

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:) OTA Case No. 18012106
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CHRISS W. STREET) Date Issued: August 17, 2018
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OPINION ON PETITION FOR REHEARING

Representing the Parties:

For Appellant: Chriss W. Street
For Respondent: David Hunter, Tax Counsel III
Office of Tax Appeals: Mai C. Tran, Tax Counsel IV

M. GEARY, Administrative Law Judge: On November 14, 2017, the Board of Equalization (BOE) issued a decision in which it sustained the Franchise Tax Board’s (FTB’s) proposed assessment of \$57,300 in additional tax, an accuracy-related penalty of \$11,460, and applicable interest, for the 2007 tax year. Pursuant to Revenue and Taxation Code section 19048,¹ on December 13, 2017, Chriss W. Street (appellant) petitioned for a rehearing of the BOE’s decision on the grounds that new evidence shows that the decision was based on insufficient evidence or is against the law.² Upon consideration of appellant’s petition according to the standards expressed in *Appeal of Wilson Development, Inc.*, 94-SBE-007, October 5, 1994,³ and California Code of Regulations, title 18, § 30602(c)(5)(A-D), we conclude that the grounds set forth therein do not constitute good cause for a new hearing.⁴

¹ Unless otherwise indicated, all statutory (“section” or “§”) references are to the Revenue and Taxation Code.

² Pursuant to Assembly Bill 102, The Taxpayer Transparency and Fairness Act of 2017, and Assembly Bill 131 (2017-18 Reg. Sess.), the duty of resolving administrative appeals for personal income tax matters has been transferred from the BOE to the newly created Office of Tax Appeals.

³ Formal and Memorandum opinions issued by the BOE can be seen on the Board’s website at: <http://www.boe.ca.gov/legal/legalopcont.htm>.

⁴ See, also, OTA’s recent decision in *Appeal of Sjofinar Do*, 2018-OTA-002P, March 22, 2018.

In *Appeal of Wilson Development, Inc., supra*, the BOE determined that good cause for a new hearing may be shown where one of the following grounds exists and the rights of the complaining party are materially affected: 1) an irregularity in the proceedings by which the party was prevented from having a fair consideration of its appeal; 2) accident or surprise, which ordinary prudence could not have guarded against; 3) newly discovered evidence, material for the party making the petition for rehearing, which the party could not, with reasonable diligence, have discovered and produced prior to the decision; 4) insufficiency of the evidence to justify the decision, or the decision is against the law; or 5) the decision is contrary to law. These standards for a petition for rehearing have been codified in the Office of Tax Appeals Rules for Tax Appeals. (Cal. Code Regs., tit. 18, § 30602(c)(5)(A-D).)

On October 7, 1996, Fruehauf Trailer Corporation (Fruehauf) filed for protection under Chapter 11 of the Bankruptcy Code. Appellant served as Chairman of the Board and President of Fruehauf until April 1997. On September 17, 1998, the Bankruptcy Court approved a plan of reorganization which later resulted in the creation of the End of the Road Trust (Trust). Appellant and Trust entered into an employment agreement pursuant to which appellant agreed to serve as trustee beginning on October 27, 1998. According to the employment agreement, appellant was to be paid an annual salary of \$200,000, plus an annual bonus. The agreement provided that “all reasonable and customary expenses” incurred by appellant in the performance of his duties would be reimbursed by the Trust. In addition, appellant was entitled to participate in “all fringe benefits.” Appellant received a signing bonus of \$350,000 to reward him for work performed prior to “becoming an employee of the Debtors as well as after assuming the position.” During the years of his trustee services, the Trust issued Forms W-2 to appellant.

Appellant resigned as Trustee of the Trust on or about August 1, 2005. On February 2, 2007, Daniel Harrow (Harrow), the Successor Trustee of the Trust, sued appellant for breach of the employment agreement, breach of various fiduciary duties, equitable forfeiture of compensation, fraud, conversion, and other related causes (the Trust lawsuit). Appellant sent Harrow a letter dated December 28, 2006, in which he sought indemnification for his acts as trustee and requested that his legal defense fees be paid by the Trust pursuant to the employment agreement. Harrow denied appellant’s request, and appellant filed a counterclaim seeking indemnification for legal fees and other relief. The Trust prevailed in its lawsuit and won a judgment against appellant for \$7 million. Appellant lost on his counterclaim. Appellant was

represented by Phillip Greer (Greer) in the Trust lawsuit, and allegedly incurred legal fees in 2007 relating to that representation.

Appellant sued Greer for negligence and fraud allegedly committed during Greer's representation of appellant in the Trust lawsuit (the malpractice lawsuit). On May 30, 2017, a jury found that Greer was negligent, at least in part because his acts or omissions resulted in certain facts being deemed admitted by appellant in the Trust lawsuit. The jury also found that Greer had fraudulently failed to disclose his negligence to appellant. Greer filed an appeal of the adverse judgment in September 2017.

On his 2007 tax return, Schedule C (Profit or Loss from Business – Sole Proprietorship), appellant reported the legal fees allegedly paid to Greer as a deductible professional and legal expense incurred by him as a "professional trustee." FTB audited the return and determined that appellant did not incur the legal fees in connection with any trade or business activity, but rather, incurred them solely as an employee of the Trust. Based on that determination, FTB transferred the claimed deduction from Schedule C to Schedule A, which includes a section for deduction of unreimbursed employee expenses. Because of that change, FTB assessed an alternative minimum tax (AMT) of \$57,300 and an accuracy-related penalty of \$11,460. Appellant appealed that determination to the BOE.

In addition to his claim that the legal fees were deductible as an ordinary and necessary expense of a professional trustee, appellant had argued in the appeal that some of the fees had been incurred in his capacity as elected Treasurer/Tax Collector for Orange County, and that FTB had conducted research regarding the Trust lawsuit without seeking input from him and that FTB had made false assumptions, which were the basis for its determination. FTB had argued that the employment agreement and the Trust's issuance of W-2 forms established that appellant was an employee of the Trust, and that the invoices for Greer's legal services specifically referred to the Trust lawsuit. FTB also argued that its assessment is supported by the fact that appellant did not report any business or trade activities on a Schedule C during all the years he was employed by the Trust.

In its November 14, 2017 decision, the Board adopted the staff Summary Decision and sustained the FTB's assessment of the AMT and penalty.⁵ The Summary Decision describes the

⁵ This was a nonappearance matter, meaning that appellant did not appear and that the BOE decided the matter based on the written record.

procedural background of the appeal and the parties' arguments. It describes the bases for the conclusion that appellant had not carried his burden of establishing that FTB's proposed assessment was wrong by reference to (1) the employment agreement; (2) the Trust's issuance to appellant of W-2 forms, which reflected withholding for federal and state income tax and Medicare tax and showed appellant's participation in the Trust's retirement plan; (3) appellant's request that the Trust indemnify him for legal expenses; (4) appellant's failure to provide evidence to show that he was a professional trustee and not an employee, such as IRS Forms 1099; and (5) appellant's failure to provide evidence to refute FTB's assertions that (a) appellant did not report his trustee income or claim expenses in connection with such activity on a Schedule C during the years he was trustee; and (b) appellant was an employee of Orange County during the time he alleges that Greer provided legal services relating to that employment.


In his petition for rehearing, appellant contends that the Summary Decision was based on insufficient evidence. Specifically, appellant argues that "new evidence," the jury's verdict in the malpractice lawsuit, establishes that the summary decision relied on "purported facts, information, documentation and or conclusory theories that have been proven to be fraudulent." Alternatively, appellant argues that he should be allowed to file an amended return to deduct the legal fees as losses due to theft.

To be sufficient to warrant a rehearing, new evidence must be material for the party making the petition for rehearing and "newly discovered," which means the party could not, with reasonable diligence, have discovered and produced it prior to the decision of the appeal. The verdict rendered in the malpractice lawsuit is not such evidence. It was rendered almost six months prior to the BOE's decision, and appellant certainly was aware of it. Also, appellant has not established how the jury verdict is material to the issues considered by the BOE. The Summary Decision describes the factual bases for the conclusion (see above). We find that the evidence considered by the BOE was sufficient to support its factual findings and that the jury's verdict in the malpractice lawsuit is not "new evidence" and is not material to the issues decided by the BOE.

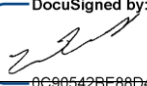
Appellant's alternative argument that he should be allowed an opportunity to amend his return to deduct the legal fees as losses due to theft is not based on new evidence. It could have been made to the BOE. The law does not allow us to grant rehearings to allow a party to try new theories.

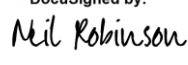
DISPOSITION

Appellant's petition for a rehearing is denied.

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Michael F. Geary
Administrative Law Judge

We concur:

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Tommy Leung
Administrative Law Judge

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Neil Robinson
Administrative Law Judge