

BEFORE THE OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

IN THE MATTER OF THE APPEAL OF,)
DONALD LIST,) OTA NO. 18010892
APPELLANT.)
_____)

TRANSCRIPT OF PROCEEDINGS

Los Angeles, California

Tuesday, April 23, 2019

Reported by:
ERNALYN M. ALONZO
HEARING REPORTER

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Transcript of Proceedings, taken at
355 South Grand Avenue, South Tower, 23rd Floor,
Los Angeles, California, 91401, commencing at
1:10 p.m. and concluding at 2:15 p.m.,
on Tuesday, April 23, 2019, reported by
Ernalyn M. Alonzo, Hearing Reporter, in and
for the State of California.

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APPEARANCES:

Panel Lead: Hon. DANIEL CHO

Panel Members: Hon. KENNY GAST
Hon. LINDA CHENG

For the Appellant: DONALD LIST, Taxpayer
ROBERT B. ROSENSTEIN, ESQ.

For the Respondent: State of California
Franchise Tax Board
By: BRADLEY KRAGEL
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	<u>DIRECT</u>	<u>CROSS</u>	<u>REDIRECT</u>	<u>RECROSS</u>
Donald List	15	20	21	

E X H I B I T S

(Appellant's Exhibits were received at page 8.)

(Franchise Tax Board's Exhibits were received at 6.)

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1 Los Angeles, California; Tuesday, April 23, 2019

2 1:10 p.m.

3
4 ADMINISTRATIVE LAW JUDGE CHO: Let's go on the
5 record.

6 This is the appeal of Donald List, OTA
7 Case No. 18010892. Today is April 23, 2019, and the time
8 is approximately 1:10 p.m. We're holding this hearing in
9 Los Angeles, California. My name is Daniel Cho, and I'll
10 be the lead Administrative Law Judge in this appeal. With
11 me are Administrative Law Judges, Linda Cheng and Kenny
12 Gast.

13 Can the parties please introduce and identify
14 yourselves for the record, beginning with appellant.

15 MR. ROSENSTEIN: I'm Robert Rosenstein of
16 Rosenstein and Associates. With me is Donald List.

17 ADMINISTRATIVE LAW JUDGE CHO: FTB?

18 MR. KRAGEL: My name is Bradley Kragel,
19 K-r-a-g-e-l. I'm here with Lou Ambrose. We represent
20 respondent, Franchise Tax Board.

21 ADMINISTRATIVE LAW JUDGE CHO: Thank you. The
22 issue in this appeal is whether appellant has established
23 that he's entitled to additional cost basis on the sale of
24 certain stock in the 2009 tax year. Is that your
25 understanding, Mr. Rosenstein?

1 MR. ROSENSTEIN: Yes, sir. It is.

2 ADMINISTRATIVE LAW JUDGE CHO: Is that your
3 understanding as well, FTB?

4 MR. KRAGEL: Yes.

5 ADMINISTRATIVE LAW JUDGE CHO: Thank you. With
6 respect to the evidentiary record, FTB has provided
7 Exhibits A through F. The appellant has not objected to
8 these exhibits. Therefore, these exhibits are entered
9 into the record.

10 (Franchise Tax Board's Exhibits A-F were received
11 in evidence by the Administrative Law Judge.)

12 ADMINISTRATIVE LAW JUDGE CHO: FTB (sic) has
13 submitted records 1 through 25.

14 MR. ROSENSTEIN: Excuse me, Your Honor. That's
15 Mr. List. You said FTB. That's just for the record.

16 ADMINISTRATIVE LAW JUDGE CHO: I'm sorry. One
17 more time, Mr. Rosenstein?

18 MR. ROSENSTEIN: You said the FTB submitted 1
19 through 25.

20 ADMINISTRATIVE LAW JUDGE CHO: Oh, I'm sorry.

21 MR. ROSENSTEIN: I didn't mean to correct you,
22 but I just -- since we're on the record.

23 ADMINISTRATIVE LAW JUDGE CHO: No problem. Thank
24 you very much for that correction.

25 Appellant has submitted Exhibits 1 through 25.

1 FTB has objected to portions of Exhibits 1 and 4. FTB
2 would you mind just explaining the grounds for your
3 objection.

4 MR. KRAGEL: We object to those two exhibits
5 which are declarations of appellant and his wife to the
6 extent in those declarations they characterize a property
7 used to -- in exchange for stock and separate property.
8 Our objections are based on the grounds that the
9 characterization of the property, separate property or
10 community property, would be a legal conclusion.

11 They can certainly testify to the objection as to
12 what the property was, cash or stock. But it's a legal
13 conclusion to characterize it as separate or community
14 property.

15 ADMINISTRATIVE LAW JUDGE CHO: Thank you.

16 And Mr. Rosenstein, do you have a quick response?

17 MR. ROSENSTEIN: Two things. One, it's being
18 submitted to show the state of mind of the individuals
19 that were involved in the transaction. It's also a
20 foundation that is laid in the declarations. It indicate
21 clearly that the property was Mr. List's prior to marriage
22 and traceable to that.

23 And according to both California and Colorado
24 law, that's separate property. Anything acquired before
25 or after marriage by gift is separate property. So

1 there's a foundation in the declarations as well as
2 showing the state of mind saying that we concluded that it
3 was separate property. That's why we did this
4 transaction.

5 ADMINISTRATIVE LAW JUDGE CHO: Thank you. The
6 panel has discussed the issue, and we've decided we're
7 going to overrule the objection. Because for one main
8 reason is that our OTA regulations state that we're not
9 required to follow the California Code of Ethics and
10 California Code of Procedures for these hearings.

11 However, we will follow the California Code of
12 Ethics with respect to giving the evidence its appropriate
13 weight in this appeal. So, therefore, we will admit the
14 evidence but giving it its appropriate weight in light of
15 the California Code of Ethics. And that kind of goes to
16 all the evidence in this appeal.

17 We'll be accepting all of the evidence in this
18 appeal. But for each piece of evidence we will
19 independently exam and give all the evidence its
20 appropriate weight that we deem in this appeal.

21 (Appellant's Exhibits 1-25 were marked for
22 identification by the Administrative Law Judge.)

23 With that being said, are there any other
24 questions before we actually start the process of the
25 presentation, Mr. Rosenstein?

1 MR. ROSENSTEIN: None.

2 ADMINISTRATIVE LAW JUDGE CHO: Mr. Kragel?

3 MR. KRAGEL: No.

4 ADMINISTRATIVE LAW JUDGE CHO: All right. In
5 that case, Mr. Rosenstein, you'll have five minutes to
6 present your opening arguments.

7 MR. ROSENSTEIN: Thank you.

8

9 OPENING STATEMENT

10 MR. ROSENSTEIN: The case is actually very
11 simple. Whether or not a sale took place after the
12 parties had no longer been together -- and we'll go into
13 the details of that more in the closing -- for well over a
14 year. This appeal follows a determination by the
15 Franchise Tax Board.

16 And the beginning document, or the managing
17 document as it would be, is the audit issue presentation.
18 That's the conclusions. That's the documentation that
19 starts it all. There's an audit. If we don't like what
20 the auditor decided, we appeal from that until we get to
21 the point we're at now.

22 The FTB in its audit presentation has conceded,
23 which is why we're so confused, that a sale took place.
24 On page 6 of 10, the FTB states -- we're referring to the
25 Oppenheimer accounts, which we'll demonstrate were a

1 separate property. The Oppenheimer accounts listed on
2 page 8 of the separation agreement are valued as of
3 3/31/05, quote, "The sale took place on 5/17/05. The
4 values of the accounts were used and were not valued at
5 5/15. In addition, these accounts were listed receiving
6 free and clear of any claims."

7 Then on page 7 of 10, the FTB states, "The
8 separation agreements vary in detail. The stock sales
9 transaction would have been included in the agreement,"
10 quote, "especially, since it took place on the same day as
11 the separation."

12 Well, wait a second. Twice, which is what we
13 were dealing with at the audit level, which is what we've
14 been giving evidence on. We have a concession that a sale
15 took place. So that's where our beginning confusion
16 starts.

17 The FTB is going to argue that there's a set of
18 rules from the Internal Revenue Service that says, okay,
19 within the first one year if there's a transaction between
20 the parties, it's not a sale. They are not factually in
21 the reports and in the briefs and everything else.
22 There's nobody that argues that this took place within the
23 first year, and we'll reaffirm that with Mr. List.

24 There's another period of time between one year
25 and six years. There's a rebuttable presumption that it

1 wasn't a sale. But it's rebuttal presumption. It's
2 interesting when the FTB gave its brief. They didn't talk
3 about rebuttable presumption. It's a rebuttable
4 presumption.

5 The other thing to keep in mind when they talk
6 about the separation agreement, you know, it's been
7 over -- from the regulations. And again I want to remind,
8 Your Honors, that a regulation is not law. This is
9 important. The regulation is not law. They're relying on
10 a regulation that -- they're not dealing with a set of
11 regulations, like, if you're dealing with asbestos or
12 the -- there's an actual regulation. You shall do this.
13 You shall not do this and everything else.

14 They're relying on a question and answer.
15 They're not dealing with a regulation. It's a set of
16 questions, answers, questions. The questions aren't there
17 to answer everything at once. The new law which
18 overturn -- which if we had to we could at any time submit
19 and say we want them all to apply to clarify what was
20 meant.

21 What clarified was the separation agreement or
22 settlement agreement was primarily to deal with support?
23 If you take a look at the -- and it specifically overturns
24 the old law, and then it has a definition that says, oh,
25 yeah. The old law applies unless you sign an agreement at

1 any time that says I want to be governed by the law.

2 So we can do that if we needed to. But what
3 needs to be made clear is what the parties always
4 intended. Now, they're going to say, okay. It was part
5 of the other agreement. So let's say we're dealing with 1
6 through 6, and we're dealing with a presumption issue that
7 we have to rebut, which we will.

8 There's a couple of key phrases, which I will do
9 at closing because I -- as I said, I'll keep this short.
10 But there are key phrases that are in the agreement to
11 show it was not anything more than a sale. And it was put
12 in there that way out of convenience, going through a
13 divorce. So they put it. They threw it in there, but
14 it's the intent of the parties.

15 The other thing they're going to argue is
16 Mrs. List's declaration should be ignored. It doesn't
17 carry any weight. The Court has already ruled. They are
18 going to give it the weight that they're going to give.
19 Well, first of all, they're trying to say it's bias. And
20 the case they cite to is the case where the mother signed
21 the declaration.

22 This has nothing to do with a mother. This is an
23 ex-wife that was willing to come forward and dealt with
24 her own tax issues and everything else, you know. And it
25 was -- and she signed the declaration. I think that's

1 pretty weighty. The other thing that they use as they go
2 through this, is when they talk about the weight to be
3 given declarations. The other cases all deal with
4 deductions. So they didn't have evidence of their
5 deduction, so they gave a declaration.

6 In one case there was a declaration that said,
7 "Oh, my tax return was filed correctly. It's all
8 correct." This has nothing to do with the requirement of
9 having to keep books and records of deductions. All of
10 the income, every dime of the income was reported on
11 Mr. List's tax return for the sale of 3D.

12 The only issue we're dealing with here is what's
13 the basis? And I think we'll demonstrate the basis should
14 be as we've set forth in our brief. Thank you.

15 ADMINISTRATIVE LAW JUDGE CHO: Thank you very
16 much.

17 FTB, you may proceed.

18 MR. KRAGEL: Thank you, Judge.

19

20 OPENING STATEMENT

21 MR. KRAGEL: The issue as we understand it is
22 whether appellant has established that respondent erred in
23 disallowing part of the cost basis on paying on
24 appellant's sale of corporate stock in 2009. The
25 disallowable basis arose from appellant's acquisition in

1 2005 of his former wife's interest in the corporate stock
2 of the company.

3 Respondent determined that appellant was not
4 entitled to claim additional basis because the
5 transaction, whereby he acquired his wife's interest, was
6 a nonrecognition event under Internal Revenue Code,
7 Section 1041. The evidence submitted in our brief, which
8 I'll discuss more in closing, supports respondent's
9 conclusion.

10 And for those reasons, respondent would
11 respectfully request that the panel sustain respondent's
12 determination. Thank you.

13 ADMINISTRATIVE LAW JUDGE CHO: Great. Thank you
14 very much. All right. We'll move on to witness
15 testimony.

16 Mr. List, before we have you testify, I'm going
17 to place you under oath. So if you don't mind standing
18 and raising your right hand.

19
20 DONALD LIST,
21 produced as a witness by and on behalf of himself, and
22 having been first duly sworn by the Administrative Law
23 Judge, was examined and testified as follows:

24
25 THE WITNESS: Yes, I do.

1 ADMINISTRATIVE LAW JUDGE CHO: Thank you. Please
2 have a seat.

3 Mr. Rosenstein, when you're ready.

4 MR. ROSENSTEIN: Thank you.

5

6 DIRECT EXAMINATION

7 BY MR. ROSENSTEIN:

8 Q Would you state your name for the record?

9 A Donald List.

10 Q Mr. List, were you at one point married to Donna
11 List?

12 A Yes, I was.

13 Q And did you separate from her with no intent of
14 returning to the marital relation on/or about
15 November 10, 2003?

16 A That's correct.

17 Q Are you familiar with a company called or was
18 called Alotech?

19 A Yes, I am.

20 Q What company was that?

21 A That was the company that I had ownership in
22 going back to the '80s and 1980s and '90s. That was my
23 own stock interest that I received; some from inheritance,
24 some from gifting, and some of my own earnings of the
25 company. And I ended up selling it in 1999.

1 Q As it related to your ownership interest, did you
2 obtain all of that ownership interest prior to the time
3 you married Donna?

4 A Yes, I did.

5 Q And you, at one point, became 100 percent owner
6 of the stock?

7 A That's correct.

8 Q And the company, Alotech, repurchased stock from
9 your mother's interest; correct?

10 A That's correct.

11 Q And you guaranteed it?

12 A That's correct.

13 Q And the company paid her buyout; correct?

14 A That's correct.

15 Q So with her buyout you became 100 percent owner?

16 A That is correct.

17 Q And you didn't require any new stock. It was
18 just your stock, your percentage; correct?

19 A Correct.

20 Q Now, at some point you and Donna separated. At
21 some point did it proceed to a divorce?

22 A Yes, it did.

23 Q And did you engage an attorney to represent you?

24 A For the divorce?

25 Q For the divorce procedure?

1 A Yes, I did.

2 Q And did you discuss with the attorney what your
3 intent was regarding acquiring Donna's interest in 3D?

4 A That's correct. I did.

5 Q What did you express to that attorney?

6 A There was a certain number of assets that were
7 going to be divided. I had my own personal assets. The
8 3D company was an asset that I recognized that we held in
9 community property. But I wanted to acquire her share of
10 it as the company. It was early in its stages, continuing
11 to grow.

12 I recognized the opportunity there that it would
13 be worth more in value in the coming years. And,
14 therefore, I was willing to use some of my own personal
15 assets to acquire her share of it. And that's what I
16 expressed to him.

17 Q You signed a separation agreement. Did you read
18 it?

19 A Well, like in anything I haven't even read this.
20 Sadly to say. Because some of it -- some of it is too
21 difficult to understand the jargon. But even aside from
22 that, when some -- you know, it was a difficult time in my
23 life. I retained an attorney. I was going to be making a
24 settlement with my then wife, who became my ex-wife, a
25 division of some assets.

1 One asset I wanted to acquire. He carried out my
2 wishes. He told me he carried out my wishes. When it was
3 time to sign -- this dragged on for way too long. Anyway,
4 it took almost -- almost two years to resolve everything
5 that we needed to between us. When he said it was time to
6 sign, I just signed. I truthfully did not probably read
7 as many pages of that divorce agreement that I probably
8 should have.

9 Q But you spoke with the attorney; correct?

10 A Yes, I did. Yes.

11 Q And when you spoke to the attorney, what did he
12 say to you regarding the acquisition of the 3D stock?

13 A Well, basically, I had expressed to him what I
14 was trying to accomplish. And he said that we would use
15 approximately five million and change of my cash to
16 purchase her share.

17 Q So it was always your intent to purchase that
18 interest?

19 A Correct.

20 Q Now, if we use \$5.9 million, approximately, that
21 put the value at about \$12 million?

22 A Right. I was only owner of 50 percent of the
23 company at the time.

24 Q I was talking about the 100 percent value?

25 A Right. So that would make it 50 percent. That's

1 correct.

2 Q About five years later the company was sold;
3 correct?

4 A That's correct.

5 Q And your sale, according to your tax return and
6 otherwise, was \$18 million?

7 A That's correct.

8 Q And when you filed your tax return with the State
9 of California, did you report all 18.1 million?

10 A Yes.

11 Q And your -- where were you living at the time you
12 purchased Donna's stock?

13 A In the state of Colorado.

14 Q You had residence there?

15 A I had residence there.

16 MR. ROSENSTEIN: I have nothing further.

17 ADMINISTRATIVE LAW JUDGE CHO: Thank you very
18 much.

19 Mr. Kragel, do you have any questions of the
20 witness?

21 MR. KRAGEL: Just a few, Judge.

22 ADMINISTRATIVE LAW JUDGE CHO: Go ahead.

23 ///

24 ///

25 ///

1 CROSS-EXAMINATION

2 BY MR. KRAGEL:

3 Q Mr. List, were you employed during the course of
4 your marriage?

5 A Was I employed?

6 Q Yes.

7 A Yes, I was employed.

8 Q Where did you work?

9 A I worked predominantly at a company called
10 Alotech Products.

11 Q Did you work there during the entire course of
12 your marriage?

13 A Yes, I did.

14 Q What was your position at Alotech?

15 A I was the president.

16 Q Did your wife work outside the home during the
17 course of the marriage?

18 A No, she did not.

19 Q Did she do anything for Alotech?

20 A No, she did not.

21 MR. KRAGEL: Thank you.

22 MR. ROSENSTEIN: May I redirect for just a
23 moment?

24 ADMINISTRATIVE LAW JUDGE CHO: One second. I'm
25 just going to ask my panel members.

1 MR. ROSENSTEIN: Sure.

2 ADMINISTRATIVE LAW JUDGE CHO: Panel members, do
3 you have any questions for the witness?

4 ADMINISTRATIVE LAW JUDGE CHEN: No.

5 ADMINISTRATIVE LAW JUDGE GAST: No questions.

6 ADMINISTRATIVE LAW JUDGE CHO: Okay. Mr.
7 Rosenstein, go ahead.

8

9 REDIRECT EXAMINATION

10 BY MR. ROSENSTEIN:

11 Q Mr. List, the earnings were -- when you worked
12 for Alotech, were you receiving a salary?

13 A Yes, I was.

14 Q What was the range of that salary during your
15 marriage?

16 A Well, it goes back. It's been a number of years.
17 It ranges anywhere from a couple of hundred, to a quarter
18 of a million dollars, and above.

19 Q And did you place that money into the joint
20 checking account and use it for living for you and Donna
21 and the family?

22 A That's correct.

23 MR. ROSENSTEIN: Thank you.

24 ADMINISTRATIVE LAW JUDGE CHO: Thank you very
25 much.

1 Mr. List, I just wanted to remind you that for
2 the duration of this hearing you will be under oath of
3 affirmation. So if there are any questions later on that
4 the panel may have or that anybody may have, just please
5 be aware you are still under oath of affirmation.

6 THE WITNESS: Okay. Sure.

7 ADMINISTRATIVE LAW JUDGE CHO: With that,
8 Mr. Rosenstein, you can have your 20 minutes for closing
9 statements.

10 MR. ROSENSTEIN: If I need that long.

11 ADMINISTRATIVE LAW JUDGE CHO: If you need that
12 long, correct.

13

14

CLOSING STATEMENT

15 MR. ROSENSTEIN: Okay. It's interesting
16 throughout the brief, as well as the documentation, that
17 the Franchise Tax Board doesn't even use the right numbers
18 in coming up with what we say should be the basis.
19 They're saying that we're claiming it should be \$7,000,398
20 and some change. We're not.

21 I mean this is -- we are being as straightforward
22 in this process and has always been as straightforward in
23 this process as we can. What we're saying is it should be
24 50 percent of the community property because he already
25 owned 50 percent of the community property. His

1 50 percent is already his \$500,000.

2 He then undisputed -- and I've got to tell you.
3 Throughout the brief I mean, you know, it's -- we all know
4 the term red herring, trying to confuse and everything
5 else. If you read their brief, that's all they keep
6 trying to do. They start with, well, Don List didn't give
7 us any evidence at the hearing. He did nothing to prove
8 his basis. He did nothing to prove it was community
9 property.

10 Well, wait a second. There's nothing in the
11 audit presentation. There was nothing anywhere that says
12 Mr. List didn't do that. Now, I'm not under oath. So
13 please don't take this as -- again, this is argument. But
14 I'm the one that went to the Franchise Tax Board, and I
15 presented the evidence locally and also up in Sacramento.
16 So I know the evidence was permitted.

17 I'm not asking you take that as -- take that as
18 much as their argument because it's not supported by any
19 evidence. But I'm just going to say what happened is
20 there's a bunch of red herrings in there trying to get
21 everybody upset. But -- so we have a purchase of
22 \$333,000, and there is a -- and the purchase of
23 \$5,898,322. They can see that.

24 In fact their brief list where the money came
25 from, the transfer of the Oppenheimer account. And that

1 was all Mr. List's separate property. So if you take
2 that -- what we're saying is that amount is \$6,731,322.
3 We're saying it's a million dollars less, and they're
4 saying we think it should be. Again, showing the
5 credibility behind what we're trying to do here.

6 Again, just for following the facts, the parties
7 separated in November 10th, 2003. They signed the
8 stipulation agreement on May 17th, 2005, well over the one
9 year required. The code section -- the actual code
10 section, not the CFR, not any other interpretation. Black
11 and white code section says one year. It doesn't say one
12 to six years. That's a question and an answer of ours,
13 but it's rebuttal four to six years.

14 And, again, that's in Internal Revenue Code
15 Section 1041. As I said, it's important to pick up the
16 two statements by the auditor that says, "I'm concluding
17 there was a sale." I just read right from the report.
18 Again, that's the foundational document that we rely on.
19 We're appealing from her decision and all sorts of other
20 stuff we want. It should be noted, by the way, she said
21 it's incident. She never brought out the one to six
22 years. She was just saying it was incident two.

23 The page 12 -- just to show the confusion --
24 starts off by saying it was Don's separate property. He
25 testified it's community property. The document says it's

1 community property. Yet, in their brief they are saying
2 it was separate property. It's just like somebody threw
3 stuff together to try to argue against us. Maybe if we
4 throw enough mud on the wall, the mud will stick
5 somewhere. Well, that's not how we make rulings. We make
6 rulings on facts and law.

7 If you take a look at the settlement agreement --
8 separation agreement, they agree to file a return directly
9 for 2004. In 2005, it says, "The party stipulate and
10 agree that the trust transfers of property between the
11 parties as set forth regarding of title to said property,
12 are transfers of marital property and not separate
13 property." That's what they're saying.

14 Well, wait a second. This was separate property.
15 No question about it. As Mr. List has testified, it was
16 his intent that he told his lawyer. Donna said it.
17 Donna's declaration could be used to support Don's
18 testimony and the other evidence we've presented that this
19 was separate property used to buy a piece of community
20 property. The FTB says it was a sale. It was a sale.

21 The other thing that's interesting, if you look
22 at the agreement between the parties -- excuse me for one
23 second here. We start on page 10, and we start talking
24 about property, real property the parties owned -- real
25 estate the parties owned and approved land the parties

1 owned. The husband owns 50 percent. Then we get to --
2 which is again, where the brief is wrong where it says
3 it's separate property.

4 It says the parties owning interest in 3D
5 Fasteners, retirement account, the parties own. They tell
6 us it's already divided. They talk about the parties
7 owned, previously settled. Then we get to the issue
8 that's dealing with the real property -- excuse me -- the
9 financial accounts, page 8-B. It doesn't say the parties
10 own it.

11 What it says is, "The wife shall receive, that
12 they're dividing, that they own it." There's nowhere
13 dealing with these financial accounts anywhere. And then
14 it also says they're going to receive. They are going to
15 keep and receive the cash. Receiving means you're getting
16 paid for something, common language. If you already have
17 it, you don't receive it.

18 This was done out of convenience by a lawyer.
19 The fact is a lawyer should have written it. Could
20 have -- I'm not sure of should have, but could have
21 written two separate agreements. He just did it in one.
22 So we can carve that out is what we're trying to say. It
23 had nothing to do with this.

24 Mr. List has testified he did this because he saw
25 greater growth, and by increasing the basis here, buying

1 that out. As it grew another six-million dollars, it was
2 all his. If had just -- if he hadn't purchased her
3 interest, he would have been entitled to keep all of the
4 money. Oh, wait a second. We have another issue.
5 Something important. They didn't bring it up. I can ask
6 Mr. List. I'm sorry. I didn't ask him.

7 Even if there's a transfer between spouses of a
8 gift, and even though transfer between spouses is exempt
9 from inheritance tax and gift tax, it still requires
10 filing on your tax return. I can inquire. The panel can
11 inquire. There was no state tax return or gift tax return
12 filed because it was a purchase.

13 So again, you got to keep in mind the sections,
14 the language. The other thing they're going to argue
15 is that the -- it's interesting. They're going to argue,
16 according to the agreement, paragraph 10, page 14. The
17 parties stipulate and agree that it is their intention
18 that all transfers of property, via between the parties as
19 set forth herein regardless of the title to said property,
20 are transfers of marital property and not separate
21 property are in exchange for martial rights and
22 considerations. And, therefore, the transfers are not
23 taxable events.

24 This wasn't a transfer. This was purchased, and
25 it goes right into a different section. If we go to -- on

1 the next page same paragraph, it reads, "The parties shall
2 file separate income tax return in for the year 2005 and
3 all subsequent years." This is what is important.

4 "Each party shall take and declare any and all
5 income associated and/or tax deduction or benefits
6 associated with or attributable to the assets being
7 received by that party." Receive the money for the sale
8 of stock, and the parties agreed that Donna was
9 responsible. What Donna did we don't know. I mean,
10 honestly, we don't know. We're not involved. When they
11 separated I was no longer involved with her.

12 But the agreement does lay out a separate
13 agreement that can be removed from here. And it also
14 shows the rebuttable presumption based on the testimony,
15 Donna's testimony. And, again, if you take a look over
16 the cases that they cite, the fact of the matter is the
17 declarations can be used to substantiate other evidence.
18 Well, this is before the Court. So, therefore, it
19 substantiates that.

20 The parties both acknowledge their declarations,
21 and now testimony, that it was separate property used to
22 purchase. So all the FTB wants to do is say there's no
23 credibility. They haven't produced one evidence, one
24 piece of evidence. They haven't produced one witness that
25 says it wasn't separate property. They haven't produced

1 one person or one piece of evidence to say what both an
2 ex-wife, who made something against her interest, which
3 was the issue of a taxable event. She didn't do it. And
4 Mr. List and now the documents, we've beat whatever
5 rebuttable presumption there is.

6 And, again, the code section says after one year.
7 It's a regulation. And by the way, it's a temporary
8 regulation. If you look at the regulation, there's a "T".
9 It's a temporary regulation. It can be -- it hasn't gone
10 through the full -- yeah, it's been around since 2000, but
11 it hasn't gone through the full vetting. Sometimes the
12 federal government moves slowly. Well, this is one of
13 those cases.

14 They rely heavily on the Dunman case, which is
15 what I stated earlier that -- how do I put it? That case
16 was a nasty case where everybody was proven to be lying.
17 In fact that case people were sanctioned. It's also -- if
18 you read the full opinion, you'll see it has nothing do
19 with this case. And, again, it all dealt with deductions
20 and the people that were making the declarations. It was
21 a horrible case. We distinguish ourselves from that.

22 In the response to -- we file a response to the
23 offer of presentation and the FTB responded. It states,
24 "We do accept the separation agreement between Don and
25 Donna List as persuasive evidence that the property was

1 divided up. And the matter of division could be
2 corroborated with the signed declarations."

3 What is that? Those are the documents that put
4 us in the whole appeal process. They say we recognize it
5 and the method, the sale, can be put into evidence
6 corroborated based upon the declaration. I mean, this is
7 FTB. I mean, the fact of defense we argue now is a whole
8 bunch of other things, and we throw other things into the
9 pot.

10 The evidence is what the FTB has said, which is
11 what we were confused about. And I kept saying, "Where
12 are you guys going?" Again, the question -- again,
13 remember I'm telling you that -- reminding you that the
14 24CFR1.104-1T has a bunch of questions and answers.

15 Well, questions and answers aren't regulation or
16 governing law. That's an opinion of the person who wrote
17 it. And it provides that after one year there's a
18 presumption, but it's a rebuttable presumption.

19 If you give me one minute, I'm just about
20 through.

21 ADMINISTRATIVE LAW JUDGE CHO: Okay. Thanks.
22 Also just to let you know, you have about two minutes
23 left. You'll have time on rebuttal.

24 MR. ROSENSTEIN: Okay. I think I'll save it for
25 rebuttal.

1 ADMINISTRATIVE LAW JUDGE CHO: All right. Thank
2 you very much.

3 Mr. Kragel, proceed when you're ready.

4 MR. KRAGEL: Thank you, Judge.

5

6 CLOSING STATEMENT

7 MR. KRAGEL: This matter arises out of
8 appellant's sale of his interest of the company called
9 3D Fasteners in 2009 after he acquired his wife's interest
10 in 2005. Appellant and his wife were married in 1984.
11 During the marriage, appellant and his wife acquired stock
12 holding interest in a company called 3D Fasteners. They
13 separated in 2003 and were divorced in 2005.

14 As part of the divorce they entered into a
15 separation agreement. Section 7 of the separation
16 agreement is entitled Property Division. In that section
17 it stated that appellant's wife would receive all or part
18 of nine financial accounts with Oppenheimer and Company.
19 The combined total of four of those accounts was
20 approximately 5.9 million dollars, which appellant would
21 later claim was the purchase price that appellant claimed
22 for his wife's share in the 3D Fasteners stock.

23 There's nothing in Section 7 that says it's the
24 purchase price for anything. Section 7 further stated
25 that appellant and his wife owned interest in

1 3D Fasteners, which they had agreed had a fair market
2 value of 1.5 million dollars.

3 Section 10 stated in full, quote, "The parties
4 stipulate and agree that it is their intention that all
5 transfers of property by and between the parties as set
6 forth herein, regardless of title to said party, are
7 transfers of marital property and not separate property,
8 and are in exchange for marital rights and
9 considerations." And, therefore, the transfers are not a
10 taxable event and no capital gains have been declared or
11 need to be declared.

12 In 2005, the Boulder County Superior Court in
13 Colorado granted the decree of dissolution and ordered the
14 parties to form the separation agreement. In 2009,
15 appellant and the other co-owner of 3D Fasteners sold the
16 company for approximately 36.2 million dollars. In his
17 tax return, appellant reported gross proceeds of 18.1
18 million dollars, and a cost basis of 5.7 million dollars,
19 approximately, which resulted in a gain of 12.4 million.

20 During August -- during audit, respondent asked
21 appellant to produce supporting documentation for the
22 basis he claimed in 3D Fasteners. Appellant's
23 representative initially informed respondent that
24 appellant's basis resulted from three transactions; a
25 1 million dollar loan to the company, which was later

1 converted to capital.

2 The buyout of another owner, of which appellant's
3 share was \$500,000, and the combined total of four of the
4 nine Oppenheimer accounts mentioned in the separation
5 agreement. Respondent determined that the cost basis in
6 3D Fasteners was 1.5 million dollars based on the original
7 loan amount and the amount of the buyout of the other
8 owner of \$500,000.

9 Respondent issued a notice of proposed assessment
10 based on that determination, which resulted of additional
11 taxes of approximately \$444,000 using the 1.5 million as
12 the cost basis for sale of the stock. Internal Revenue
13 Code section 1041(a) provides that no gain or loss is
14 recognized on a transfer of property from an individual to
15 a spouse or a former spouse if the transfer is incident to
16 divorce.

17 Such a transfer is treated as acquired by the
18 transferee by gift, and the basis of the transferee in the
19 property is the adjusted basis for the transfer. The
20 transfer is considered incident to divorce if the transfer
21 occurs within one year after the date on which the
22 marriage ceases, or the transfer is related to the
23 cessation of marriage.

24 California conforms to Section 1041 through
25 Revenue and Taxation Code Section 18031. The regulations

1 under Section 1041 apply to any transfer of property
2 between spouses regardless of whether the transfer is a
3 gift or a sale or exchange between spouses acting at arm's
4 length.

5 The regulations further provide that a transfer
6 of property is incident to divorce if the transfer occurs
7 not more than one year after the date of which the
8 marriage ceases, or the transfer is related to the
9 cessation of marriage. A transfer of property is treated
10 as related to the cessation of marriage if the transfer is
11 pursuant to a divorce or separation agreement.

12 In the present case, the evidence shows that
13 appellant's wife transferred property, her shares in
14 3D Fasteners, to her spouse, appellant. Because she was
15 his spouse at the time of the transfer, subsection (a)(1)
16 applies, and appellant takes her basis in the transferred
17 stock. Alternatively, assuming that she was not his
18 spouse, subsection (a)(2) applies. The transfer from
19 appellant's wife to appellant was incident to divorce
20 because it was related to the cessation of marriage in
21 that it was pursuant to a separation instrument.

22 For those reasons, respondent request that the
23 panel sustain respondent's determinations. As far as
24 the -- we also included in our brief arguments and
25 references and status regarding the sale. We'll submit in

1 the brief in that regarded.

2 I do have just one comment in regard to
3 appellant's presentation. I believe in the -- where he's
4 referring to concessions that the FTB made that it was a
5 sale, it's my recollection that language was in the
6 background section of the letter and doesn't necessarily
7 qualify as a sale so much as just explaining what the
8 positions of the parties are and referencing it. It
9 didn't necessarily openly conclude that it was a sale.

10 If the panel has any questions, I can do my best
11 to answer them. Thank you.

12 ADMINISTRATIVE LAW JUDGE CHO: Thank you very
13 much.

14 I guess for now I'll open it up to the panel to
15 see if anyone has any questions. Judge Gast, would you
16 like to ask any questions.

17 ADMINISTRATIVE LAW JUDGE GAST: Maybe just one
18 clarifying question for the taxpayer, either Mr. List or
19 Mr. Rosenstein. Do you know how Mrs. List treated the
20 transaction? Did she report gain on her return?

21 MR. ROSENSTEIN: I can answer that for both of
22 us. We have no way of knowing.

23 ADMINISTRATIVE LAW JUDGE GAST: Okay. All right.
24 Do you know if a joint return was filed?

25 MR. ROSENSTEIN: It definitely was not.

1 ADMINISTRATIVE LAW JUDGE GAST: For 2003?

2 MR. ROSENSTEIN: Well, no. We're dealing with
3 2005.

4 ADMINISTRATIVE LAW JUDGE GAST: Yeah, I know. I
5 was just curious for '03 and '04.

6 MR. ROSENSTEIN: '03 and '04 joint return filed.

7 ADMINISTRATIVE LAW JUDGE GAST: Okay. No further
8 questions.

9 MR. ROSENSTEIN: Every year before that they were
10 married; correct?

11 MR. LIST: Correct.

12 ADMINISTRATIVE LAW JUDGE GAST: Okay. Thank you.

13 ADMINISTRATIVE LAW JUDGE CHO: Do you have any
14 questions, Judge Cheng?

15 ADMINISTRATIVE LAW JUDGE CHENG: I do. It's also
16 a clarifying question for taxpayer. Is it your position
17 that the separation agreement entered into on
18 May 17, 2005, is not a transfer incident to divorce? Is
19 that your position? I wasn't clear on that.

20 MR. ROSENSTEIN: Our position is that portion was
21 a sale. Yes, it was part of an incident of divorce, but
22 it goes into a second period that allows a rebuttable
23 presumption as to whether it was a sale or not. The first
24 one says it's absolutely not -- it's going to be a
25 nontaxable event. The second half, between after one year

1 before six, is rebuttable presumption under the
2 regulations.

3 The law black and white code section says that
4 only applies to the first year. Remember this is what I
5 need the panel to focus on when it's looking at 1041. The
6 black and white law says one year. It's somebody who
7 wrote questions and answers that basically we would call a
8 safe harbor. You get over six you're in the safe harbor.
9 But between one and six you got to show that the sale was
10 actually a sale of the intended parties.

11 ADMINISTRATIVE LAW JUDGE CHENG: Well, I need you
12 to focus on my question, which is was this transfer
13 incident to divorce?

14 MR. ROSENSTEIN: The transfer was not.

15 ADMINISTRATIVE LAW JUDGE CHENG: Was or was not?

16 MR. ROSENSTEIN: Was not. The transfer was not.
17 The transfer was a purchase that could have been done in a
18 separate agreement.

19 ADMINISTRATIVE LAW JUDGE CHENG: But it wasn't
20 though.

21 MR. ROSENSTEIN: No. I understand that, and that
22 was an error on an attorney's part. But as the FTB says,
23 they accept the fact that the parties could state in the
24 rebuttal to my -- rebuttal to the FTB, which I read, that
25 the parties by declaration could make the determination of

1 what the transaction was between them.

2 ADMINISTRATIVE LAW JUDGE CHENG: Okay. As a
3 follow-up, if it was a sale to Mr. List, what did Mrs. --
4 former Mrs. List pay for it?

5 MR. ROSENSTEIN: No. Mr. List purchased it.

6 ADMINISTRATIVE LAW JUDGE CHENG: I'm sorry.

7 MR. ROSENSTEIN: There's no dispute. It was
8 5.8 million dollars plus some change. It's actually in
9 the brief -- on both of our briefs. And it talks about
10 the accounts that are specified; what was used for the
11 purchase.

12 ADMINISTRATIVE LAW JUDGE CHENG: Okay. Thank
13 you.

14 MR. ROSENSTEIN: I'm sorry. I can give you the
15 exact amount if you would like. It's in the briefs.

16 ADMINISTRATIVE LAW JUDGE CHENG: No. I'm good
17 with that. Thank you.

18 ADMINISTRATIVE LAW JUDGE CHO: Okay. I have one
19 quick clarifying question as well, and this goes to
20 appellant. Just to make sure I fully understand your
21 argument, and if I understand your figures as you were
22 explaining them. I just want to make sure.

23 So it's appellant's argument that your actual
24 basis in the stock was the \$500,000 community property of
25 the initial 1 million dollars investment in 3D; is that

1 correct? It's \$500,000, plus the \$333,000 of the buyout
2 that occurred, plus the 5.8 million of the purchase from
3 Mrs. List.

4 MR. ROSENSTEIN: That's correct.

5 ADMINISTRATIVE LAW JUDGE CHO: So my question is
6 the \$333,000 purchased from the other owner, did that
7 occur while you were still married to Mrs. List?

8 MR. LIST: I'm trying to recall the time frame.
9 I don't recall.

10 ADMINISTRATIVE LAW JUDGE CHO: So I guess the
11 reason why I'm asking is because I was wondering why. Is
12 there a special reason why that shouldn't be divided in
13 half as well? Wouldn't that have been community property
14 if it was purchased during the marriage? Or did you
15 separate property first? Is that why you're giving us the
16 full value of the basis?

17 MR. ROSENSTEIN: Did you take any money from your
18 personal account?

19 MR. LIST: Yes. All these transactions were all
20 done from my own personal accounts and personal cash. I
21 don't recall the time frame of when it was done. It would
22 have been, you know, before or after the 2005 separation.

23 ADMINISTRATIVE LAW JUDGE CHO: Okay. So you
24 don't remember whether the buyout from the other partner
25 occurred prior to separation? Is that what you said?

1 MR. LIST: No. Correct. I'm fairly certain it
2 would have been after 2005.

3 ADMINISTRATIVE LAW JUDGE CHO: Okay.

4 MR. LIST: I'm not 100 percent certain.

5 ADMINISTRATIVE LAW JUDGE CHO: And I just want to
6 clarify, but I think the separation agreement value of the
7 stock at 1.5 million, and I think that was basis at the
8 time in 2005, I believe. So would that have accounted for
9 the buyout amount?

10 MR. LIST: You mean of the other partner?

11 ADMINISTRATIVE LAW JUDGE CHO: Yes.

12 MR. ROSENSTEIN: If the Court looks, there is --
13 there was a problem with the former accountant that
14 treated this as if it was an S corporation. It was a
15 C corporation. There are some declarations and everything
16 in there. In fact, again, I'm going to respond that would
17 have been part of my closing statement, but Counsel
18 brought up things that supposedly happened during the
19 interview process without any evidence. And, again as I
20 said, I was the representative he kept referring to.

21 There was a companion case called Daryl Ver Doorn
22 that triggered the audit that the accountant -- and we
23 have it all in here. It's all evidence. It included the
24 basis for Mr. Van Doorn at about the same 5.7 million
25 dollars. And when it was pointed out, and we went in --

1 and this shows a little credibility, if nothing else,
2 since he brought up the transaction that happened with the
3 auditor. It was the same auditor or different auditor,
4 but whatever. The first part of the appeal was resolved.

5 Mr. Ver Doorn immediately paid his taxes. It
6 wasn't like two people, you know. The transaction was the
7 same transaction when the FTB came back and said this
8 doesn't make sense. Mr. Van Doorn paid that money. He
9 wrote a check. So this was -- if it wasn't supposed to be
10 a sale, nobody would have been -- and for what it's worth,
11 that \$333,000 was also, again, just for information. It
12 was allowed on Mr. Ver Doorn's tax return as well.

13 ADMINISTRATIVE LAW JUDGE CHO: Okay. Thank you.
14 Just one quick clarifying question to the FTB. So with
15 respect to cessation of marriage, what's the FTB's
16 position as to when that actually occurred?

17 MR. KRAGEL: When they received their divorce
18 decree.

19 ADMINISTRATIVE LAW JUDGE CHO: Okay. That's all
20 the questions I had. Judges Gast or Judge Cheng, any
21 other questions?

22 ADMINISTRATIVE LAW JUDGE CHENG: No questions.

23 ADMINISTRATIVE LAW JUDGE GAST: No.

24 ADMINISTRATIVE LAW JUDGE CHO: All right. Then
25 moving on to Mr. Rosenstein's rebuttal. You'll have 10

1 minutes.

2 MR. ROSENSTEIN: Thank you.

3

4 REBUTTAL STATEMENT

5 MR. ROSENSTEIN: Let me address the last question
6 that was asked. It's brief. So I won't go into all the
7 law or anything else. When you separate and never intend
8 to return under Colorado law -- remember we're doing
9 Colorado and even California law. It occurs when you
10 intend never to return together. The agreements, though
11 only deal with separation agreements, the divorce decree
12 and everything else, 1041.

13 So the important thing to remember is the day
14 they separated with no intent, which is Mrs. List's
15 comment -- I think she's still Mrs. List -- and Mr. List.
16 And even in the court papers, which are attached, that was
17 the day of separation with no intent to return. So the
18 year was from that time.

19 Something to point out, and we briefed it, is the
20 community property, this community, separate property to
21 become community property with all those transmutation.
22 There's been no argument, but I wanted to clear that up.
23 It wasn't a division of any way of community property. In
24 order for there to be a transmutation, it has to be a
25 major writing and undertaking.

1 We briefed it in here because at the time they
2 married in California, the initial trust that we have. It
3 says writing a trust is a statute. It says writing a
4 trust is not transmute community property. You have to do
5 a whole bunch of other things before transmutation takes
6 place. It's in the brief so I don't need to go through
7 it.

8 It's interesting if you listen to the FTB's
9 argument. They haven't given one shred of evidence -- as
10 I said in the beginning -- to dispute any of the facts
11 that we have put forth. In fact, the oral argument --
12 and, again, it's not evidence -- but he keeps using the
13 word acquired. Listen. He acquired her interest, not
14 that they divided the interest. He acquired it, and he
15 paid for it.

16 They keep wanting to ignore the document. I'm
17 going to go back to one part. It's very interesting
18 that's one thing that makes us lawyers. But paragraph 10,
19 which I read at the beginning -- which, Mr. Gast, I think
20 goes a little bit to your question. It specifically
21 stated that anything that happened in 2005, the parties
22 were responsible for. He only wanted to read part of it.

23 If you go to the agreement at paragraph 10, it
24 reads transfers of property. Read the language. It's
25 very clear. The FTB -- and by the way, Counsel said he

1 was remembering -- I just looked it up -- that he thought
2 that it was the position paper with the background part
3 where we say the FTB conceded it was a sale, the two
4 sections I read. It's in their analysis. It's not in the
5 background. It's not in contention. It's the FTB's
6 analysis of all of the facts, all the presentation, all
7 the evidence that was given. So I think I ask the Court
8 to please recognize that.

9 To your issue regarding incident two, as I said,
10 it's a separate document that can be taken out. It can be
11 performed. And the courts -- and, again, they're briefed.
12 It's in here. They're supposed to take the intention of
13 the parties. The FTB also stated in their documents in
14 their reply, that they acknowledge the agreement. And
15 specifically the FTB has said the character can be
16 decided. The method of division can be decided by the
17 parties, and the evidence of the declarations could be
18 used to corroborate the positions.

19 So I think they -- I think we on both sides
20 make -- can make all the arguments that we want, but the
21 facts are the facts. The law is the law. Black and white
22 law says one year. Black and white. The rest of it is
23 somebody's opinion, and it's part of a question. It's not
24 part of the regulation.

25 Thank you.

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ADMINISTRATIVE LAW JUDGE CHO: Thank you very much. And I just want to say thanks to both parties for doing such a great job presenting and being very eloquent in your arguments and speech.

This concludes the hearing. The panel will meet and confer and decide the case based documents that was presented today. Our goal is to issue a written decision within 100 days of today. So the case is submitted and the record is closed, and the hearing is now adjourned.

Thank you very much.

(Proceedings adjourned at 2:15 p.m.)

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HEARING REPORTER'S CERTIFICATE

I, Ernalyne M. Alonzo, Hearing Reporter in and for the State of California, do hereby certify:

That the foregoing transcript of proceedings was taken before me at the time and place set forth, that the testimony and proceedings were reported stenographically by me and later transcribed by computer-aided transcription under my direction and supervision, that the foregoing is a true record of the testimony and proceedings taken at that time.

I further certify that I am in no way interested in the outcome of said action.

I have hereunto subscribed my name this 15th day of May, 2019.

ERNALYN M. ALONZO
HEARING REPORTER