

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:
A. KHAN

) OTA Case No. 18042861
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OPINION

Representing the Parties:

For Appellant: Michael Hallock
Tax Appeals Assistance Program (TAAP)¹

For Respondent: Brian C. Miller, Tax Counsel III
Sonia C. Woodruff, Tax Counsel IV

J. MARGOLIS, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19045, A. Khan (appellant) appeals an action by respondent Franchise Tax Board (FTB) proposing additional tax of \$3,131, a late-filing penalty of \$796.25, and applicable interest, for appellant’s 2013 tax year.

Office of Tax Appeals (OTA) Administrative Law Judges Jeffrey I. Margolis, Kenneth Gast, and John O. Johnson held a hearing for this matter on September 30, 2020.² At the conclusion of the hearing, the record was closed, and this matter was submitted for decision.

ISSUES

1. Whether appellant established that he was a nonresident of California from May 25, 2013, through the end of 2013.
2. Whether the late-filing penalty proposed under R&TC section 19131 should be abated or reduced.

¹ Appellant filed his own appeal letter and reply brief. Scott Dutra of TAAP filed appellant’s supplemental brief, and Michael Hallock of TAAP represented appellant in connection with the oral hearing in this matter.

² The oral hearing was noticed for Cerritos, California, but was conducted electronically due to COVID-19.

FACTUAL FINDINGS

1. Appellant is a United States citizen who was born in Pakistan in 1978 but raised in Saudi Arabia for the first seven years of his life. In 1985, he moved to the United States with his parents (who had lived in the United States for some time before appellant's birth and are United States citizens). Appellant's parents returned to Saudi Arabia in the early 2000s and spent another four years there.
2. Appellant received a medical degree from Western University College of Osteopathic Medicine of the Pacific in Pomona, California. In 2005, he became a licensed osteopathic physician and surgeon in California. He has maintained his California license to practice medicine continuously through the present date. His primary area of practice is in ophthalmology.
3. Appellant married his former spouse on May 30, 2003. They had three children together, born in 2004, 2005 and 2007.
4. Appellant and his former spouse entered into a one-year lease of a residence located in Chino, California, that was to commence on September 1, 2011, and terminate on August 31, 2012.
5. Shortly thereafter, on September 22, 2011, appellant and his former spouse separated.
6. In October 2012, appellant's former spouse initiated divorce proceedings against him in San Bernardino County Superior Court. That action was dismissed in December 2012 for lack of prosecution, but a new divorce action was filed by her in January 2013. Proceedings in that action continued for several years, until at least mid-2016. Eventually, their marriage was dissolved.
7. Appellant's 2012 California return was filed jointly with his former spouse. The address reflected on the return was the address of appellant's parents, in San Dimas, California.
8. Because he moved frequently, appellant would use his parents' San Dimas address for official correspondence and notices. For example, he owned a 2008 Toyota, whose certificate of title reflects his parents' address. In addition, on his 2013, 2014, and 2015 California tax returns, appellant used his parent's address as his mailing address.
9. In 2012, appellant—who is Muslim—decided to move overseas and live in a Muslim country for “spiritual reasons.” On May 25, 2013, appellant left California to live in Saudi Arabia. He had been planning for this move for almost a year prior to his

departure. Appellant's minor children remained in California with their mother, appellant's former spouse.

10. In connection with his move from California to Saudi Arabia, appellant:
 - a. ceased using a storage locker in California he had been renting and sold most of his belongings;
 - b. disposed of both his cars prior to his departure;
 - c. found suitable employment as a physician in Saudi Arabia that was to last for an indefinite period of time;
 - d. established residency in Saudi Arabia by obtaining a residency permit;
 - e. rented an apartment in Saudi Arabia under a two-year lease, for the period from July 1, 2013 until June 30, 2015;
 - f. bought a new car in Saudi Arabia on September 20, 2013;
 - g. obtained a Saudi driver's license that would be valid for 10 years;³
 - h. closed his California bank accounts prior to leaving California and opened bank accounts in Saudi Arabia after he moved there;
 - i. acquired a credit card in Saudi Arabia;
 - j. developed social connections and relationships overseas (some of which existed before his move to Saudi Arabia); and
 - k. moved to Medina, Saudi Arabia, a city that is one of the holiest cities in Islam.⁴
11. Commencing on or after June 1, 2013, appellant began working in Saudi Arabia as a physician. According to Form 2555, *Foreign Earned Income*, attached to appellant's originally filed 2013 federal and California tax returns, during 2013 he worked in Saudi Arabia as an ophthalmologist employed by the Hospitals and Centers of Marabi. A Certificate of Insurance dated February 24, 2013, issued by the Gulf General Cooperative Insurance Company in Jeddah, Saudi Arabia, provided coverage for appellant to practice as an ophthalmologist from June 11, 2013, through June 10, 2017.
12. After appellant moved to Saudi Arabia on May 25, 2013, he did not return to California for any reason during 2013.

³ Saudi driver's licenses were available for periods of one, three or 10 years. Appellant acquired a license that would be valid for 10 years, even though it cost more than licenses for shorter durations.

⁴ Appellant had visited Medina frequently (once every year or two) throughout his teenage and adult years.

13. Appellant had a California driver's license prior to his move to Saudi Arabia. He neither surrendered it in connection with his move to Saudi Arabia, nor did he renew it while in Saudi Arabia.
14. Appellant was registered to vote in California before he moved to Saudi Arabia. He did not cancel his voter registration; however, he did not vote in this state while he was in Saudi Arabia.
15. Appellant and his family have long-standing religious and social connections in Saudi Arabia.
16. While in Saudi Arabia, appellant was briefly engaged to be married to a woman there.⁵
17. During 2014 (the year after the year at issue in this appeal), appellant returned to California for 58 days. During his time in California in 2014, appellant made at least two court appearances in his divorce proceeding. He also performed some contract work as a physician while in California.
18. During 2014, appellant's parents stayed with him at his apartment in Saudi Arabia for three and a half months. Appellant's brother also visited him in Saudi Arabia in 2014.
19. In 2015, appellant left Saudi Arabia and returned to California, where he now resides.
20. Appellant filed his 2013 California income tax return late, on February 19, 2015. He filed a California individual income tax return, Form 540, which is supposed to be used for full-year residents of California. That form was completed and provided to him by his tax return preparer, an enrolled agent based in New York.
21. On appellant's 2013 California return, the enrolled agent deducted \$67,217 that appellant had earned from his work in Saudi Arabia pursuant to the foreign earned income exclusion permitted by federal law (Internal Revenue Code section 911).⁶ On that return, appellant's reported total California tax liability, after credits, was \$54.
22. Since California does not conform to the federal foreign earned income exclusion provision, appellant's return came under audit. FTB issued a Notice of Proposed Assessment (NPA) to appellant dated June 28, 2017, disallowing the exclusion and

⁵ During his time in Saudi Arabia, appellant met a Saudi woman who would later become his wife. The record is unclear as to whether this is the same woman he was "briefly engaged to" in Saudi Arabia.

⁶ Appellant included in his 2013 income, the California-source income he earned *prior to* his move to Saudi Arabia. After moving to Saudi Arabia, he earned no additional California-source income in 2013.

- determining a tax deficiency of \$3,131 and a late-filing penalty of \$796.25. Appellant filed a protest from the NPA.
23. After receiving the NPA, appellant filed an amended California return dated August 24, 2017, on the basis that he had ceased to be a California resident on May 25, 2013. On that amended return, appellant reported a California income tax liability after credits of \$934 and claimed to have made a \$500 estimated tax payment (transferred from his 2012 year), leaving a tax amount due of \$434. Because appellant's return was filed after the NPA had been issued to appellant for 2013, FTB declined to process the return.
 24. By letter dated November 13, 2017, FTB denied appellant's protest and informed him that it had determined he was a California resident for all of 2013 because he had not shown that he was absent from California for other than a temporary or transitory purpose.
 25. Appellant submitted a "Reasonable Cause – Individual and Fiduciary Claim for Refund" dated March 2, 2015, to FTB, claiming that he had reasonable cause for filing his 2013 return late, and that FTB had failed to credit him with \$500 of overpaid 2012 taxes that were designated as an estimated tax payment towards tax year 2013.
 26. On January 9, 2018, FTB issued a Notice of Action, affirming the NPA.
 27. Appellant filed this timely appeal from FTB's Notice of Action.

DISCUSSION

Issue 1: Whether appellant established that he was a nonresident of California from May 25, 2013, through the end of 2013.

A presumption of correctness attends the FTB's determination, and the burden of proof rests on the taxpayer to prove error. (*Appeal of Seltzer* (80-SBE-154) 1980 WL 5068). This principle applies in most tax cases, including those involving residency determinations. (See, e.g., *Appeal of Mazer*, 2020-OTA-263P⁷; *Appeals of Young* (86-SBE-199) 1986 WL 22876.)

California residents are taxed upon their entire taxable income (regardless of source), whereas nonresidents are only taxed on income from California sources. (R&TC, §§ 17041(a), (b), and (i), 17951.) Part-year residents are taxed on their entire taxable income earned while

⁷ Office of Tax Appeals (OTA) opinions are available on OTA's website, at <<https://ota.ca.gov/opinions>>.

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residents of this state, as well as all income derived from California sources while nonresidents. (R&TC, § 17041 (b) and (i).)

California defines a “resident” as including: (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. (R&TC, § 17014(a)(1)-(2); see also Cal. Code Regs., tit. 18, § 17014.) It is undisputed that appellant was a California domiciliary and resident prior to his move to Saudi Arabia on May 25, 2013. Furthermore, the law is clear that “[a] domicile once acquired is presumed to continue until it is shown to have been changed, and to constitute the new domicile two things are indispensable: First, residence in the new locality; and second, the intention to remain there.” (*Noble v. Franchise Tax Bd.* (2004) 118 Cal.App.4th 560, 568 (*Noble*), internal quotations and citations omitted.) Appellant contends that he ceased being a California domiciliary and resident when he moved to Saudi Arabia in May 2013 with the intention of remaining there indefinitely.⁸

The California courts and FTB’s regulations have defined “domicile” as the location where a person has the most settled and permanent connection, and the place to which a person intends to return when absent. (*Whittell v. Franchise Tax Bd.* (1964) 231 Cal.App.2d 278, 284 (*Whittell*); Cal. Code Regs., tit. 18, § 17014(c).) An individual who was domiciled in California and then leaves retains his or her California domicile as long as there is a *definite intention* of returning to California. (Cal. Code Regs., tit. 18, § 17014(c).) To change domicile, a taxpayer must actually move to another taxing jurisdiction and intend to remain there permanently or indefinitely.⁹ (*Noble, supra*, 118 Cal.App.4th at p. 568.)

⁸ In its opening brief, FTB acknowledged that appellant “contend[s] he had no intention of returning to California when he left in May 2013.” Yet FTB inconsistently claimed that appellant “does not dispute that he maintained California domicile during all of 2013.” Our review of appellant’s briefs reveals that appellant clearly indicated his position was that when he left California for Saudi Arabia in 2013, he became a Saudi resident and intended to remain there indefinitely. A change of residence, coupled with an intention to remain in the new place of residence indefinitely, constitutes a change of *domicile*. (Cal. Code Regs., tit. 18, § 17014(c); *Noble, supra*, 118 Cal.App.4th at p. 568.) Thus, appellant did not concede that he remained a California domiciliary throughout 2013. But even if appellant had remained a California domiciliary, if his move to Saudi Arabia was for other than a “temporary or transitory purpose,” he still would not be a resident of California for tax purposes while he lived in Saudi Arabia. (R&TC, § 17014(a)(1)-(2).)

⁹ Although it has been said that “it is the ‘intent’ of the person that determines domicile” (*Appeal of Harrison* (85-SBE-059) 1985 WL 15838), “it is well settled that this intention is not to be determined merely from unsubstantiated statements, but rather the ‘acts and declarations of the party must be taken into consideration.’ ” (*Ibid.*, quoting from *Estate of Phillips* (1969) 269 Cal.App.2d 656, 659.)

FTB contends that, despite appellant's move to Saudi Arabia on May 25, 2013, appellant remained a California "resident" within the meaning of R&TC section 17014(a)(2) because: (i) he continued to be a California domiciliary; and (ii) his move to Saudi Arabia was for a "temporary and transitory purpose." We disagree.

The evidence shows that appellant abandoned his California domicile on May 25, 2013, when he established a new domicile in Saudi Arabia, as he moved there with the intention of staying indefinitely, not for a temporary or transitory purpose. The testimony of appellant and the other witnesses (appellant's wife, brother-in-law, and Saudi Arabian work colleague) was credible and consistent in this regard. Their testimony is well supported by the objective facts showing that: appellant's marriage to his former spouse, a California resident, was irreparably broken before his departure from California on May 25, 2013; appellant had separated approximately 20 months earlier from his former spouse, who had filed for divorce approximately six months prior to his departure; appellant sold his property in California (leaving nothing in storage); and appellant started a new life for himself in Saudi Arabia. Appellant rented a large apartment in Saudi Arabia under a two-year lease, joined a mosque, obtained suitable employment there as a physician, became involved in professional and religious organizations, purchased a vehicle, obtained a Saudi driver's license (valid for 10 years), and became engaged to a Saudi woman.

Against these uncontroverted facts, FTB's assertions are unconvincing. FTB notes that appellant did not affirmatively act to cancel his California voter registration, driver's license, or license to practice medicine. But during the period appellant resided in Saudi Arabia, he did not vote in California, and neither his California driver's license nor his California license to practice medicine came up for renewal.¹⁰ FTB claims that appellant "benefitted from and was protected by California law" because he "maintain[ed] -- and exercise[ed] -- his privilege to practice medicine in this state." While it is true that appellant passively maintained his license in California, he did not, in fact, practice medicine in California after he left the state on May 25, 2013, and continuing through the end of the tax year at issue.¹¹

¹⁰ Even if appellant had renewed his license to practice medicine in California during the relevant period, this would not necessarily be inconsistent with his intention to remain indefinitely in Saudi Arabia.

¹¹ Appellant did return to California in the latter part of 2014 and stayed for 58 days. While here, appellant visited with his children, participated in his marital dissolution proceedings, and earned some extra income working

FTB notes that appellant continued to use his parents' mailing address in California to receive some of his correspondence. While this is a factor to be considered, it is not determinative. (See generally *Appeal of Bragg* (2003-SBE-002) 2003 WL 21403264); *Appeal of Mazer, supra.*) In the circumstances before us, appellant's use of his parents' United States mailing address does not show an intention to return to California; it simply reflects the difficulty of having mail forwarded on a timely basis to his new domicile in Saudi Arabia.

FTB's principal contention, however, is that appellant remained a California domiciliary because his children continued to reside in California with their mother, appellant's former spouse. Appellant, however, had no choice but to leave his children in the custody of their mother; the mother had commenced a dissolution action against appellant, and she would not allow the children to go to Saudi Arabia with him. FTB relies upon *Appeal of Bailey* (76-SBE-16) 1976 WL 4032 (*Bailey*) for the proposition that the fact that appellant's immediate family members (i.e., his children and former spouse) remained in this state proves that he remained a California domiciliary despite his move to Saudi Arabia. However, *Bailey* is readily distinguishable; it does not support FTB's position. In *Bailey*, the taxpayer (Annette Bailey), her husband (John Bailey), and their child had been domiciled together in California until 1965. That year, John Bailey moved to British Columbia, where he leased an apartment and started a business, while Annette Bailey and the child remained in California. However, in *Bailey*, — unlike the situation in the appeal before us—*the marriage was not fractured*. The couple remained married to each other. Furthermore, the State Board of Equalization found that, despite Mr. Bailey's residence in British Columbia, it was "clear that Mr. Bailey considered the parties' California abode as the marital abode. His wife and child remained here, and he visited here whenever business circumstances allowed. The record also indicates that he intended to return to

temporarily on a contract basis. But as FTB notes in its briefing: "This appeal, however, is about Appellant's California residency during 2013, not 2014."

California whenever his business association in Canada should terminate”¹² (*Bailey, supra*, 1976 WL 4032 at p. *2.) There is no comparable evidence in the record before us.¹³

Accordingly, we conclude that appellant ceased being a California domiciliary, and was not a “resident” of California within the meaning of R&TC section 17014(a) after he moved to Saudi Arabia on May 25, 2013.

Issue 2: Whether the late-filing penalty proposed under R&TC section 19131 should be abated or reduced.

R&TC section 19131 provides that FTB shall impose a late-filing penalty when a taxpayer fails to file a return on or before its due date or extended due date, unless it is shown that the late filing is due to reasonable cause and not due to willful neglect. The penalty is computed at five percent of the amount of tax required to be shown on the return for every month that the return is late, up to a maximum of 25 percent. (R&TC, § 19131(a).) At the hearing, appellant’s representative indicated that appellant was no longer disputing the imposition of the late-filing penalty, but that the penalty should be abated or reduced in the event that the tax assessment proposed against appellant is abated or reduced. We agree that the penalty applies to the appellant’s 2013 tax liability, as revised herein.

HOLDINGS

1. Appellant was a nonresident of California from May 25, 2013, through the end of 2013.
2. Appellant has not established that his untimely filed return for the 2013 tax year was due to reasonable cause and not due to willful neglect.

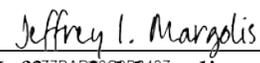
¹² Although *Bailey* only involved Annette Bailey’s tax liability, the opinion indicates that FTB had concluded that John Bailey was *not* a California resident for California tax purposes. His California tax liability arose solely from his community property share of his wife’s earnings, which constituted California-source income.

¹³ Citing *Appeal of Bragg, supra*, FTB claims that the location of the taxpayer’s family is a “strong indication” of the taxpayer’s domicile. But in *Bragg* the taxpayer’s family lived *with* the taxpayer during the year at issue. That is not the case here.

FTB also claims that appellant “benefitted from the protections of California law,” because his former wife had commenced divorce proceedings against him in a California court and those proceedings continued through the period he resided in Saudi Arabia. However, FTB provides no authority for its position that appellant’s participation in a lawsuit he did not institute supports a finding of residency in the state the lawsuit was filed, or that it otherwise somehow undermines his claim of having become a resident and domiciliary of Saudi Arabia in May 2013.

DISPOSITION

FTB’s proposed tax deficiency and penalty computation shall be recomputed on the basis that appellant ceased to be a California resident on May 25, 2013, and that he continued to be a nonresident of California throughout the remainder of the 2013 tax year.

DocuSigned by:

Jeffrey I. Margolis
Administrative Law Judge

We concur:

DocuSigned by:

Kenneth J. Gast
Administrative Law Judge

DocuSigned by:

John O. Johnson
Administrative Law Judge

Date Issued: 12/21/2020