account, while appellant argues he did not receive his share of the proceeds until February 3, 1992.

[88] See the sourcing discussion beginning on page 22 of the FTB's 1991 Concluding Summary and on page 11 of its 1992 Concluding Summary. Also, the FTB's 1992 NOA states that that the assessment is "further and alternatively sustained" on the basis that appellant's intellectual property had a business situs in California. However, as noted below, the FTB has also argued that appellant's income constitutes California source income under R&TC section 17951 and Regulation 17951-4 on the ground that appellant operated a business out of California. (*See, e.g.*, FTB 1992 July 16, 2014 Br., pp. 22-24.)

[89] *Miller v. McColgan* (1941) 17 Cal.2d 432, 443; *Christman v. Franchise Tax Board* (1976) 64 Cal.App.3d 751, 758-759; Rev. & Tax. Code § 17952; Cal. Code Regs., tit. 18, § 17952.

agreement, that income is not taxable by California.

However, there is an exception to the foregoing general rule where an intangible has a "business situs" in California. Under Regulation 17952, intangible property has a business situs in California "if it is employed as capital in this State or the possession and control of the property has been localized in connection with a business . . . in this State so that its substantial use and value attach to and become an asset of the business . . . ." The regulation provides two examples of intangible property acquiring a business situs: (1) the pledge of an intangible by a nonresident as security for debt of a California business and (2) a bank account at a California branch office that is used to pay expenses in California. In *Holly Sugar Corp. v. McColgan* (1941) 18 Cal.2d 218, 224, the California Supreme Court explained that business situs arises from the owner of the intangible employing the intangible "as an integral portion of the business activity of the regular place, so that it becomes identified with the economic structure of that place and loses its identity with the domicile of the owner."

With the foregoing in mind, the question with regard to R&TC section 17952 is whether the patents and applications for patents licensed by appellant were employed by appellant as an integral part of a California business so that the "substantial use and value" of the property constituted an asset of the California business. As noted above, the question only arises during time periods when appellant was not a resident of California. Therefore, in order for the business situs exception to apply, appellant must have used the intellectual property as an integral part of a California business while he was residing in Nevada. At the hearing, the parties should be prepared to discuss whether the evidence indicates that, during any periods when appellant was a Nevada resident, he employed the patents as an integral part of a California business.

The FTB has also argued that appellant's income had a California source under R&TC section 17951 and Regulation 17951-4 on the basis of the FTB's contention that appellant operated a California licensing business.[90] At the hearing, the parties should be prepared to address whether a preponderance of the evidence indicates that, during any periods in which appellant was a Nevada

[90] See, e.g., FTB 1992 July 16, 2014 Br., pp. 22-24; FTB 1992 Reply Br., pp. 20-22.

resident, he operated a California business, and whether the licensing payments received were earned in the operation of any such business.

Burden of Proof

At the hearing, the parties should be prepared to discuss whether the burden of proof should shift to the FTB for some or all sourcing issues. However, as both parties have provided substantial evidence, if the Board determines that either party has established by a preponderance of the evidence that the party should prevail, then the burden of proof would be irrelevant. (*See Steiner v. Comm'r*, T.C. Memo. 1995-122 [stating that the burden of proof is "merely a 'tie-breaker''].)

ISSUE (3): Whether the FTB has shown that it properly imposed a penalty for fraudulently failing to file a tax return.

Background

On April 10, 1997, the FTB notified appellant that the FTB reviewer determined to impose a fraudulent failure to file penalty. (FTB Feb. 19, 2013 Br., p. 13, Ex. EE, Tab 24.).

On August 14, 1997, the FTB issued its 1992 NPA, which stated that the fraudulent failure to file penalty was being assessed in accordance with R&TC section 19131, subdivision (d). On November 1, 2007, respondent issued a Determination Letter for both the 1991 and 1992 tax years in which respondent stated that it would affirm the NPA for 1992 as well as the NPA for 1991. The Determination Letter reflected that a fraud penalty would be imposed.[91]

On December 26, 2007, respondent issued its 1992 NOA. The NOA affirmed the NPA, including the fraud penalty. The NOA referenced the November 1, 2007 Determination Letter for further information. (FTB Op. Br., p. 1, Ex. A, Tab 4 (FTB 28811 [NOA]).)

Contentions – Issue (3) – Fraud Penalty

Appellant's Contentions

Appellant argues that the FTB imposed fraud penalties "in bad faith" in order to "coerce settlements." Appellant further argues that "[t]he fraud penalties are based on 10 trumped up factors that

[91] The NPA is attached as Exhibit EE, Tab 2, of the FTB's February 19, 2013 additional brief. The determination letter can be found at Exhibit A, Tab 4, of respondent's 1991 opening brief. (The determination letter is located after the NOAs, and the fraud penalty is discussed at pages 26 – 29. In support of the fraud penalty, the letter argues, among other things, that appellant backdated the sale of his California home and misrepresented that Ms. Jeng paid a $15,000 deposit.)

are based on false inferences, speculation and false statements that ignore Mr. Hyatt's eyewitness testimony and documentary evidence." Appellant contends that the FTB has failed to meet its burden of proving fraud by "clear and convincing evidence." Appellant asserts that the FTB "maintains its fraud penalty on its $24 million error[,]" even after admitting the error. (App. 1992 CS, pp. 5-6; see also App. 1992 Reply to FTB CS, p. 12.)

Appellant contends that the "FTB must not be allowed to violate the established law and regulations for conducting audits, assessing taxes, and appealing tax assessments as it is attempting to do here." Appellant further contends that the FTB's audits "have lasted over 20 years into 2016, and [that] FTB has intentionally delayed the administrative process into 2016." Appellant argues that "[m]ost of the current assessments are not in the NPAs or NOAs, have not been audited or protested, [and] are in large part based on an admitted $24 million error that FTB has admitted to but has still not conceded." Appellant argues that the fraud assessments are "tainted" by FTB's "abusive policy of using the fraud penalty to coerce . . . settlements even though [the] FTB audit reviewers were not convinced of fraud." (App. 1992 CS, p. 6; see also App. 1992 Reply to FTB CS, p. 13.)

Appellant argues that the "1992 fraud penalty is particularly arbitrary because FTB improperly based the 1992 fraud penalty on the 1991 facts and because FTB did not audit for 1992 . . . ." Appellant further argues that "[t]here was no taxpayer fraud" as he sold his California house and "continues to live in Las Vegas." Appellant asserts that the FTB mischaracterizes his "desire for privacy as fraudulent intent" by, for example, characterizing "the purchase of his Las Vegas Tara home in a trust as fraudulently concealing assets despite the fact that the home was disclosed on his tax return and in the audit file[]." (App. 1992 CS, p. 6; App. 1992 Reply to FTB CS, p. 13.)

Appellant contends that "[o]verwheming documentary and testimonial evidence establishes that Mr. Hyatt moved to Las Vegas and that he believed that he was a Nevada resident and he was a Nevada resident." Appellant further contends that the "FTB has never assessed a fraud penalty on the sourcing assessments" and that the 1991 accuracy-related fraud penalty and the 1992 failure to file fraud penalty "are significantly different penalties." Appellant asserts that he "had a reasonable cause and good faith belief that he satisfied the legal requirements for Nevada residency for the 1991 disputed period and all of 1992" and further that he did satisfy the requirements and still resides in

Nevada. (App. 1992 CS, pp. 6–7; see also App. 1992 Reply to FTB CS, p. 13.)

Appellant argues that the 1992 fraud penalty was an "afterthought[,]" noting that FTB employee Carol Ford stated "[w]e determined the 1992 fraud penalty should be assessed for 1992, since the facts and circumstances were the same as 1991." Appellant further argues that the "material" for the 1992 penalty was taken from "the 1991 fraud penalty write-up[,]" and that "[t]here is nothing in the record showing any independent grounds for imposing the fraud penalty for 1992." Appellant contends that the FTB has failed to show "the specific intent to evade a tax believed to be owing." (App. 1992 CS, p. 7; see also App. 1992 Reply to FTB CS, p. 13.)

Appellant argues that this "is a case of FTB fraud." Appellant asserts that "[t]he simple fact that the FTB audit reviewers were not convinced of fraud should be dispositive of the fraud penalties." Appellant further argues that ". . . all of FTB's experts on its audit task force, including the legal auditor, were doubtful about FTB's residency cases and FTB made a sourcing assessment that is inconsistent with its residency assessment." (App. 1992 CS, p. 8.)

Appellant asserts that the FTB initially set forth its fraud penalties with "false fraud factors" that have subsequently been "dropped." Appellant also asserts that the FTB failed to follow the statutory requirements for assessing the penalty in the NPAs because the 1991 and 1992 NPAs "recite" only the statute without citing reasons as required by R&TC section 19034. (App. 1992 CS, p. 8.)

Appellant argues that the FTB "provides only generalized argument instead of clear and convincing evidence." Appellant further argues that the *Appeal of Robert F. and Helen R. Adickes*, 90-SBE-012, decided November 27, 1990 (*Adickes*), is "not relevant" because "Mr. Hyatt actually moved to Nevada[,]" "[t]here is no issue of fabricated documents and Mr. Hyatt's three CDE [Contemporaneous Documentary Evidence] affidavits authenticate and explain thousands of documents." Appellant further argues that the testimony of 150 eyewitnesses "cannot be overcome by FTB's false inferences and speculation." (App. 1992 CS, p. 9.)

Appellant discusses each of 10 factors cited by the FTB in favor of its fraud penalty and argues that the factors do not establish fraud.

First Factor. Appellant argues that his alleged "physical presence" in California does not support a fraud penalty because his "overwhelming presence was in Las Vegas . . . [,]" pointing to the

testimony from 72 witnesses that he moved away. Appellant argues that, out of 190 days in the disputed period, he had "125 full days in Nevada, 37 days partly in Nevada and partly in California (each time for a temporary or transitory purpose) and 9 full days in a California hospital as he recovered from a cancer surgery." (App. 1992 CS, pp. 9-10.)

Second factor. Appellant argues that the sale of his former California home "on October 1, 1991 was a bona fide sale, not a sham as falsely alleged by FTB . . . ." Appellant further argues that "two former elected Orange County assessors . . . have confirmed that the sale of [his] former La Palma house on October 1, 1991, was a bona fide sale." Appellant contends that dozens of witnesses testified about his move from La Palma. (App. 1992 CS, p. 10.)

Third factor. Appellant asserts that he "did not suppress evidence of his stay at the Continental Hotel as falsely alleged by FTB." Appellant further asserts that "[b]ecause he was part of a van tour the Continental Hotel did not register van tour guests and made no record of [his] stay . . . ." Appellant states that hotel employees "all testified that tour guests did not register . . . and thus the hotel did not maintain records of tour guests[,]" and thus argues that there were no records of his stay to suppress. (App. 1992 CS, pp. 10-11.)

Fourth factor. Appellant argues that he did not conceal or destroy DNC corporate records. He further argues that DNC "was known to all three auditors . . . and [it] was secretly audited by FTB." (App. 1992 CS, p. 11.)

Fifth factor. Appellant argues that, contrary to the FTB's assertion, he and his representatives cooperated at audit and protest and further contends that "[a]ll three auditors as well as three protest hearing officers all concurred that Mr. Hyatt cooperated at audit." (App. 1992 CS, p. 11.)

Sixth factor. Appellant contends that he "produced extensive records to support his 1991 tax return and did not produce inadequate records as falsely alleged by FTB." Appellant further contends that the FTB disregarded much of the records "and then assessed a fraud penalty in large part because it claimed that records that were in the audit file were not produced." Appellant also asserts that he "kept adequate records of his moving expenses because he moved himself by pulling a trailer to Las Vegas and thus had no records of moving expenses." (App. 1992 CS, p. 11.)

Seventh factor. Appellant argues that he did not abuse the corporate form and that

neither he nor DNC "deducted personal expenses as business expenses . . . ." (App. 1992 CS, p. 11.)

Eighth factor. Appellant argues that he properly reported his 1991 income on his 1991 part-year tax return and he did not fail to report income. He further argues that he "properly reported the $200,000 and $400,000 payments he received from Pioneer and Philips during 1991 on his 1991 part year tax return." (App. 1992 CS, p. 11.)

Ninth factor. Appellant contends that he "provided truthful and accurate statements to the government and does not have a propensity to make false statements as falsely alleged by the FTB." Appellant further contends that he properly registered to vote in Nevada and that Mr. Zuzak "has refuted Mr. Dameron's false hearsay statement that Mr. Zuzak told him Mr. Hyatt was on Jennifer Circle in October 1991." (App. 1992 CS, p. 11.)

Tenth factor. Appellant disputes the FTB's allegation that he solicited false testimony, arguing that his witnesses did not offer false testimony and that the FTB offered "no evidence that Mr. Hyatt was even present at any witness interviews." (App. 1992 CS, p. 12.)

FTB's Contentions – Issue (3) – Fraud Penalty

The FTB disputes appellant's contention that facts regarding 1991 are not relevant to the 1992, arguing that appellant's contention "is contradicted by the fact that his own briefs contain discussion of 1991 events in the 1992 tax year." The FTB argues that during 1992 appellant "continues to pursue his business plan to extract licensing income . . . and conducts that pursuit, and every other significant aspect of his life, from the Orange County area of California." (FTB 1992 CS, p. 16.)

The FTB disputes appellant's position that he left California on September 26, 1991 to go to Las Vegas. The FTB argues that appellant's position ". . . leads to Mr. Hyatt's mystery whereabouts for the three weeks commencing September 26, the five years of waiting for the Continental Hotel explanation, the highly suspicious sale of the Jennifer Circle property and alleged occupancy of a one-bedroom unit in a low-income housing facility, and the contradictions of the change of residency assertions by contemporaneous objective documents" which the FTB argues clearly demonstrate appellant's affairs were centered in California. The FTB further argues that examples of "continuing conduct during January" include business correspondence using the Cerritos Post Office Box and Jennifer Circle telephone number, attendance at California court proceedings, "conducting a house

purchase in Nevada by means of telefax transmissions to and from the Jennifer Circle fax machine . . . [,]" banking activities, medical appointments, "meetings with his lawyers and representatives of Hitachi corporation," and a flight to and from LAX. The FTB argues that at the end of January ". . . Mr. Hyatt's long-time patent lawyer [sent] an invoice for professional services and Philips [sent] significant business correspondence to Mr. Hyatt at the Cerritos Post Office Box." (FTB 1992 CS, pp. 16-17.)

The FTB contends that "February 1992 commences with Mr. Hyatt expanding the permitted use of his Cerritos Post Office Box to include Grace Jeng and Barry Lee as designated users, and crafting Gilbert Hyatt stationary designating the Cerritos Post Office Box as his return contact information . . . ." The FTB further contends that appellant issues $2.2 million to Philips and MLMC on checks "stating he resides at Jennifer Circle, and telefaxes written instructions to Philips regarding what is to be done with his share of certain SHARP monies, instructions which incorporate the Cerritos Post Office Box and Jennifer Circle telephone and telefax numbers." The FTB also asserts that additional California activities include banking, visiting safe deposit boxes, obtaining notary services, meetings with "his patent lawyer and Encino CPA," medical appointments and an "extended in-patient stay at the Los Alamitos Medical Center[,]" correspondence from appellant's patent lawyer to appellant in California, "the USPTO utilizing the Post Office Box, Mr. Hyatt signing for a FedEx delivery from Philips at his Jennifer Circle home," and Philips sending legal and financial information to appellant "at his Jennifer Circle home." (FTB 1992 CS, p. 17.)

The FTB argues that "Mr. Hyatt's conduct remains the same in March, 1992." In support, the FTB contends that appellant continues to receive business documents from Philips at his Jennifer Circle address, faxes correspondence to Philips using California return contact information, attends meetings with his patent lawyer and doctor, speaks at an Anaheim convention, obtains a signature guarantee from his La Palma bank, opens an IRA through a San Francisco investment advisor, receives correspondence in California, and requests a tax filing extension "on behalf of DNC" which "advises he can be contacted through the Cerritos Post Office Box." The FTB asserts that Mr. Hyatt also pursues his purchase of the Tara property with faxes exchanged using his Jennifer Circle fax machine. (FTB 1992 CS, pp. 17-18.)

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Applicable Law – Issue (3) – Fraud Penalty

R&TC section 19131, subdivision (a), imposes a penalty if a taxpayer fails to file a return on or before the due date for the return.[92] Subdivision (d) of that section provides that, if any failure to file is fraudulent, the penalty to be imposed shall be 15 percent of the tax for each month after the due date until the return is filed but the total penalty shall not exceed 75 percent of the tax.

The burden is on the FTB to prove, by clear and convincing evidence, that appellants have committed civil fraud. (See, e.g., *Adickes*, *supra*, 90-SBE-012, Nov. 27, 1990; *Appeal of Barbara P. Hutchinson*, 82-SBE-121, June 29, 1982.) "Clear and convincing" has been defined as "explicit and unequivocal," leaving "no substantial doubt," and "sufficiently strong to command the unhesitating assent of every reasonable mind." (*Adickes*, *supra*.)

Fraud implies bad faith, intentional wrongdoing, and a sinister motive; the taxpayer must have the specific intent to evade a tax believed to be owed. (*Jones v. Comm'r* (5th Cir. 1958) 259 F.2d 300 (*Jones*); *Powell v. Granquist* (9th Cir. 1958) 252 F.2d 56.) Fraud may be proved by circumstantial evidence, and the taxpayer's entire course of conduct may establish the requisite fraudulent intent. (*George v. Comm'r*, T.C. Memo. 2015-158.) "Because fraudulent intent is rarely established by direct evidence, [the Ninth Circuit] has inferred intent from various kinds of circumstantial evidence." (*Bradford v. Comm'r* (9th Cir. 1986) 796 F.2d 303, 309.) These badges of fraud include: (1) understating income; (2) inadequate records; (3) failure to file tax returns; (4) implausible or inconsistent explanations of behavior; (5) concealing assets; and (6) failure to cooperate with tax authorities. (*Id*.) Although fraud may be established by circumstantial evidence, it is never presumed or imputed, and it will not be sustained upon circumstances that at most create only a suspicion of fraud. (*Jones*, *supra*, 259 F.2d at p. 303.)

STAFF COMMENTS – ISSUE (3) – FRAUD PENALTY

In order to prevail on this issue, the FTB will need to show, by clear and convincing evidence, that appellant, acting in bad faith and with an intent to deceive and evade tax believed to be owing, intentionally failed to file a 1992 California tax return. (See *Jones*, *supra*, 259 F.2d 300, 303;

[92] This provision became operative on January 1, 1994. Prior to that date, and during 1991 and 1992, the same language was set forth in R&TC section 18681, subdivision (d). The renumbering of the provision is irrelevant to the substantive issues.

Adickes, *supra*, 90-SBE-012.) Thus, the FTB will want to show that appellant knew he had a filing obligation for 1992 and, in an effort to deceive, chose not to file a California tax return in order to evade tax. As noted above, "clear and convincing" has been defined as "explicit and unequivocal," leaving "no substantial doubt," and "sufficiently strong to command the unhesitating assent of every reasonable mind." (*Adickes*, *supra*.)

ISSUE (4): Whether appellant has shown a legal basis for the abatement of interest under R&TC section 19104.

Background

The following timeline and background information primarily notes events that are directly or indirectly referenced by the parties in connection with interest abatement arguments. It does not constitute an exhaustive chronology and by listing an event staff does not express an opinion as to whether the event is legally relevant to the interest abatement analysis. In some cases, documents are not clear as to which tax year is being discussed, or discuss both years.[93]

On February 13, 1996, the FTB auditor determined that appellant received approximately $51 million during the beginning of 1992. (FTB Feb. 19, 2013 Br., p. 12, Ex. EE, Tab 3.)

On April 1, 1996, the auditor sent appellant a tentative Determination Letter that included a schedule which carried over the determination that approximately $51 million had been received by appellant early in 1992. (FTB Feb. 19, 2013 Br., p. 12, Ex. EE, Tab 18.)

On June 18, 1996, the FTB auditor closed the case and submitted it for approval. (App. 1992 Op. Br., p. 72 & Annex V, H02377.)

On August 12, 1996, the case was initially reviewed by Ms. Carol Ford and submitted to Ms. Penelope Bauche for changes. On December 12, 1996, the fraud penalty was reviewed. On April 4, 1997, Ms. Ford emailed Ms. Bauche stating that Sheila Cox had been following up regarding the Hyatt matter and outlined the prior reviews noted above. Ms. Ford states that Sheila Cox was unhappy "to take the heat" for a $2 million error in tax and then the penalty "but also with having the case sit around

[93] According to a timeline provided by the FTB, between 1996 and 2008, the FTB issued sixteen Information Document Requests (IDRs). (FTB 1992 Op. Br., Ex. H, Tab 36.) However, as the exact dates of the IDRs are not clear from the timeline, they are not listed below unless staff located a separate document or reference to the date of the IDR.

for so long." Ms. Ford stated that Ms. Cox had wondered if it had anything to do with "sitting on" cases to close them after the end of the fiscal year, and that Ms. Ford stated she replied that she had "nothing to do with the decision . . . ." (App. 1992 Op Br., Ex. 73 [referencing the reviews noted above].)[94]

On April 10, 1997, the FTB sent revised schedules including a fraud penalty. (FTB Feb. 19, 2013 Br., p. 13, Ex. EE, Tab 24.)

On May 1, 1997, FTB hearing officer Anna Jovanovich logged that she had called Mr. Cowan to confirm that he wished to consolidate the protests, which is what Mr. Cowan apparently told an auditor. She stated that she could halt the review of 1991 until she received the 1992 file. She stated that he requested she complete her review of 1991 as soon as possible as he argued she would then accept appellant's position and there would be no need to consider 1992. She states that she anticipated completing her review (perhaps referring to the 1991 year) by mid-May, barring interruptions. She further states that he had indicated a dispute regarding the audit computations and she suggested that he include that dispute in his letter of protest. (FTB 1992 Op. Br., p. 45, fn. 131 & Ex. H, Tab 22.)[95]

According to the FTB, on May 12, 1997, Ms. Cox sent a letter stating that the case was being sent for the issuance of a NPA. (FTB 1992 Op. Br., p. 34 [describing May 12, 1997 letter].)

On May 28, 1997, Ms. Jovanovich logged that she had left a voicemail for appellant's representative that she had been interrupted by another case but was back reviewing his client's case and anticipated completion in June. It appears that she was referring to the 1991 year. (FTB 1992 Op. Br., p. 45, fn. 131 & Ex. H, Tab 22.)

On June 12, 1997, FTB hearing officer Anna Jovanovich logged that she spoke at length with appellant's representative, Mr. Cowan. She states that she described the protest process and settlement possibilities. She states she explained the need for extensive letters and investigation and that she would be a sending lengthy letter asking for documentation. She notes that he reiterated that his

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[94] The FTB states that, "[a]ccording to the testimony of audit supervisors, administrators and managers who would have intimate knowledge of the processing of Mr. Hyatt's audit, it was not delayed for purposes of meeting any perceived fiscal goals." (FTB 1992 Op. Br., pp. 33-34, Ex. H, Tab 11 [testimony of Ms. Bauche] & Tab 12 [testimony of Ms. Ford].)

[95] There are two entries for May 1, 1997, one referencing a voicemail and another referencing a conversation with appellant's representative.

client wished for the 1991 year to be finished first rather than waiting to consider it with 1992. (FTB 1992 Op. Br., p. 45, fn. 131 & Ex. H, Tab 22 [p. 75 of the PDF].)

On July 17, 1997, appellant responded to the FTB's April 10, 1997 audit report. Appellant stated that the report incorrectly shows that he received $48,780,951 from Philips on January 15, 1992 when in fact this amount represents the entire amount received by him from Philips during all of 1992. (App. 1992 Op. Br., p. 54, fn. 274 & Annex V, H 02257.)

On August 6, 1997, Ms. Jovanovich logged that appellant's representative had called inquiring regarding status and she advised that "several interruptions and a week's vacation" had delayed her review but that she is now returning to her review. She stated that he could call her supervisor if he had concerns. (FTB 1992 Op. Br., p. 45, fn. 131 & Ex. H, Tab 22.)

On August 14, 1997, the FTB issued its 1992 NPA. (FTB 1991 Op. Br., Ex. A, Tab 2.)

On September 4, 1997, Ms. Jovanovich logged that she spoke at length with the representative and suggested that he quickly file a protest and then request disclosure. She stated that she told the representative that she would be sending a lengthy letter that would probably cover parts of 1992. (FTB 1992 Op. Br., p. 45, fn. 131 & Ex. H, Tab 22.)

On October 10, 1997, appellant protested the NPA.[96]

On December 3, 1997, appellant's representative, Mr. Cowan, wrote a memo to the file stating that Ms. Jovanovich had told him that she was delayed in reviewing appellant's 1991 file because she had been assigned other cases. (App. 1991 Op. Br., p. 92, fn. 506, Ex. 93.)

On November 21, 1997, Ms. Jovanovich logged that she spoke at length with appellant's representative regarding the time plan for the protest. She wrote that they both agreed it would be "more efficient" to handle the 1991 and 1992 years together and for requests and answers to go out at one time for both years. She stated that his protest letter had been sent to the Legal Department where it "sits" in her supervisor's office and should be assigned shortly. She further stated that "now" would be a good time for him to request disclosure, while she is reviewing 1991, as it will take time to finish that review, which is going "MUCH slower than I originally anticipated – both due to its complexity & unexpected

[96] FTB 1992 Op. Br., Ex. H, Tab 25 [protest]; see also App. Annex V, 01_H_Bates_from_H00241.pdf.

interruptions."[97]

On January 6, 1998, appellant sued the FTB in Nevada.[98]

On January 8, 1998, Ms. Jovanovich logged that she called appellant's representative to confirm the receipt of the file. He stated that he had requested the disclosure of documents for the 1992 tax year on December 11, 1997. She stated that she told him that, if the Disclosure Department does not borrow the file, she will finish the review of the 1991 file in a few days and begin the review of 1992 and then the Disclosure Department could have the file when she finishes. She stated that he seemed "agreeable" to the plan and emphasized that he wanted to do whatever was quickest in terms of proceeding at protest. (FTB 1992 Op. Br., p. 45, fn. 131 & Ex. H, Tab 22.)

On January 14, 1998, according to the FTB call records, the FTB left a voicemail for appellant's representative stating that its Disclosure Office took the 1992 file but left a copy with protest and that the FTB would be giving the protest "top priority (barring litigation) . . . ." (FTB 1992 Op. Br., p. 45, fn. 131 & Ex. H, Tab 22.)

On March 17, 1998, appellant's attorney Mr. Cowan sent a memo to appellant and his team that, "[w]hile there are no 'pure' tax reasons to quash [an FTB subpoena for banking information], there may be tactical reasons to do so (such as making the FTB work for its requests [from] now on or taking this opportunity to file the motion in the Nevada courts or otherwise) . . . ." (FTB 1992 Op. Br., pp. 49-50 & Ex. E, Tab 38.)

On March 18, 1998, FTB attorney Terry Collins submitted an affidavit in Nevada court stating that the FTB "intends to continue processing, and continues to process, Mr. Hyatt's protests . . . despite his filing of [the Nevada] legal action . . . ." (App. 1992 Op. Br., Ex. 65.)

In March or April of 1999, FTB employee Carol Ford erased files related to appellant, according to her testimony. (App. 1992 Op. Br., p. 9, fn. 33 [citing testimony of Ms. Ford].)

According to the FTB, in December 1999, the FTB issued an IDR to appellant, and

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[97] FTB 1992 Op. Br., p. 45, fn. 131 & Ex. H, Tab 22 (see Nov. 19 and Nov. 21 entries on page 71 of the PDF).

[98] FTB 1992 Op. Br., Ex. A, Tab 11. In addition to seeking damages for various torts, appellant's complaint sought declaratory relief confirming his status as a Nevada resident from September 26, 1991 to the present.

appellant requested six months to reply.[99]

On December 27, 1999, the Nevada court adopted a protective order allowing appellant to designate information as confidential information which could not be shared outside of the FTB's litigation team except in certain circumstances.[100]

On March 7, 2000, FTB employee Charlene Woodward sent FTB supervisor George McLaughlin a memo attaching a copy of a memorandum she wrote to Terry Collins analyzing a protective order that had been issued in the Nevada litigation. The memo states in part that Ms. Woodward "made a preliminary attempt to organize the materials" but that they could not take further action until they received complete audit files. The memo further states that "[w]e will effectively be creating a parallel universe of information . . . [,]" and cautions that "[w]e will not be discussing the case with the litigation attorneys . . . ." The memo also states that "[i]n all other respects, we need to proceed with the protest as if there were no litigation – our actions on protest must not be held hostage to the litigation, to the extent we can avoid it." The letter attached to the memo is addressed to Terry Collins from George McLaughlin (but evidently drafted by Ms. Woodward) and describes procedures to be followed to comply with the protective order, including the identification by litigation attorneys of confidential information, who would then request that Mr. Hyatt voluntarily consent to the disclosure of such information and, if such consent is not provided, could issue an administrative subpoena. Also on March 7, 2000, Mr. McLaughlin provided Charlene Woodward with a copy of his memo to Mr. Collins and stated that ". . . we can take no further action, until we get the complete audit files."[101]

On April 3, 2000, FTB supervisor George McLaughlin entered into the log a "Request for Audit Support." The entry states that this is a "high profile" residency case that is "the companion to the 'high profile' federal litigation case in Nevada." It further states that "[t]he protest has been on hold for

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[99] FTB 1992 Op. Br., p. 50. Staff could not locate a copy of the IDR or appellant's response.

[100] FTB 1992 Op. Br., p. 50 & Ex. H, Tab 27. The order had been prepared on December 3, 1999 by a "Discovery Commissioner."

[101] FTB 1992 Op. Br., p. 37, Ex. H, Tab 14; App. 1992 Op. Br., Exs. 69 (letter from Mr. McLaughlin to Ms. Woodward) & 68 (memo from Mr. McLaughlin to Mr. Collins).

awhile, but is now active – and we intend to close it by March 3, 2001. It adds that there is an IDR outstanding with an extended due date of June 30, with protest hearings set for September 27 and October 4. It requests the assignment of an auditor to work with FTB employee Charlene Woodward.[102]

On April 11, 2000, the FTB filed a motion to vacate the protective order. (App. 1992 Reply Br., Ex. 24 [hearing transcript referencing the motion to vacate].)

On May 24, 2000, appellant's CPA Mike Kern was deposed in the Nevada litigation and stated that appellant initially moved into the Continental Hotel.[103] According to the FTB, this was the first time appellant had informed the FTB of his assertion as to where he initially moved to in Nevada. Appellant apparently placed that deposition under the Nevada protective order.[104]

On May 30, 2000, Ms. Cinnamon logged that she did not have the original protest record, including the protest letter. She states that, when she is done with the audit record, she will "pursue reconstructing a facsimile of the historical protest record" if needed. (App. 1992 Op. Br., Ex. 70.)

On June 7, 2000, the Nevada Supreme Court issued a temporary stay with regard to the protective order.[105]

On September 11, 2000, Ms. Cinnamon requested to Mr. Miller that any missing audit files be sent to her. (App. 1992 Op. Br., Ex. 67.)

On September 13, 2000, the Nevada Supreme Court issued an order clarifying the temporary stay it issued on June 7, 2000, stating that the order was intended to stay all proceedings in the district court.[106] (FTB 1992 Op. Br., Ex. H, Tab 30.)

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[102] FTB 1992 Op. Br., Ex. H, Tab 13; App. 1991 Op. Br., Ex. 80; App 1992 Op. Br., Ex. 60.

[103] FTB Op. Br., pp. 50 – 51, Ex. C, Tab 34.

[104] FTB 1992 Op. Br., p. 51, Ex. C, Tab 34. Mr. Kern's testimony is marked "Confidential – NV Protective Order."

[105] FTB 1992 Op. Br., Ex. H, Tab 30. This document is a Nevada Supreme Court order dated September 13, 2000, which references the earlier order. Appellant argues that the stay only stayed the production of documents claimed to be privileged by the FTB and that the protective order did not restrict the ability of the FTB to obtain documents under California law. (App. 1992 Reply Br., p. 85, fn. 550.)

[106] Appellant argues that the stay only stayed the production of documents claimed to be privileged by the FTB and that the NPO did not restrict the ability of the FTB to obtain documents under California law. (App. 1992 Reply Br., p. 85, fn. 550.)

On September 27 and October 4, 2000, protest hearings were held.[107]

On October 10, 2000, Mr. McLaughlin sent a memo stating in part that the audit files have been "a significant problem" and that "[w]ith the Herculean effort by Cody Cinnamon, we were able to determine that we have some semblance of the complete audit file – recognizing that there are still gaps that can't fully be accounted for and redactions/omissions that are related to the confidential/privilege issue." Mr. McLaughlin requested that a complete file by sent to Mr. Hyatt's counsel, who had requested it. (App. 1992 Op. Br., Ex. 66.)

On December 14, 2000, FTB attorney Cody Cinnamon sent Mr. Hyatt additional IDRs for both 1991 and 1992. (App. 1992 Op. Br., Ex. 59 [February 28, 2000, letter from Mr. Coffill responding].)

On February 2, 2001, appellant filed a 132-page protest supplement letter. (App. 1992 Op. Br., p. 63 & Annex IV.)

On February 28, 2001, appellant's counsel responded to Ms. Cinnamon's December 14, 2000 letter and stated in part that Ms. Cinammon had stated a timetable for resolving the protest by the end of the first quarter in 2001. (App. 1992 Op. Br., Ex. 59.)

On April 26, 2001, Terry Collins sends a letter to Mr. Cinnamon stating that, while the Nevada Supreme Court is deliberating, they will not take action which might cause Mr. Hyatt to file additional requests with the court and will not request permission to disclose materials covered by the protective order. Mr. Collins states that there are "many documents relevant to the protest that we are unable to furnish at this time . . ." and "strongly suggest[s] . . . that you need to review these additional documents prior to making your decision. [emphasis in original]" The letter states that the Nevada Supreme Court held oral argument on February 5, 2001 and that it takes, on average, about four months for a decision to be rendered. (FTB 1992 Op. Br., Ex. H, Tab 31.)

On June 13, 2001, the Nevada Supreme Court ordered summary judgment in favor of the FTB. Later, on April 4, 2002, the Nevada Supreme Court vacated its prior ruling. (*FTB v. Hyatt* (2003)

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[107] As noted previously, the FTB argues that both hearings covered both years while appellant contends that the 1991 protest hearing was held on October 4 and the 1992 protest hearing was held on September 27, 2000. (See FTB 1992 Reply Br., p . 81; App. 1991 Op. Br., p. 88; App. 1992 Op. Br., p. 68.)

538 U.S. 488, 492 [referencing the June 13, 2001 ruling].)

On June 15, 2001, appellant apparently sent a letter to Ms. Cinnamon stating that there were no pending document requests.[108]

On January 17, 2002, there was a hearing in the Nevada District Court regarding an FTB motion to vacate the protective order, and the court stated that it did not think that the Nevada Supreme Court intended for its stay to have the broad application that was being sought. (App. 1992 Reply Br., p. 85, fn. 550 & Ex. 23.)

On February 20, 2002, Ms. Cinnamon emailed Mr. McLaughlin stating that she had stated to appellant's representative that she had been "instructed not to work on the case due to the pending Nevada litigation." (App. 1992 Op. Br., p. 69, Ex. 63.)[109]

On March 7, 2002, appellant's representative at that time, Eric Coffill, sent a letter to the FTB stating that FTB supervisor George McLaughlin had informed the representative that the protests were not being worked on because of the pending Nevada litigation. Mr. Coffill stated that he had telephoned the FTB because "we had not heard from FTB for over seven months" and also stated that there were no pending document requests. Appellant's counsel further stated that FTB attorney Cody Cinnamon had told him that she had not charged time on the protests since June 2001 and that Mr. McLaughlin had told the representative that the protests are "written up" and that determination letters could be issued quickly once the case was activated. (App. 1992 Op. Br., fn. 359 & Ex. 61.)

On April 4, 2002, the Nevada Supreme Court vacated its prior ruling which had dismissed Mr. Hyatt's lawsuit. (*FTB v. Hyatt* (2003) 538 U.S. 488, 492 [referencing the April 4, 2002 ruling].)

On April 5, 2002, FTB attorney Ben Miller sent an email stating that the Nevada Supreme Court had allowed Mr. Hyatt to proceed with his intentional tort case. Mr. Miller then states:

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[108] This letter is referenced in a later March 7, 2002 letter from appellant's counsel which is attached as Exhibit 61 to appellant's 1992 opening brief.

[109] The FTB states that appellant incorrectly describes this as an email when it was a log entry. (FTB 1992 Op. Br., p. 38.) However, appellant provides a copy of the email. It may be that the communication was made by email and noted in the log.

> I think this means we should put things on hold with administrative matters, in particular the recent draft letter. This puts a new light on things and we well want to proceed under the protective order to try and get documents[.] It is clear that the protective order is [not] going away anytime in the near future.

(FTB 1992 Op. Br., Ex. H, Tab 15.)

On May 20, 2002, FTB supervisor George McLaughlin wrote to appellant's former representative Eric Coffill that Mr. Coffill's outline of events was "substantially correct." The letter also states, among other things, that the Nevada litigation had impacted protest proceedings and that the FTB had been complying with the Nevada protective order. (FTB 1992 Op. Br., Ex. H, Tab 17.)

On June 3, 2002, the California Department of Justice requested appellant's consent, under the protective order and, pursuant to R&TC section 19504, to the release of all documents and testimony marked as confidential under the protective order. (FTB 1992 Op. Br., Ex. H, Tab 32.)

On July 7, 2002, the FTB issued a subpoena requesting six categories of documents produced in the Nevada litigation. (App. 1992 Reply Br., Ex. 26.)

On July 22, 2002, appellant's counsel sent a letter to Mr. Miller regarding the subpoena issued on July 7, 2002. Appellant's counsel requests a clarification and questions the relevancy of the documents requested. (FTB 1992 Op. Br., Ex. H, Tab 33.)

According to appellant, on December 2002, the FTB destroyed backup tape data. (App. 1991 Op. Br., p. 10, fn. 36 [citing testimony].)

On February 28, 2003, the Sacramento County Superior Court issued a ruling compelling appellant to comply with the FTB subpoena as to five categories of documents, but not enforcing compliance with a sixth "catch-all" category. (FTB 1992 Op. Br., Ex. A, Tab 10 [Dec. 31, 2003 California Court of Appeal decision].)

On March 20, 2003, appellant appealed the judgment of the Superior Court. (*Id.*)

On December 31, 2003, the Court of Appeal of California, Third Appellate District, affirmed the Superior Court. The FTB states that, after the Court of Appeal decision became final, it began the process of copying and transferring the information released pursuant to the ruling.[110]

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[110] *Id.* (decision). FTB 1992 Op. Br., p. 53 (regarding the copy and transfer of files).

In or about May 2004, according to the FTB, the documents obtained through the subpoena were received by the protest hearing officer. (FTB 1992 Op. Br., p. 53.)

On August 5, 2005, an FTB attorney stated to the Nevada court that there was no evidence that the protest had been put on hold. (App. 1991 Op. Br., p. 89, fn. 492.)

On October 28, 2005, FTB attorney Bob Dunn requested appellant's consent to release documents covered by the protective order.[111]

On December 6, 2005, the FTB responded to a November 9, 2005 letter from appellant's counsel. The letter states that the FTB had not received a response to its document request, which it had expected to be provided by November 30, 2005, and that the FTB did not intend to alter its document request. (FTB 1992 Op. Br., Ex. H, Tab 34.)

On January 30, 2006, the FTB issued another subpoena for documents covered by the Nevada protective order. (FTB 1992 Op. Br., Ex. H, Tab 35.)[112]

On January 19, 2007, the FTB requested, pursuant to the Protective Order, that appellant consent to the FTB's production of litigation documents. The documents for which consent to disclosure was requested include transcripts of depositions of appellant, Grace Jeng, and many others others, appellant's 1991 and 1992 amended federal income tax returns, and documents related to an IRS audit. (FTB 1992 Op. Br., Ex. H, Tab 28.)

On November 1, 2007, the FTB sent a 50-page protest Determination Letter indicating that the hearing officer intended to affirm the NPA.[113]

On December 26, 2007, the FTB issued its NOA for 1992, which sustained the protest hearing officer's determination and refers to the November 1, 2007 Determination Letter. (FTB Feb. 19, 2013 Br., Ex. A, Tab 4.)

In January of 2008, appellant filed notices of appeal for 1991 and 1992. Both appellant and the FTB filed lengthy briefs, with many attachments, and both parties requested and received

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[111] This letter is referenced in Ex. H, Tabs 34 & 35, of the FTB's 1992 Opening Brief.

[112] According to the FTB, it did not receive the last of the documents requested until June 2007. (FTB 1992 Op. Br., p. 53.)

[113] FTB 1991 Op. Br., p. 1, Ex. A, Tab 4 [Determination letter is located after the NOAs and marked FTB 28751].

numerous extensions of time for briefing. The regular briefing process, prior to additional briefing requested pursuant to Rule 5435, subdivision (a), concluded in August of 2012 with the filing of appellant's supplemental briefs.[114]

Appellant's supplemental briefs included 93 new affidavits or declarations. On August 29, 2012, the FTB submitted over 7,000 pages of evidence it obtained from Philips. On October 5, 2012, the FTB requested that its submission be withdrawn in order to comply with a New York Supreme Court order obtained by appellant.

On January 17, 2013, and February 25, 2013, the Appeals Division requested additional briefing from the parties regarding the alleged $24 million error and the litigation in New York regarding the Philips documents. During the additional briefing process, the parties had numerous disputes regarding which Philips documents could be submitted or referenced in the briefing. In addition, during the additional briefing process, both parties requested and received numerous extensions of time for briefing.

On April 23, 2014, it appeared that the New York litigation had resolved, and the Appeals Division requested additional briefing regarding the Philips documents and affidavits submitted by appellant, and requested that each party provide a concluding summary for each appeal. From 2014 to 2016, numerous additional disputes arose regarding the briefing and the Philips documents. In March of 2015, in response to filings made by the FTB, appellant renewed litigation in New York, which was not resolved until September of 2015. Following the resolution of the litigation, the parties engaged in a process designed to reach agreement, or narrow areas of disagreement, regarding which documents could be submitted under a New York court order relating to Philips documents. After various extensions were provided, the additional briefing process concluded late in 2016.[115] An oral hearing was originally planned for March 2017 but, at appellant's request, the oral hearing was rescheduled to

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[114] Appellant filed supplemental briefs in July and August of 2012. Appellant filed corrected supplemental briefs on August 15, 2012 and provided DVDs with linked briefing on November 14, 2012.

[115] Pursuant to Rule 5435, the Appeals Division, individual Board Members, or the Board, can request additional briefing at any time. Therefore, while staff does not presently anticipate any further additional briefing, it cannot foreclose that possibility. Prior to the hearing, the parties may receive inquiries sent by the Appeals Division in response to Board Member requests.

May 2017.

As noted previously, the FTB then requested a two-month continuance due to a family medical emergency. Appellant did not object but requested that the hearings be held on the calendar commencing on August 29, 2017. In light of the foregoing, the appeals were rescheduled for the August 29, 2017 calendar.

Contentions – Issue (4) – Interest Abatement

Appellant's Contentions

In his 1992 Opening Brief and his 1992 Reply Brief, appellant requests interest abatement from August 14, 1997, the date of the NPA, through December 26, 2007, when the NOA was issued. (See App. 1992 Op. Br., p. 82.) In later briefing, appellant requests that all interest be abated based on the ruling of the Nevada Supreme Court. Appellant requests interest abatement for "the additional reason of FTB's extraordinary 11-year delay in processing the two protests[,]" and also argues that interest abatement is warranted due to actions taken by the FTB during appeal. (App. 1992 Sep. 28, 2016 Br., pp. 57-59; see also App. 1992 Reply to FTB CS, pp. 13-19.)

Appellant's 1992 Concluding Summary does not include a separate section or significant discussion regarding interest abatement. However, appellant argues that the FTB wrongly continued to impose interest in bad faith despite its $24 million error, and appellant incorporates by reference arguments made in Section 1.12 of appellant's 1991 Concluding Summary. There, appellant argues that interest should be abated based on the Nevada Supreme Court finding which appellant states found that the FTB committed fraud and the intentional infliction of emotional distress in part because of its delays. In his conclusion, appellant also argues that "[a]ny interest assessments should be abated because they resulted from intentional delay of FTB." (App. 1992 CS, pp. 1, 24; App. 1991 CS, pp. 26–27; see also App. 1992 Reply to FTB CS Reply, pp. 13 -14.)[116]

In appellant's 1992 Concluding Summary, he argues that interest abatement is appropriate under R&TC section 19104 on the basis that "[t]here have been many unreasonable delays

[116] Appellant further discusses interest abatement in his 1991 Opening Brief, at pages 88 to 90, in his 1992 Opening Brief, at pages 68 to 70, in his 1992 Reply Brief, at pages 83 to 89, in 1992 Second Additional Brief, dated September 28, 2016, at pages 57 to 59, and in his 1992 Reply to the FTB's Concluding Summary, at pages 13 to 17.

attributable to ministerial and managerial acts performed by FTB staff during the processing of the protest." Appellant further argues that the delays "are not significantly attributable to Mr. Hyatt." As examples, appellant points to "FTB intentionally plac[ing] a 'hold' on Mr. Hyatt's protest . . . [,]" FTB losing, destroying or withholding "numerous documents from audit files[,]" "FTB delay[ing] the protest by assigning the protest officer to other cases and failing to reassign Mr. Hyatt's case . . . [,]" "FTB fail[ing] to expeditiously issue the 1992 NPA . . . [,]" and "FTB's $24 million error in calculating the 1992 NPA . . . ." (App. 1992 CS, pp. 26-27; see also App. 1992 Reply to FTB CS, pp. 16-17.)

In appellant's reply to the FTB's 1992 Concluding Summary, appellant expands on interest arguments made in his 1992 Concluding Summary and replies to arguments raised by the FTB. Appellant argues that the "FTB's extraordinary 11 year delay in the processing of the protests [was] uconscionable[,]" and that the Nevada Supreme Court "upheld the jury finding that FTB personnel committed fraud in processing Mr. Hyatt's audits and protests." Appellant further argues that "[e]ven though Philips was identified in Mr. Hyatt's 1991 part year California tax return and even though FTB issued and withdrew subpoenas from Philips in 2006, FTB delayed until 2011 to actually pursue discovery from Philips[,]" and "then did so with unlawful, overbroad subpoenas that forced Mr. Hyatt to obtain a protective order from the New York courts . . . ." (App. 1992 Reply to FTB CS, pp. 13-14.)

Appellant notes that "***over 10 years*** passed between the time Mr. Hyatt received the NPA for the 1992 tax year on October 10, 1997, and FTB's issuance of the [NOA] on December 26, 2007. [appellant's emphasis]" Appellant argues that the delay "was due to the intentional misconduct of the FTB in which it refused to perform managerial and ministerial acts as required under law and affirmatively put a 'hold' on the protest process." Appellant further argues that this issue "was determined in favor of Mr. Hyatt and against the FTB in the Nevada tort case . . . [,]" citing the jury verdict and the decision in *FTB v. Hyatt* (2014) 335 P.3d 125. (App. 1992 Reply to FTB CS, p. 14.)

Appellant contends that the FTB makes "bald assertions" regarding "irrelevant" events that do not rebut his request for interest abatement. In this connection, appellant makes four arguments. Appellant first argues that his actions during protest and in the Nevada tort case did not delay the tax proceedings. In response to the FTB's argument regarding a March 17, 1998 fax from Mr. Cowan, appellant argues that Mr. Cowan did not work closely with his Nevada litigation team and that the FTB

"falsely portrays a single communication . . . as an attempt to delay the tax proceedings." Appellant further argues that ". . . the action suggested by Mr. Cowan was not followed." (App. 1992 Reply to FTB CS, pp. 14-15.)

Appellant disputes the FTB's contention that he did not respond to an Information Document Request (IDR) in 1999, arguing that he "respond[ed] to all requests . . . and produced substantial documents." Appellant contends that the FTB falsely blames the protective order issued by the Nevada court in 1999 for a delay when "it is the FTB that decided to delay the tax proceedings based on the protective order." Appellant contends that the order only restricted the use of materials in the Nevada case in the tax protest proceedings and that the FTB remained free to use its subpoena powers to obtain materials that were confidential under the protective order. (App. 1992 Reply to FTB CS, p. 15.)

Appellant argues that the FTB could have issued a penalty against him if it was not producing documents as requested but did not do so because he "complied with all its requests for documents during the tax protest proceedings." Appellant further argues that the FTB did not request a stipulation to material being turned over until June of 2002, which the FTB "argues required a court order[,]" "[b]ut most of these documents were already in the protest officer's possession, and the FTB had made no effort to determine what documents the protest officer already had when it issued the subpoena." Appellant further contends that the FTB made no further requests under the protective order until October of 2005 and then in 2007, and that these requests "were promptly answered by Hyatt with no delay caused to the FTB." (App. 1992 Reply to FTB CS, pp. 15-16.)

Appellant argues that there was a six-year delay when the FTB placed a "hold" on the proceedings and that this delay "constitutes a ministerial or managerial act." Appellant further argues that the protest officer was instructed to "hold" the protest "despite the fact she had already drafted the protest Determination Letter, pending the Nevada litigation involving Mr. Hyatt and FTB." Appellant contends that there was "no conceivable reason for this delay" as "[t]he issue of residency was not a cause of action" in the litigation. Appellant further contends that, in February of 1998, a month after appellant filed his lawsuit, FTB counsel stated under oath that the FTB intends to and continues to process appellant's protest despite the filing of his Nevada legal action. Appellant asserts that "[s]till further delay was caused by FTB when it waited 14 months after the 1992 audit was completed [on

June 18, 1996] to issue the 1992 NPA [on August 14, 1997]." (App. 1992 Reply to FTB CS, pp. 16-17.)

Appellant's second argument is that his actions in the New York litigation did not delay the tax proceedings. Appellant notes that the FTB "describes proceedings in New York regarding subpoenas it served in 2011 . . . ." Appellant argues that rather his actions causing delay as it was the FTB that "wait[ed] until 2011 to pursue the subject subpoenas" and issued "vastly overbroad requests." Appellant further argues that the New York court properly found that the subpoenas were too broad and that the FTB "appealed that issue causing additional delay." Appellant contends that the FTB violated the New York court order causing more delay "when Mr. Hyatt was forced to bring successful enforcement actions to enforce the New York court order." (App. 1992 CS, pp. 17-18.)

Appellant's third argument is that the "due process litigation" he commenced in federal District Court has not delayed proceedings. Appellant argues that "[c]ontrary to FTB's allegation, the District Court action was brought to protect Mr. Hyatt's constitutional rights because . . . the long delays in the tax proceedings caused by FTB have resulted in the deaths of witnesses, loss of memory and loss of documents." (App. 1992 Reply to FTB CS, p. 17.)

Appellant's fourth argument is that the FTB's actions have caused proceedings to be delayed from 2008 to the present. Appellant notes that the FTB argues that he received 19 extensions. However, appellant contends that the FTB "repeatedly sought and received permission for additional briefing and submission of evidence[,]" which, because appellant is entitled to file final briefing, caused an "endless cycle" of briefing. (App. 1992 Reply to FTB CS, p. 18.)

Appellant argues that his representatives "expeditiously filed" his opening briefs on December 9, 2008, "less than a year after the appeals were filed on January 22 and 23, 2008." Appellant further argues that a "great effort was required to obtain testimony from the large number of witnesses that had previously been identified to FTB but had not been approached by FTB." Appellant also asserts that the FTB raised the sourcing issue for the first time in its NOAs so that addressing sourcing issues took "[a] considerable amount of effort." Appellant also contends that the "FTB made numerous false statements and misrepresentations in its 1991 and 1992 opening briefs related to sourcing and it was necessary for Mr. Hyatt to expend considerable time and effort to rebut those numerous false statements and misrepresentations in his replies." (App. 1992 Reply to FTB CS, p. 18.)

Appellant disputes the FTB's statement that it prevailed in the New York action, arguing that the New York court "significantly limited the scope of FTB's subpoenas by excluding discovery in years 1993-1997 and by excluding irrelevant discovery of the *Hyatt v. Boone* interference." Appellant contends that the New York court "found that FTB had violated its order on multiple occasions and ordered correction of the violations." (CS Reply, p. 18.)

In conclusion, appellant argues that the FTB, not appellant, "has caused the extensive delays in the audit, protest and this appeal." Appellant further argues that "[t]he extensions of time have been necessary to deal with FTB's extraordinary briefing technique of making thousands of false statements, mischaracterizations and fabrications[,]" which require "enormous effort and thousands of pages of attachments and briefing to rebut . . . ." (App. 1992 Reply to FTB CS, p. 19.)

FTB's Contentions – Issue (4) – Interest Abatement

The FTB argues that the "many delays" are attributable to appellant and have been discussed in its opening brief for the 1992 appeal at pages 30–37 and its additional brief dated March 28, 2013 at pages 1 - 4, which it incorporates by reference. The FTB then addresses (1) appellant's protest and Nevada lawsuit (from 1998 to 2008), (2) the New York proceedings (from 2011 to 2015), (3) the federal proceedings in *Hyatt v. Betty Yee, et al.* (from 2004 to present), and (4) appeal proceedings (from 2008 to present). (FTB 1992 CS, pp. 18-23.)

The FTB first contends that appellant's tax attorney Mr. Cowan and attorney Donald Kula "worked closely" and, "with the support and concurrence of Mr. Hyatt," adopted a strategy "designed to delay the California tax proceedings by intertwining those proceedings with the Nevada litigation." In support, the FTB argues that a memorandum shows "an intent to make respondent 'work' for everything they got." The FTB further contends that Mr. Cowan acknowledged "that the litigation would have an effect on the protest."[117]

The FTB states that, in late 1999, it issued a comprehensive IDR that repeated questions "never answered at audit and requested additional documentation." The FTB states that appellant requested six months to respond. (CS, p. 19.)

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[117] FTB 1992 CS, p. 19, Endnote 98 [March 17, 1998 Cowan fax], Endnote 99 [FTB Sept. 16 1999 log entry].

The FTB argues that, on December 27, 1999, appellant obtained a Protective Order from the Las Vegas court which allowed appellant "to unilaterally designate documents . . . revealed in the Nevada litigation that could not be shared with respondent's protest hearing officer." The FTB further argues that appellant used the Protective Order "to keep relevant evidence from [its] protest hearing officer, including testimony of his Nevada accountant revealing Mr. Hyatt's alleged stay at the Continental Hotel. (FTB 1992 CS, p. 19.)

The FTB argues that the Nevada Supreme Court failed to modify the order in mid-2002 and that the FTB followed the order by asking appellant "to release designated information to the protest hearing officer for consideration in the California tax matter." However, the FTB contends, appellant refused. The FTB states that it then "issued an administrative subpoena for the information[,]" and that, in February 2003, a California Superior Court compelled appellant "to comply with all but one of the requests contained within respondent's administrative subpoena." The FTB states that appellant then appealed and the appeals court "eventually held [in 2003] that there was no reason why respondent's personnel working on the protest should have access to evidence produced by Mr. Hyatt in his Nevada litigation."[118] The FTB argues that appellant's actions "impeded the progress of the administrative tax proceedings" and contradict appellant's argument that the Nevada litigation did not interfere with the California tax proceeding. (FTB 1992 CS, pp. 19-20.)

The FTB contends that, in 2004, appellant was ordered by the Nevada court to produce documentation, but, "[d]espite the 2003 California appellate court holding, Mr. Hyatt continued to designate as confidential[] evidence relevant to his California tax protest under the Nevada Protective Order." The FTB further contends that, in late 2005, it issued a second subpoena, which appellant at first refused to provide, relenting only on the threat of litigation and ultimately providing documents in early 2006. The FTB states that it subsequently issued five additional IDRs and appellant again designated as confidential information under the Nevada Protective Order. The FTB states that "issued a third demand[,]" and that it issued its NOAs in November 2007. (FTB 1992 CS, p. 20.)

With regard to the New York proceedings, the FTB states that, in March 2011, it issued

[118] The FTB refers to *FTB v. Hyatt*, decided December 31, 2003, and available on Westlaw at 2003 WL 23100266.

subpoenas to nonparties including Philips and two of its in-house attorneys. The FTB argues that it sought discovery in response to evidence introduced in appellant's submissions in August 2010.[119] The FTB states that the subpoenas "sought documents and testimony that reflected the nature of Mr. Hyatt's patent-licensing business" and sought information for the seven-year period of the Hyatt-Philips relationship (1991 – 1997). (FTB 1992 CS, p. 20-21.)

The FTB argues that appellant then commenced proceedings to quash the subpoenas, including an emergency motion filed in New York in July of 2011. The FTB argues that, on July 27, 2011, New York Judge Lefkowitz rejected appellant's arguments that production was barred and also ruled that appellant failed to demonstrate that material regarding his residency or the licensing of his patents was irrelevant. The FTB further argues that the judge ultimately modified the subpoenas "to only include material related to tax years 1991 and 1992 with respect to the issues of Hyatt's residency and income received in those years, his relationship with [Philips], and the licensing of his patents and any revenue in 1991 and 1992." (FTB 1992 CS, p. 21.)

The FTB contends that Mr. Hyatt then appealed, and, on October 11, 2012, the New York Appellate Court stayed the FTB from filing the Philips documents with the Board pending its decision. The FTB further contends that, on March 13, 2013, the appeals court affirmed the judge's order. The FTB asserts that appellant ". . . thereafter twice renewed the court battle seeking to suppress the use of certain Philips documents, but lost." The FTB further asserts that appellant filed a contempt petition "for which Judge Lefkowitz gave him no relief." (FTB 1992 CS, p. 21.)

The FTB states that, in April 2014, appellant filed a lawsuit in federal district court of California against the members of the FTB and the Board seeking an injunction preventing further proceedings and preventing "any assessment or collection of State income taxes against Mr. Hyatt for the 1991 and 1992 years, or any subsequent years based on any of the theories that respondent has asserted against him in the currently pending administrative proceeding." The FTB notes that, on February 10, 2015, the federal lawsuit "was dismissed with prejudice[,]" and that appellant then appealed. (FTB 1992 CS, p. 22.)

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[119] As discussed below, the FTB is referring to materials filed with appellant's reply briefs.

With regard to appeal proceedings, the FTB observes that appellant filed his appeals in January of 2008 and, "after multiple extensions[,]" filed his opening briefs on December 9, 2008. The FTB argues that, in August 2010, appellant "submitted a reply brief that included new affidavits made by witnesses who had never before been identified or testified in the dispute, including an affidavit from an individual in Philips' New York [office] describing the patent negotiations . . . during the disputed California residency period and Hyatt's purported lack of involvement in those negotiations." The FTB contends that it issued its subpoenas in March 2011 "[a]s a result of these new affidavits . . . ." (FTB 1992 CS, pp. 22-23.)

The FTB asserts that it "prevailed in three suppression actions filed by Hyatt in New York with the limited exception of having the scope of the production [limited] to documents that pertain to the two tax years on appeal, i.e. 1991 and 1992." The FTB further asserts that the New York proceeding concluded in April of 2015, and it was not until April of 2016 that SBE staff issued its decision allowing respondent's briefing on the Philips documents to be considered . . . , despite Mr. Hyatt's objections . . . ."[120] (FTB 1992 CS, p. 23.)

The FTB argues that appellant has received "19 extensions to file various briefs covering more than four and a half years of additional time." The FTB further argues that appellant made extension requests during 2016 and that the delays "result from Mr. Hyatt's conscious strategy to prolong the SBE proceedings then blame respondent (and SBE) for these delays." The FTB asserts that "[i]n reality, Mr. Hyatt remains completely responsible for the protracted nature of these proceedings." (FTB 1992 CS, p. 23.)

Applicable Law – Issue (4) – Interest Abatement

Interest is not a penalty but is merely compensation for a taxpayer's use of the money. (Rev. & Tax. Code, § 19101, subd. (a); *Appeal of Amy M. Yamachi*, 77-SBE-095, June 28, 1977;

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[120] It may be that the FTB means to refer to a New York decision in April 2014. The Appeals Division promptly requested briefing following this decision, only to see further disputes arise. At various times, the FTB retracted its filings so it could replace them with further redacted filings intended to address confidentiality concerns and disputes regarding the Philips documents. In April of 2015, the New York court held an oral hearing, but it did not issue a decision until September 8, 2015, and that decision did not become final until October. When that decision became final, the Appeals Division set forth a process for the parties to identify, and if possible agree upon, items that should be redacted pursuant to the various New York rulings. That process did not conclude until early 2016 and, in an effort to avoid further disputes, the Appeals Division itself made those redactions to which both parties agreed and provided the redacted filing.

Appeal of Audrey C. Jaegle, 76-SBE-070, June 22, 1976.) There is no reasonable cause exception to the imposition of interest. (*Appeal of Audrey C. Jaegle*, *supra*.)

As in effect for the year at issue, R&TC section 19104, subdivision (a)(1), provides, in part, that the FTB may abate all or a part of any interest on a deficiency to the extent that interest is attributable in whole or in part to any unreasonable error or delay committed by respondent in the performance of a ministerial act.

For deficiencies with respect to tax years beginning on or after January 1, 1998, R&TC section 19104, subdivision (a), also allows interest abatement related to errors and delays in the performance of a "managerial" act. (Rev. & Tax. Code, § 19104, subd. (e); *Appeal of Ernest J. Teichert*, 99-SBE-006, Sep. 29, 1999 (*Teichert*).) Specifically, R&TC section 19104, subdivision (e), provides in relevant part that, except as provided in subparagraph (c) of paragraph (2) of subdivision (b) (which provides that the Board can review requests to abate interest that are made on or after January 1, 1998), the amendments made by Chapter 600 of the Statutes of 1997 are operative "with respect to taxable years *beginning on or after January 1, 1998*. [emphasis added]" The term "taxable year" means the year "upon the basis of which the taxable income is computed." (Rev. & Tax. Code §§ 17010, 18402, subd. (c)(1).) The referenced amendments made by Chapter 600 state that abatement may be provided for managerial acts, in addition to ministerial acts. Here, as the year "upon the basis of which the taxable income is computed" is 1992, rather than a taxable year beginning on or after January 1, 1998, interest abatement may only be obtained for unreasonable errors or delays in the performance of a ministerial act.

An error or delay can only be considered when no significant aspect of the error or delay is attributable to the appellant and after respondent has contacted the appellant in writing with respect to the deficiency or payment. (Rev. & Tax. Code, § 19104, subd. (b)(1).)

In the *Appeal of Michael and Sonia Kishner*, 99-SBE-007, decided September 29, 1999 (*Kishner*), the Board adopted the language from Treasury Regulation section 301.6404-2(b)(2), defining a "ministerial act" as:

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[A] procedural or mechanical act that does not involve the exercise of judgment or discretion, and that occurs during the processing of a taxpayer's case after all prerequisites to the act, such as conferences and review by supervisors, have taken place. A decision concerning the proper application of federal tax law (or other federal or state law) is not a ministerial act.

Treasury Regulation 301.6404-2(b) provides the following examples:

Example 1. A taxpayer moves from one state to another before the IRS selects the taxpayer's income tax return for examination. A letter explaining that the return has been selected for examination is sent to the taxpayer's old address and then forwarded to the new address. The taxpayer timely responds, asking that the audit be transferred to the IRS's district office that is nearest the new address. The group manager timely approves the request. After the request for transfer has been approved, *the transfer of the case is a ministerial act*. The Commissioner may (in the Commissioner's discretion) abate interest attributable to any unreasonable delay in transferring the case.

Example 2. An examination of a taxpayer's income tax return reveals a deficiency with respect to which a notice of deficiency will be issued. The taxpayer and the IRS identify all agreed and unagreed issues, the notice is prepared and reviewed (including review by District Counsel, if necessary), and any other relevant prerequisites are completed. *The issuance of the notice of deficiency is a ministerial act*. The Commissioner may (in the Commissioner's discretion) abate interest attributable to any unreasonable delay in issuing the notice.

Example 3. A revenue agent is sent to a training course for an extended period of time, and the agent's supervisor decides not to reassign the agent's cases. During the training course, no work is done on the cases assigned to the agent. *The decision to send the revenue agent to the training course and the decision not to reassign the agent's cases are not ministerial acts*; however, both decisions are managerial acts. The Commissioner may (in the Commissioner's discretion) abate interest attributable to any unreasonable delay resulting from these decisions.

Example 4. A taxpayer appears for an office audit and submits all necessary documentation and information. The auditor tells the taxpayer that the taxpayer will receive a copy of the audit report. However, before the report is prepared, the auditor is permanently reassigned to another group. An extended period of time passes before the auditor's cases are reassigned. *The decision to reassign the auditor and the decision not to reassign the auditor's cases are not ministerial acts*; however, they are managerial acts. The Commissioner may (in the Commissioner's discretion) abate interest attributable to any unreasonable delay resulting from these decisions.

Example 5. A taxpayer is notified that the IRS intends to audit the taxpayer's income tax return. The agent assigned to the case is granted sick leave for an extended period of time, and the taxpayer's case is not reassigned. *The decision to grant sick leave and the decision not to reassign the taxpayer's case to another agent are not ministerial acts*; however, they are managerial acts. The Commissioner may (in the Commissioner's

discretion) abate interest attributable to any unreasonable delay caused by these decisions.

Example 6. A revenue agent has completed an examination of the income tax return of a taxpayer. There are issues that are not agreed upon between the taxpayer and the IRS. Before the notice of deficiency is prepared and reviewed, a clerical employee misplaces the taxpayer's case file. *The act of misplacing the case file is a managerial act.* The Commissioner may (in the Commissioner's discretion) abate interest attributable to any unreasonable delay resulting from the file being misplaced.

Example 7. A taxpayer invests in a tax shelter and reports a loss from the tax shelter on the taxpayer's income tax return. IRS personnel conduct an extensive examination of the tax shelter, and the processing of the taxpayer's case is delayed because of that examination. *The decision to delay the processing of the taxpayer's case until the completion of the examination of the tax shelter is a decision on how to organize the processing of tax returns. This is a general administrative decision. Consequently, interest attributable to a delay caused by this decision cannot be abated* under paragraph (a) of this section.

Example 8. A taxpayer claims a loss on the taxpayer's income tax return and is notified that the IRS intends to examine the return. However, a decision is made not to commence the examination of the taxpayer's return until the processing of another return, for which the statute of limitations is about to expire, is completed. *The decision on how to prioritize the processing of returns based on the expiration of the statute of limitations is a general administrative decision. Consequently, interest attributable to a delay caused by this decision cannot be abated* under paragraph (a) of this section.

Example 9. During the examination of an income tax return, there is disagreement between the taxpayer and the revenue agent regarding certain itemized deductions claimed by the taxpayer on the return. To resolve the issue, advice is requested in a timely manner from the Office of Chief Counsel on a substantive issue of federal tax law. *The decision to request advice is a decision concerning the proper application of federal tax law; it is neither a ministerial nor a managerial act. Consequently, interest attributable to a delay resulting from the decision to request advice cannot be abated* under paragraph (a) of this section.

Example 10. The facts are the same as in Example 9 except the attorney who is assigned to respond to the request for advice is granted leave for an extended period of time. The case is not reassigned during the attorney's absence. *The decision to grant leave and the decision not to reassign the taxpayer's case to another attorney are not ministerial acts*; however, they are managerial acts. The Commissioner may (in the Commissioner's discretion) abate interest attributable to any unreasonable delay caused by these decisions.

Example 11. A taxpayer contacts an IRS employee and requests information with respect to the amount due to satisfy the taxpayer's income tax liability for a particular taxable year. Because the employee fails to access the most recent data, the employee gives the

> taxpayer an incorrect amount due. As a result, the taxpayer pays less than the amount required to satisfy the tax liability. *Accessing the most recent data is a ministerial act.* The Commissioner may (in the Commissioner's discretion) abate interest attributable to any unreasonable error or delay arising from giving the taxpayer an incorrect amount due to satisfy the taxpayer's income tax liability.
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> Example 12. A taxpayer contacts an IRS employee and requests information with respect to the amount due to satisfy the taxpayer's income tax liability for a particular taxable year. To determine the current amount due, the employee must interpret complex provisions of federal tax law involving net operating loss carrybacks and foreign tax credits. Because the employee incorrectly interprets these provisions, the employee gives the taxpayer an incorrect amount due. As a result, the taxpayer pays less than the amount required to satisfy the tax liability. *Interpreting complex provisions of federal tax law is neither a ministerial nor a managerial act*. Consequently, interest attributable to an error or delay arising from giving the taxpayer an incorrect amount due to satisfy the taxpayer's income tax liability in this situation cannot be abated under paragraph (a) of this section.
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> Example 13. A taxpayer moves from one state to another after the IRS has undertaken an examination of the taxpayer's income tax return. The taxpayer asks that the audit be transferred to the IRS's district office that is nearest the new address. The group manager approves the request, and the case is transferred. Thereafter, the taxpayer moves to yet another state, and once again asks that the audit be transferred to the IRS's district office that is nearest that new address. The group manager approves the request, and the case is again transferred. The agent then assigned to the case is granted sick leave for an extended period of time, and the taxpayer's case is not reassigned. *The taxpayer's repeated moves result in a delay in the completion of the examination. Under paragraph (a)(2) of this section, interest attributable to this delay cannot be abated because a significant aspect of this delay is attributable to the taxpayer*. However, as in Example 5, the Commissioner may (in the Commissioner's discretion) abate interest attributable to any unreasonable delay caused by the managerial decisions to grant sick leave and not to reassign the taxpayer's case to another agent. [emphasis added by staff]

Respondent's determination not to abate interest is presumed correct, and the burden is on the appellant to prove error. (*Appeal of Michael E. Myers*, 2001-SBE-001, May 31, 2001.) By statute, the Legislature has limited the Board's jurisdiction in an interest abatement case to a review of the FTB's determination for an "abuse of discretion." (Rev. & Tax. Code, § 19104, subd. (b)(2)(B).) To show an abuse of discretion, an appellant must establish that, in refusing to abate interest, the FTB exercised its discretion arbitrarily, capriciously, or without sound basis in fact or law. (*Woodral v. Comm'r* (1999) 112 T.C. 19, 23.) Interest abatement provisions are not intended to be routinely used to avoid the payment of interest, thus an abatement should be ordered only "where failure to abate interest would be widely perceived as grossly unfair." (*Lee v. Comm'r* (1999) 113 T.C. 145, 149.) In *Lee*, the

Tax Court found that the mere passage of time in the litigation of a tax dispute does not establish an error or delay in the performance of a ministerial act. (*Id*. at p. 150.)

STAFF COMMENTS – ISSUE (4) – INTEREST ABATEMENT

As noted above, there is no reasonable cause exception to the imposition of interest. (*Appeal of Audrey C. Jaegle, supra*.) Especially for the tax year at issue in this appeal, it is difficult to establish grounds for the abatement of interest. In order to establish legal grounds for interest abatement, R&TC section 19104 requires, for the year at issue, that appellant show all of the elements outlined below.

First, appellant must show an "unreasonable error or delay."

Second, the "unreasonable error or delay" must have been committed by the FTB in the performance of a "ministerial act." A "ministerial act" refers to a "procedural or mechanical act that does not involve the exercise of judgment or discretion, and that occurs during the processing of a taxpayer's case after all prerequisites to the act . . . have taken place." (Treas. Reg. § 301.6404-2(b)(2).) Appellant incorrectly argues that a "managerial act" may suffice. While that is true for interest accruing on deficiencies for tax years after 1997, it is not true for the tax year at issue. For the tax year at issue, an unreasonable error or delay in the performance of a managerial act is not sufficient to establish interest abatement.[121]

According to the regulations set forth above, examples of ministerial acts may include the transfer of a case, a mechanical failure to look up the most recent data regarding the amount due, and issuance of a notice of deficiency, if all prerequisites to such actions have been completed. (Treas. Reg. § 301.6404-2(b), Examples 1, 2 & 11.) Thus, an unreasonable error or delay in such acts could constitute grounds for interest abatement, if other requirements are met as well.

At the hearing, the parties should be prepared to discuss whether the FTB auditor misread the payment table provided by appellant's representative on February 7, 1996, and whether any misreading of the payment table, or the FTB's failure to correct this calculation, could constitute

[121] See discussion in "Applicable Law" above. See also *Braun v. Comm'r*, T.C. Memo. 2005-221, p. 4. *Braun* notes that, at the federal level, the provision allowing for an abatement based on managerial acts is only effective for interest accruing with respect to deficiencies for tax years beginning after July 30, 1996. For California purposes, the provision for managerial acts is only effective with respect to interest accruing on taxable years beginning on or after January 1, 1998.

ministerial acts. It appears to staff that the FTB's decision about whether to accept the table and documentation as a basis for its calculation of tax might be distinguished from any error in reading the table. The parties should be prepared to discuss at the hearing whether any decision by the FTB about whether and when to correct its income calculation was an act requiring judgment and discretion (even if one views the act as one reflecting poor judgment) or a mechanical act or failure to act. As noted below, to establish interest abatement, in addition to showing a ministerial act, it would also have to be shown, among other things, that such actions or inactions delayed proceedings for an identified period (i.e., that proceedings would have been concluded sooner if such acts or delays had not occurred).

The loss of a file and assignment decisions are managerial acts, rather than ministerial acts. (*Id*., Examples 6 & 10.) Delaying action on a taxpayer's claimed deduction while the IRS examines a tax shelter at issue is a general administrative decision for which an abatement is not available. (*Id*., Example 7.) It appears to staff that an FTB determination to defer actions during the protest period due to litigation-related issues would be an act requiring judgment and discretion, and also a general administrative decision, and therefore would not constitute a ministerial act. Under R&TC section 19104, the legal issue is whether FTB committed an unreasonable error or delay in performing a ministerial act. For this reason, unless appellant can tie his allegations of bad faith to an unreasonable error or delay in performing a ministerial act, those allegations do not appear relevant to the legal analysis under R&TC section 19104.

Third, appellant must show that the interest is "attributable in whole or in part" to the unreasonable error or delay in the performance of a ministerial act. Thus, the interest accrual must have been caused, in whole or part, by the unreasonable error or delay in the performance of a ministerial act. The taxpayer must show that, but for the unreasonable error or delay, the tax liability would have been paid sooner.[122] The Tax Court has held that, by seeking an abatement of all interest, rather than interest with respect to a specific period attributed to a ministerial act, the taxpayer "is not so much seeking an abatement of interest as he is an exemption from it[,]" and that this defect, in combination

[122] See *Prakash v. Comm'r*, T.C. Memo. 2016-176, p. 3 [stating that the taxpayer must "establish a correlation between the error or delay and a specific period for which interest should be abated" and that, but for the error or delay, the taxpayer would have paid the tax liability sooner]. But see the *Appeal of Alan F. And Rita K. Shugart*, 2005-SBE-001, July 1, 2005 [abating interest based on the cumulative effect of delays when discrete periods could not be identified].

with others, placed the taxpayer's request beyond the intent of the interest abatement statute. (*Donovan v. Comm'r*, T.C. Memo. 2000-220, p. 2.)

Fourth, appellant must show that "no significant aspect" of the error or delay can be attributed to him. (Rev. & Tax. Code, § 19104, subd. (b)(1).) This provision may apply even if a taxpayer's actions were not intended to cause the error or delay. That is, if the Board determined that interest abatement was unavailable because appellant's actions significantly contributed to any asserted errors or delays, such a determination would not require a finding that appellant acted with the intent to delay proceedings or otherwise acted in bad faith.

Fifth, any error or delay in the performance of a ministerial act can only be taken into account after the FTB has contacted the taxpayer in writing with respect to the deficiency. At the hearing, the parties should be prepared to discuss when the first written contact with respect to the deficiency occurred.[123] On the one hand, staff notes that the language in R&TC section 19104, subdivision (b)(1), limiting the abatement to periods after the FTB has contacted the taxpayer in writing with regard to "that deficiency" could be read as referring to the proposed deficiency set forth in the NPA, rather than correspondence issued prior to the FTB's determination that a deficiency existed. Also, in *Teichert, supra*, 99-SBE-006, the Board found that the NPA constituted the first written contact, although it may have been that the NPA in that appeal was issued before any other correspondence. On the other hand, California's abatement provision is very similar to the federal provision (see *Kishner, supra*, applying the federal interest abatement regulations), and federal regulations and cases appear to indicate that interest abatement may be obtained for periods prior to the issuance of the notice of deficiency.[124]

Sixth, by statute, the Legislature has limited the Board's jurisdiction in an interest abatement case to a review of the FTB's determination for an "abuse of discretion." (Rev. & Tax.

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[123] In appellant's 1992 Opening Brief, at page 73, he argued that the first written contact was the November 5, 1995 letter. However, appellant only requested interest abatement for the period after the issuance of the NPAs. (App. 1991 Op. Br., p. 67.)

[124] See e.g., Treasury Regulation section 301.6404-2(c)(2), Example 1, allowing interest abatement during audit, and Example 2, allowing interest abatement for a delay in issuing a notice of deficiency. See also *Allcorn v. Comm'r* (2012) 139 T.C. 53, pp. 56-57, stating that an abatement under IRC section 6404(e)(1), which is the federal equivalent of R&TC section 19104, subdivision (b)(1), may apply when the IRS commences an audit.

Code, § 19104, subd. (b)(2)(B).) To show an abuse of discretion, an appellant must establish that, in refusing to abate interest, the FTB exercised its discretion arbitrarily, capriciously, or without sound basis in fact or law. (*Woodral v. Comm'r*, *supra*, 112 T.C. 19, 23.)

Section 40

As noted above, this matter is subject to Revenue and Taxation Code section 40. Therefore, within 120 days from the date the Board's vote to decide the appeal becomes final, a written opinion (i.e., Summary Decision or Formal Opinion) must be published on the Board's website. (Cal. Code Regs., tit. 18, § 5552, subds. (b), (f).) The Board's vote to decide the appeal will become final 30 days following the date of the Board's vote to determine the appeal, except when a petition for rehearing is filed within that period.[125] (Cal. Code Regs., tit. 18, § 5460, subd. (a).)

Following the conclusion of this hearing, if the Board votes to decide the appeal, but does not specify which type of written opinion should be prepared, staff will expeditiously prepare a nonprecedential Summary Decision and submit it to the Board for consideration at a subsequent meeting. (Cal. Code Regs., tit. 18, § 5551, subd. (b)(2).) The proposed written opinion would not be confidential pending its consideration by the Board (Cal. Code Regs., tit. 18 § 5551, subd. (b)(5)); accordingly, it would be posted on the Public Agenda Notice for the meeting at which the Board will consider and vote on the written opinion.

Any party may request that the Board delay voting to decide the appeal until it votes to adopt its written opinion for the appeal. Any such request should be made in writing to the Board Proceedings Division prior to the hearing or as part of the party's oral argument at the hearing, and the request would then be considered by the Board during its deliberations on the appeal. If the Board grants the request, the proposed written opinion will be confidential until it is adopted by the Board. (Cal. Code Regs., tit. 18, § 5551, subd. (b)(5).)

[125] If a petition for rehearing is filed, the Board's decision will not become final, and no written opinion under Section 40 will be considered until after the petition for rehearing is resolved.